

A vibrant green background filled with various white line-art icons related to business and finance, such as gears, a calculator, a laptop, a globe, a handshake, a money bag, a document, and a scale of justice. The title 'How an SBA 504 Loan Works' is centered in a large, white, bold, sans-serif font.

# How an SBA 504 Loan Works

Exploring options for commercial real estate loans? If you're a small business owner, the SBA 504 loan provides low-cost, fixed rate financing with unbeatable leverage. However, 504 loans don't have a sterling reputation – many borrowers think the application process is confusing, difficult, and takes too long to close.

This guide is here to debunk those misconceptions and details everything you need to know about SBA 504 loans. We'll explain all the ins-and-outs to eliminate surprises and showcase our streamlined process for a 45-day close.

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## Defining an SBA 504 Loan

An SBA 504 loan is a commercial real estate (CRE) loan backed by the U.S. Small Business Administration (SBA). This financing option is exclusively available to small businesses who own and occupy real estate for their business – known as owner-occupied commercial real estate (OOCRE).

Because these loans are guaranteed by the government, they're less risky to lenders. Lenders, in conjunction with the SBA, can then finance these loans at a higher leverage point and a lower, fixed interest rate. Plus, SBA 504 loans offer 25-year repayment terms, which allows you to spread your financing over a longer period and bring your monthly payments down further.

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## How to Use an SBA 504 Loan

504 loans are primarily used for commercial real estate. Use cases fall into the following four categories.



### ACQUISITION

Purchasing an existing property, land, or long-term machinery and equipment



### REFINANCING

Refinancing an existing mortgage to take advantage of lower interest rates and/or longer repayment timelines



### NEW CONSTRUCTION

Building a new commercial structure from the ground up or expanding an existing property



### RENOVATION AND IMPROVEMENT

Improvement or modernization of existing buildings, streets, utilities, parking lots, and landscaping

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## Leverage

Because SBA 504 loans are backed by a government agency, they offer the highest leverage available on commercial mortgages: up to 90%.

Leverage is another way to say **loan-to-value** (LTV). If you're getting 90% LTV on your SBA 504 loan, that means your loan comprises 90% of the appraised property value and you only need to provide a 10% down payment to close.

The leverage available for a 504 loan depends on the property type and whether you're starting a new business or expanding an existing one.

All SBA 504 loans start with a leverage point of 90%. However, the SBA considers two aspects of your loan package when determining LTV:

- › Property type
- › Years of business operation

If you're financing a **multi-purpose property** – such as an office, retail space, warehouse, or anything else that could be used for many different types of businesses – and your business has been in operation for at least two years, you're eligible for 90% LTV.

## LTV Examples

An accountant with a three-year operating history wants to purchase a \$1 million office building.

80% Starting leverage

+ 5% (Established business)

+ 5% (Multi-purpose acquisition)

= 90% LTV / \$900,000 Loan

+ \$100,000 Borrower down payment

A hotel owner with a two-year operating history wants to purchase a \$1 million hotel property.

80% Starting leverage

+ 5% (Established business)

+ 0% (Multi-purpose acquisition)

= 85% LTV / \$850,000 Loan

+ \$150,000 Borrower down payment

A prospective self-storage operator wants to break into the business and purchase a \$1 million self-storage facility.

80% Starting leverage

+ 5% (Established business)

+ 0% (Multi-purpose acquisition)

= 85% LTV / \$850,000 Loan

+ \$150,000 Borrower down payment

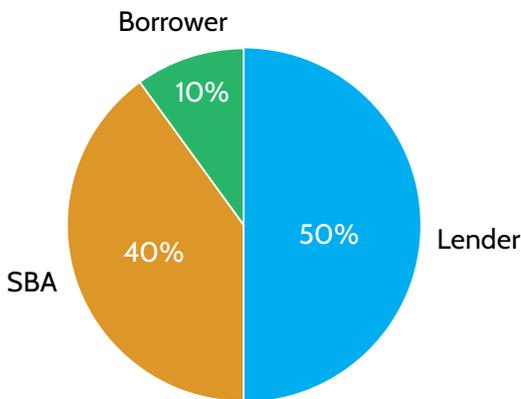
On the flip side, if you're financing **a special-purpose property** – properties with limited uses such as healthcare facilities, hotels, or self-storage – 5% will be subtracted from your leverage point. If you recently established your business, 5% will be subtracted for that factor too.

However, regardless of your property type or business history, your LTV will fall between 80-90%.

### Key Benefits of an SBA 504 Loan

High leverage + Fixed interest rate + Long repayment term  
= Low-cost financing

## How an SBA 504 Loan Works



As the borrower, you're responsible for at least 10% in the form of a down payment. As explained above in the Leverage section, you may be responsible for up to 20% down, but 10% is most common.

A lender of your choice finances 50% of the loan – you can apply for an SBA 504 loan through your bank or credit union, but it's better to apply with an SBA lending expert like Liberty SBF.

The SBA finances the remaining 40% of the loan. As you can see, this technically breaks down into **two different loans** – one financed by the lender, and one financed by the SBA.

However, the SBA doesn't have access to immediate capital to fund your second loan. They hold monthly **debenture sales** (which are government-secured bonds) to raise these funds. Because of the sales cycle, this process typically takes 45-60 days.

Instead of waiting for the SBA to fund your second loan, you'll initially receive both your first and your second loan **from your lender**. This results in an **interim period**, where you're making payments only to your lender while you wait for SBA takeout. Approximately 45-60 days later, the SBA will take out your second loan and set a fixed interest rate for your repayment term.

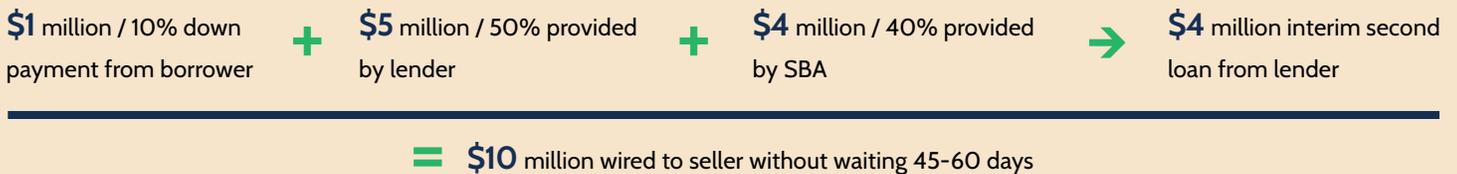
## Example SBA 504 real estate acquisition

Imagine your business is using an SBA 504 loan to purchase a new building. You complete the loan application process, get approved, and you're ready to close on your \$10 million property acquisition.

Your lender will provide 50% (\$5 million) of the purchase amount on closing, and your down payment will cover 10% (another \$1 million), but the remaining 40% from the SBA won't show up for at least another 45-60 days.

To close on your transaction, you need to wire the entire \$10 million to the seller all at once. Therefore, your lender will provide an **interim second loan** for the remaining \$4 million at the time of closing.

This second loan will be refinanced by the SBA a month or two later when the SBA debenture funding comes through, and the SBA will then become the lender on the second loan.



## The Interim Period

Let's go into more detail on the period between your lender closing your two loans and SBA takeout of your second loan. The interim period exists because:

- › The SBA only funds approved loans once per month.
- › Approved loans must meet all conditions for funding at least 3 weeks prior to the fund date

During this holding period, your loan will have an **interim interest rate** of approximately 7%. Don't let this scare you – this rate only applies for the interim period (45-60 days) and your payments will be interest-only. Plus, these payments can be financed into the whole deal, resulting in very little or zero cash out of pocket during the interim period.

When the SBA takes out your loan, your rate lowers to match the latest [SBA 504 debenture](#) rate (determined each month during the debenture sale) and becomes fixed for the term of your loan.

## Fees

Many borrowers have the impression that SBA 504 loans come with lots of fees. However, most of these fees get financed into your second mortgage, giving you minimal out-of-pocket costs.

# Application & Process Overview

## Step 1 Application and Quoting

Your first step is the SBA 504 loan application. If you apply with Liberty SBF, we have a secure online portal that allows you to input all your information and documents digitally.

Your lender will need:

- › Basics on your loan request (such as amount and property location)
- › Information about your business
- › Ownership contact details
- › Documents related to your business and personal financials

Once you submit that information, we can get you a quote and term sheet within **48 hours**.

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## Step 2 Term Acceptance & Commitment

On the term sheet, we'll provide you with a quote. If you accept the terms, we'll then provide you a formal commitment (also known as a **conditional commitment letter**, or CCL) within **2 weeks**.

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## Step 3 Underwriting

You sign your CCL and pay a small deposit, which applies to your final down payment.

We perform an internal credit review, source third-party reports, manage all necessary paperwork, and interface with the local **certified development company (CDC)**.

During this phase of the process, we'll keep you updated on our progress and let you know if we require any additional documents from you. Unlike other lenders, we're very hands-on – we'll be with you every step of the way.

### **The Role of the CDC**

CDCs don't fund your loan, but they play an important part in the SBA 504 loan application process. A CDC is a non-profit organization, located in the same state as your real estate, that partners with your lender to submit your loan package to the SBA for approval. They are responsible for procuring authorization and interacting directly with the SBA. There are two approaches your lender may take when it comes to the CDC:

- › **Passive:** the lender gives you contact information and leaves you to follow up with the CDC yourself. This scenario contributes to the misconception that all SBA 504 loan applications come with extremely lengthy timelines – if you're not sure when, how, or why you need to follow up with the CDC, the loan approval process can take 6-12 months.
  - › **Proactive:** the lender takes initiative on contacting the CDC, gets them up to speed on the loan specifics, and sources immediate feedback on any roadblocks. The lender can then coordinate with you to get past those roadblocks, resulting in a faster approval timeline.
  - › Note that most lenders take the passive approach; apply with a lender like Liberty SBF if you want experts to do the work for you.
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## Step 4 Loan Authorization and Closing

If we receive SBA authorization, we close your loan within **45 days** of issuing your commitment.

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### Eligibility Requirements

SBA 504 loans are dedicated to small business owners who own real estate for their business. The SBA also checks your loan package against the following requirements:

- ✓ Your business operates as a for-profit company in the United States
- ✓ Your business will occupy at least 51% of the property you want to purchase or refinance
- ✓ Your business falls within [SBA size guidelines](#)
- ✓ Your business has a tangible net worth of less than \$15 million
- ✓ Your business has an average net income of less than \$5 million (after federal income taxes, for the two years preceding your application)

Before approving your loan, your lender and the SBA will also check that you have qualified management experience, a feasible business plan, and the ability to repay the loan

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### Our Expertise

It's important to choose the right lender. Liberty SBF is an SBA loan specialist and nationwide direct lender with over a decade of experience. We provide commercial loans between \$250,000 and \$15 million for a variety of property types, including owner-occupied commercial real estate (professional office, industrial/warehouse), self-storage, hotel, healthcare, multifamily, retail, and more.

Unlike other lenders who take a very passive approach to SBA loans, we're highly involved in the entire process, from interfacing with third parties to chasing down documents.

If you apply for a loan with Liberty SBF, you'll benefit from our:

- › **Accelerated timelines.** After receiving a signed conditional commitment letter (CCL) and deposit, we can usually get loan approval in as little as 30 days and close in 45 days.
  - › **SBA expertise.** We specialize in SBA loans. Whereas many banks and lenders have limited experience with the operationally-intensive process of securing SBA 504 loans, we work on them every day and know exactly what to do to get your loan closed.
  - › **Non-predatory lending.** The only thing we care about is closing your loan on time at the best possible rate. We won't try to cross-sell you other financial services like business checking accounts or credit cards.
  - › **Flexible underwriting.** In some situations, we can get you approved even if other lenders can't.
  - › **Best-in-class support.** While banks will often leave you to figure out what you need to provide and when, we walk you through the entire process and provide clear requirements and deadlines. We assign a single point of contact to your account who you can reach out to at any time.
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# Starting Your SBA 504 Application

We're here to guide you through the SBA 504 process from start to finish. Start your application now by registering for our online application portal. If you need help or have a question, reach out through our [online contact form](#).

Register Now

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## Glossary

**Certified Development Company (CDC)** – A not-for-profit entity that acts as the intermediary to get loan authorization from the SBA.

**Commercial Real Estate (CRE)** – Property used exclusively for business-related purposes (i.e. workspace, not living space).

**Conditional Commitment Letter (CCL)** – A document that conditionally approves the borrower for a certain loan amount so long as certain additional internal approvals are obtained, and certain conditions are met.

**Debenture** – A type of bond that the SBA sells monthly to raise funds to buy out their approved 504 loans from lenders. These monthly sales determine the long-term fixed rate for the loan.

**Lender** – An institution or organization working with the SBA to provide loans to small businesses. Examples include non-bank lenders such as Liberty SBF, commercial banks, credit unions, venture capital funds, and private equity firms.

**Loan-to-value (LTV) Ratio** – A ratio calculated by dividing the mortgage loan amount by the appraised value of the mortgaged property.

**Owner-occupied Commercial Real Estate (OOCRE)** – Commercial real estate where the owners occupy 51% or more of the square footage.

**Small Business Administration (SBA)** – A U.S. government agency that provides support to entrepreneurs and small businesses.

**Special-purpose Property** – A property that was designed with a unique layout and/or built with unique materials for a specific purpose. A special-purpose property may be difficult to convert for different uses. Examples include theaters, churches, and museums.

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