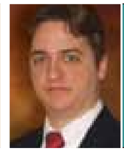

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SBA Taps the Self-Storage Market

Financing self-storage properties got a little easier with Small Business Administration loans

BY NOW, MOST COMMERCIAL MORGAGE brokers probably know that self-storage facilities are eligible for some U.S. Small Business Administration (SBA) loan programs. This change was made in September 2010 as a result of provisions in the Small Business Jobs Act of 2010, and many lenders started marketing their SBA products to self-storage owners earlier this year.

Although several of these loans have already closed, the volume hasn't been nearly as much as would be expected given SBA loan products' benefits. The likely reason that more loans haven't been made is the large amount of misinformation regarding the available programs and how borrowers can qualify for them.

There are two main SBA programs available to self-storage property owners and investors — the 504 loan and the 7(a) loan. Each of these programs has strengths and weaknesses, and brokers should advise their borrowers to consider both before moving forward with their refinance or purchase.

The SBA 504 loan

This is the lesser-known, but often the more beneficial, of the two SBA programs available to self-storage property owners and investors. With the SBA 504 program, capital comes from three sources:

1. **A first mortgage** is provided by the bank or lending institution. This typically makes up 50 percent of the total financing.
2. **A second mortgage**, referred to as a debenture, is provided by a certified development company (CDC). CDCs are nonprofit companies that aid in the economic development of specific communities. The CDC provides an additional 40 percent of the financing. For most businesses, this portion of the financing is limited to $5 million. The CDC debenture is typically fixed and fully amortizing for a 20- to 25-year term.
3. **The borrower provides** the remaining 10 percent.

The first mortgage can have a fixed or floating rate. Recently, some lenders have started offering first mortgages with maturities and amortization schedules that match those of the CDC debenture. This means that borrowers can sometimes get 25-year fully amortizing loans with fixed rates at 90 percent loan to value (LTV). These loans can be used for property acquisition, construction or refinancing.

The SBA 7(a) loan

The 7(a) program is more widely available than the 504 loan program and is a great option for self-storage property owners in many situations.

Financing provided through the 7(a) program consists of a single first mortgage provided by a bank or lending institution. The SBA then guarantees as much as 75 percent of the loan amount. The maximum amount of the guarantee is limited to 75 percent of $5 million in most cases.

Lenders are offering this product with LTVs of as much as 90 percent, but in practice, 80 percent seems to be the norm for most projects. SBA 7(a) loans can be either fixed of floating, but most lenders currently are only offering floating-rate products.

Qualifying for SBA financing

To qualify as a small business, borrowers must have a net worth of less than $15 million and must earn an average net income of less than $5 million annually. Also, they must have less cash on hand than the amount they are borrowing.

In addition to these two criteria, each lender has its own underwriting standards; not all SBA lenders are the same. It's possible for your client to be rejected by one SBA lender only to find that another SBA lender will happily finance the project.

In addition to the general criteria above, there are additional requirements to consider when using the 504 loan program. To lend the debenture portion, the CDC must show that the self-storage project meets one of the SBA's public-policy goals.

Some of these goals are:

- **Promoting women-, minority- or veteran-owned businesses:** This is one of the easiest policy goals to meet. If a company is 51 percent owned by a woman, minority or veteran, the CDC has met its policy-goal requirement.
- **Revitalizing economic-development areas:** A project may qualify under this policy goal if it is a substantial repositioning of a property. Of course, that assumes that your client's property is within an economic development area.
- **Reducing energy consumption:** Investors who plan to rehab an existing facility can qualify using this policy goal. Often,

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adding light-emitting diode lights and solar panels may be all that is necessary.

- **Rural development:** This goal is one of the most obvious for properties located in rural areas.

In addition to the goals listed above, a self-storage property also may qualify by creating new jobs. The job-creation requirement often is cited by lenders and borrowers as a reason that the 504 program will not work. This is because most self-storage properties don't employ a large number of people.

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There is a lot involved in qualifying and closing loans using the SBA's 7(a) or 504 loan programs, so it's important to work with a lender that understands the self-storage industry and the SBA process in general.

Remember, each SBA lender and each CDC is different. Knowing which lenders will lend on self-storage properties, as well as which are efficient at closing SBA loans, can mean the difference between a six-week and a 26-week loan-closing process.