



ESSENTIAL TERMS FOR SBA LOANS



EXPERTISE IN SBA FINANCING

TMC Financing is committed to help guide you through every step of the SBA loan process. We created this glossary for your reference during the loan application process and even after your loan has been approved and funded. Our role as your advocate starts with obtaining your loan approval and continues for the 20 year life of the loan.

Since 1981, TMC has provided over \$6.4 billion in financing for more than 3,900 businesses. Our industry leading experience and expertise allows us to offer unparalleled service to our clients and partners in facilitating SBA financing.

Start with TMC. We are dedicated to your success.

AFFILIATES

Definition: *Business concerns, organizations, or individuals that control each other or that are controlled by a third party. Control may include shared management or ownership; common use of facilities, equipment, and employees; or family interest. The calculation of a firm's size includes the employees or receipts of all affiliates. Affiliation with another business concern is based on the power to control, whether exercised or not. Such factors as common ownership, common management and identity of interest (often found in members of the same family), among others, are indicators of affiliation. Power to control exists when a party or parties have 50 percent or more ownership. It may also exist with considerably less than 50 percent ownership by contractual arrangement or when one or more parties own a large share compared to other parties. The affiliated business concerns need not be in the same line of business.*

SBA regulations require affiliates to be considered when calculating the size of the applicant business.

AMORTIZATION

Definition: *Gradual reduction of term debt by periodic payment sufficient to pay current interest and to eliminate the principal at maturity.*

SBA 504 loans are fully amortized over 20-year (the majority of projects) or 10-year terms.

APPRAISAL

Definition: *A professional opinion of the market value of a property, such as a home, business, or other asset, whose market price is not easily determined.*

An appraisal of the subject property is required to obtain an SBA 504 loan.

APPRAISED VALUE

Definition: *The value placed on an item, product or business by an appraiser, recognized for experience in a particular field.*

SBA 504 loans finance up to 90% of the appraised value for the subject property.

ASSUMPTION

Definition: *The act of assuming/undertaking another's debts or obligations.*

SBA 504 loans are fully assumable by a qualified buyer.

BALLOON PAYMENT

Definition: *An oversized payment due at the end of a mortgage, commercial loan or other amortized loan. Because the entire loan amount is not amortized over the life of the loan, the remaining balance is due as a final repayment to the lender.*

Balloon payments are often prepackaged into what are called “two-step mortgages.” In this type of mortgage, the balloon payment is rolled into a new or continuing amortized mortgage at the prevailing market rates.

Balloon payments can occur within a fixed-rate or adjustable-rate mortgage.

A balloon payment may be included in the terms of the first mortgage loan.

CENTRAL SERVICING AGENT (CSA)

Definition: *An entity that receives and disburses funds to the various parties involved in 504 financing under a master servicing agent agreement with SBA.*

The CSA for SBA 504 loans is Colson Services Corporation.

CERTIFIED DEVELOPMENT COMPANY (CDC)

Definition: A Certified Development Company is a nonprofit corporation set up to contribute to the economic development of its community. The 504 CDC Program provides growing businesses with long-term, fixed-rate financing for major fixed assets, such as land and buildings. CDCs work with the SBA and private-sector lenders to provide financing to small businesses. There are about 270 CDCs nationwide. Each CDC covers a specific geographic area.

TMC Financing is a CDC serving California and Southern Nevada.

CLOSE OF ESCROW

Definition: The date upon which real estate documents are recorded and title passes from Seller to Buyer. On this date the Buyer becomes the legal owner.

TMC's experienced Closing team works with the first mortgage lender, borrower, brokers and escrow agent to ensure that the close of escrow deadline is met.

CLOSING

Definition: Actions and procedures associated with the documentation and disbursement of loan funds after the application has been approved and all required documents are filed and recorded.

TMC's experienced Closing team guides the borrower through the closing process after the SBA loan has been approved.

COLLATERAL

Definition: *Something of value—securities, evidence of deposit or other property—pledged to support the repayment of an obligation.*

With an SBA 504 loan, the subject property being financed is used as collateral. In most cases, no additional collateral is required.

CONVENTIONAL LOAN

Definition: *A lender agreement that is not guaranteed or insured by the federal government.*

An SBA real estate loan is an alternative to a conventional loan. SBA 504 loans offer below-market interest rates and long-term, fixed-rate financing.

DEBENTURE

Definition: *Debt instrument evidencing the holder's right to receive interest and principal installments from the named obligor. Applies to all forms of unsecured, long-term debt evidenced by a certificate of debt.*

The SBA 504 second mortgage is commonly referred to as a debenture.

DEED OF TRUST

Definition: A document under seal which, when delivered, transfers a present interest in property. May be held as collateral.

Upon funding an SBA 504 loan, the first mortgage lender holds a First Deed of Trust and the SBA holds a Second Deed of Trust on the subject property being purchased.

DISBURSEMENT

Definition: The actual payout to borrower of loan funds, in whole or part.

The initial disbursement of loan funds is made by the permanent and interim lenders. The SBA loan funds are disbursed by the CSA to pay off the principal balance of the interim loan.

DOWN PAYMENT

Definition: The part of the purchase price paid in cash up front, reducing the amount of the loan or mortgage.

SBA 504 loans typically require as little as a 10% down payment. The down payment is also referred to as the Borrower Contribution or Injection.

EFFECTIVE RATE

Definition: Actual rate as opposed to announced, estimated, offered, planned, or promised rate.

SBA 504 effective loan rates are calculated once per month at the time of the debenture funding.

ELIGIBLE PASSIVE COMPANY (EPC)

Definition: An entity or trust which does not engage in regular and continuous business activity, which leases real or personal property to an operating company for use in the operating company's collateral.

The SBA allows an EPC to take title to the property in any legal form or ownership structure. The EPC must lease the entire subject property directly to the operating company (OC).

ENTREPRENEUR

Definition: One who assumes the financial risk of the initiation, operation and management of a given business or undertaking.

TMC Financing provides SBA lending to successful entrepreneurs to strengthen and grow their new or existing small businesses.

ENVIRONMENTAL REPORT

Definition: An evaluation of a site, prior to acquisition of title to the property, to determine the existence of hazardous waste.

TMC coordinates with the first mortgage lender to advise the borrower on the type of environmental report required for the project.

ESCROW

Definition: Documents, real estate, money, or securities deposited with a neutral third party (the escrow company) to be delivered upon fulfillment of certain conditions, as established in a written agreement.

It is TMC's goal to do everything possible to expedite the closing process of each transaction and meet the agreed upon deadlines to close escrow.

ESCROW COMPANY

Definition: A neutral third party that holds documents and money for a real estate sale transaction and ensures that all conditions of the sale are met before any disbursement of funds or articles.

TMC's Closing department works closely with the escrow company to make sure that documents are signed and recorded in a timely manner. When funds are wired by the CSA to the escrow company, TMC follows up to make sure funds are applied correctly to pay the principal balance of the interim loan.

FINANCING CONTINGENCY

Definition: Clause in a purchase agreement that protects a prospective buyer from legal action should financing for the purchase consideration fall through. Also may refer to whether a buyer's ability to finance a transaction is subject to certain conditions.

TMC coordinates with all parties in the SBA loan process to manage important dates associated with the real estate purchase, including the financing contingency.

FIRST MORTGAGE LENDER

Definition: *The lender involved in a real estate loan that has the right to payment in full before payments to other lenders are made. Also known as “Third Party Lender” and “Senior Lien Holder”.*

TMC coordinates the SBA portion of an SBA 504 loan — a partnership between a first mortgage lender and the SBA — and works with the borrower’s bank of account or with any bank or nonbank lender that participates in the SBA 504 loan program.

FUNDING

Definition: *The commercial activity of providing financing and capital.*

An SBA 504 loan has many funding sources: The borrower contributes personal or business funds, the first mortgage lender funds a portion of the purchase price, and the interim lender funds the remaining portion necessary to bridge the period until the SBA loan funds.

GREEN ENERGY GOALS

Definition: *Part of SBA’s public policy program which recognizes businesses that create renewable energy resources or reduce their own energy consumption by 10% or more as being eligible for increased SBA financing.*

TMC reviews each transaction for eligibility for increased SBA funding for businesses which meet green energy goals.

GUARANTEE, UNCONDITIONAL

Definition: *Guarantor unconditionally guarantees payment to Lender of all amounts owing under the Note. This Guarantee remains in effect until the Note is paid in full. Guarantor must pay all amounts due under the Note when Lender makes written demand upon Guarantor. Lender is not required to seek payment from any other source before demanding payment from Guarantor.*

Based on the loan structure, guarantees of individual owners and companies may be required for SBA financing.

HAZARD INSURANCE

Definition: *Insurance required showing the lender as loss payee covering certain risks on real and personal property used for securing loans.*

SBA, like all secured lenders, requires hazard insurance coverage of collateral.

INTEREST RATE

Definition: *The rate that is charged or paid for the use of money; often expressed as an annual percentage of the principal.*

The below market interest rate on SBA 504 loans is fixed for the term of the loan.

INTERIM LOAN

Definition: A short-term, temporary loan used until permanent financing is available. In a 504 transaction, there is a permanent loan and an interim loan. When the debenture funds, the SBA loan pays off the principal amount of the interim loan. Also referred to as a bridge loan.

In most cases, the first mortgage lender is also the interim lender. At close of escrow, the interim lender records a second Deed of Trust. Upon funding of the SBA loan, the interim loan is repaid, and the SBA assumes its permanent second Deed of Trust position.

LEASE

Definition: A contract between the owner (lessor) and the tenant (lessee) stating the conditions under which the tenant may occupy or use real estate or equipment. Terms usually include a specific period of time and a predetermined rate.

SBA requires that a lease be executed between the eligible passive company (EPC) as “lessor” and the operating company (OC) as “lessee”.

LESSEE

Definition: The user of equipment or property being leased.

In an SBA loan, the Operating Company (OC) is the lessee.

LESSOR

Definition: *The party to a lease agreement who has legal or tax title to equipment or property, who grants the lessee the right to use the equipment or property for the lease term, and who is entitled to the rental fees.*

In an SBA loan, the Eligible Passive Company (EPC) is the lessor.

LETTER OF INTENT (LOI)

Definition: *Written communication issued by a lender in response to a request for funding a project; neither confirming a loan nor providing final terms under which the loan may be extended, an LOI simply states that the lender would consider that type of financing.*

Sometimes referred to as Letter of Interest. With an SBA 504 loan, the first mortgage lender may issue an LOI.

LIEN

Definition: *A charge upon or security interest in real or personal property maintained to ensure the satisfaction of a debt or duty ordinarily arising by operation of law.*

The SBA Deed of Trust is a second lien on the subject property.

MATURITY

Definition: *The date on which a loan becomes due.*

SBA 504 loans have 20-year (the majority of projects) or 10-year maturity dates.

MORTGAGE

Definition: *An instrument giving legal title to secure the repayment of a loan made by the mortgagee (lender). In legal contemplation there are two types: (1) title theory—operates as a transfer of the legal title of the property to the mortgagee, and (2) lien theory—creates a lien upon the property in favor of the mortgagee.*

SBA 504 loans are structured with two mortgages — a first mortgage from the first mortgage lender, and a second mortgage from the SBA.

NOTE

Definition: *A unilateral agreement containing an express and absolute promise of the signer to pay to a named person, or order, or bearer, a definite sum of money at a specified date or on demand. Usually provides for interest and, concerning real property, is secured by a mortgage or trust deed.*

The SBA note is signed by the borrower at funding.

OPERATING COMPANY (OC)

Definition: A business actively involved in conducting business operations now, or about to be located on, real property owned by an eligible passive company (EPC).

In SBA financing, operating company refers to the business (or businesses) applying for an SBA loan that will occupy the subject property.

OWNER OCCUPIED

Definition: A property that is actively occupied by the current owner.

SBA occupancy requirements are at least 51% of an existing building and 60% of a newly constructed building.

POINTS (Loan Points/Basis Points)

Definition: Finance charges paid by the borrower at the beginning of a loan. One point is 1% of the loan amount.

The CDC processing fee is equal to one-and-one half percent (1.5%) of the net debenture amount.

PRELIMINARY TITLE REPORT

Definition: A written report issued by a title company, preliminary to issuing title insurance, which shows the recorded condition of title of the property in question.

All parties to a real estate transaction rely on a preliminary title report for the legal description, current ownership, Assessor's Parcel Number(s), as well as all encumbrances upon the property.

PREPAYMENT

Definition: Prepayment is possible with SBA 504 loans following the program guidelines. Partial prepayment is not allowed and a prepayment premium applies to all SBA 504 loans for the first half of the Note term.

SBA 504 loans have a declining prepayment premium during the first half of the stated term.

PREPAYMENT PREMIUM

Definition: A prepayment premium is money a lender charges a borrower for repaying a debt early.

SBA 504 loans have a declining prepayment premium during the first half of the stated term. The amount of the prepayment premium adjusts at six month intervals.

PREQUALIFY

Definition: *The process of determining how much a prospective real estate buyer might be eligible to borrow before applying for a loan; not a guarantee of approval.*

TMC offers free prequalification for potential borrowers upon receiving complete financial information.

PRIME RATE

Definition: *Interest rate which is charged to business borrowers having the highest credit ratings, for short term borrowing. As published daily in the Wall Street Journal, it is the basis for rates to other lenders.*

Some of the first mortgage lenders who participate in the 504 program base their interest rate on the Prime Rate.

RECONVEYANCE

Definition: *The transferring of a title back to its previous owner. Most commonly used upon payment in full of a Trust Deed. Also called a Deed of Reconveyance or release.*

TMC follows up with the title companies and interim lenders to obtain evidence that the interim lender has prepared and recorded a Deed of Reconveyance in a timely manner.

RECORDING

Definition: *The act of entering in a book of public records instruments affecting the title to real property. Recording in this manner gives notice to the world of facts recorded.*

At close of escrow the following documents are recorded: Deed of Trust, Assignment of Deed of Trust, Memorandum of Lease, and Requests for Notice of Default.

REFINANCE

Definition: *An existing mortgage loan is paid off with a new mortgage loan for the same borrower on the same property. A common reason for refinancing a property is to secure a lower interest rate.*

For the first time ever, business owners can refinance existing commercial real estate debt with below-market, FIXED rate, SBA 504 loans. The SBA 504 refinance program is only available for a limited time.

SBA 504 LOAN

Definition: *An SBA lending program, with financing guaranteed for real estate and equipment purchases, designed for start-up and existing small businesses. Typically, a 504 project includes a loan secured with a senior lien from a private-sector lender covering up to 50 percent of the project cost, a loan secured with a junior lien from the Certified Development Company (CDC) (backed by a 100 percent SBA-guaranteed debenture) covering up to 40 percent of the cost, and a contribution of at least 10 percent equity from the small business being helped.*

TMC advocates in favor of business owners to obtain SBA 504 financing for owner-occupied commercial real estate.

SBA 7A LOAN

Definition: *The SBA's general business lending program, with financing guaranteed for a variety of general business purposes, designed for start-up and existing small businesses; delivered through commercial lending institutions. Loan proceeds can be used for working capital, machinery and equipment, furniture and fixtures, land and building (including purchase, renovation and new construction), leasehold improvements, and debt refinancing (under special conditions).*

TMC advocates in favor of business owners to obtain SBA 7a financing for owner-occupied commercial real estate.

SERVICING

Definition: *The administrative aspect of a loan from the time the loan is funded. Servicing functions include the collection of timely loan payments, review of financial statements, verification that appropriate insurance is maintained and that real property taxes are paid in a timely manner.*

TMC's experienced Servicing team works with the borrower for the life of the loan.

SMALL BUSINESS ADMINISTRATION (SBA)

Definition: *An independent agency of the federal government, not to be confused with Small Business Association or variations thereof. The U. S. Small Business Administration (SBA) was created by Congress in 1953 to help America's entrepreneurs form successful small enterprises. Today, SBA's district offices in every state offer financing, training and advocacy for small firms. These programs are delivered by SBA offices in every state, the District of Columbia, the Virgin Islands and Puerto Rico. In addition, the SBA works with thousands of lending, educational and training institutions nationwide.*

As an SBA-Certified Development Company, TMC is able to provide SBA real estate financing.

TENANT IMPROVEMENTS

Definition: *Changes made to commercial or industrial property by its owner to accommodate a tenant's specific needs, such as floor and wall coverings, ceilings, partitions, air conditioning, fire protection, and security.*

An SBA 504 loan may be used to finance tenant improvements to the building being purchased.

TERM

Definition: *Fixed period for which a loan, insurance policy, or bond is issued.*

The SBA 504 loan program offers 10-year (typically for equipment) and 20-year terms.

THIRD PARTY LENDER

Definition: *The lender involved in a real estate loan that has the right to payment in full before payments to other lenders are made. Also known as “First Mortgage Lender” and “Senior Lien Holder”.*

TMC coordinates the SBA portion of an SBA 504 loan — a partnership between a third party lender and the SBA — and works with the borrower’s bank of account or with any bank or nonbank lender that participates in the SBA 504 loan program.

TITLE

Definition: *(1) A combination of all the elements that constitute a legal right to own, possess, use, control, enjoy and dispose of real estate or a right or interest therein. (2) The rights of ownership recognized and protected by the law.*

The SBA allows borrowers the flexibility to take title to the real estate in any form. For example, a borrower could take title as an individual, LLC, corporation, or trustee of a trust.

TITLE COMPANY

Definition: *A company involved in examining and insuring title claims, usually for real estate, on behalf of its customers.*

TMC’s experienced Closing team coordinates with the escrow and title company to make sure that SBA loan documents are correct and timely, and responds to questions about the closing process.

DEFINITION SOURCES:

TMC is providing access to the definitions included in this glossary for informational purposes only. TMC cannot guarantee the accuracy of this information.

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NOTES:



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