

SBA LEASE REQUIREMENTS

GENERAL RULE:

If the project real estate and improvements are owned by a separate company (*Real Estate Holding Company*) from the one that is operating the business (*Operating Company*), 100% of the real estate and improvements must be leased by the *Real Estate Holding Company* to the *Operating Company* and CDC must be provided with a copy of that Operating Lease. Any further leasing of the space to outside tenants must be structured as a sublease from the *Operating Company* to the sub-tenant.

OPERATING LEASE REQUIREMENTS:

Term: The lease must have a term that extends through the maturity date of the 504 loan. This can be the entire term OR an initial term plus options to renew. As the lease is typically signed in advance of the 504 closing and then funding occurs at a later date, keep in mind that the lease may need to be longer than 20 years to cover the term of the 504 loan.

Lease Payments: As the exact monthly payment for the 504 loan is not available at the time of closing (funding occurs later), the lease does not need to contain an exact rental amount. The SBA requires the rental amount to be substantially equal to debt service on the first lien, the SBA loan, any junior financing, plus allowable expenses, if applicable (taxes, utilities, and insurance). Therefore, there are two (2) options:

- The rental amount may be left blank AND the following statement included in the lease: “*The rent payable by the Tenant under the lease is limited to debt service plus real estate and rental taxes, association fees/dues, utilities, insurance, and reasonable repair/replacement reserves to the extent that the Tenant, in accordance with the Lease, is not paying any or all of such items.*”
- A reasonable rental amount may be included in the lease as long as it generally complies with the above-referenced SBA requirements.

OCCUPANCY REQUIREMENTS & LENGTH OF TENANT LEASES:

New Construction:

- (a) If there is a separate *Real Estate Holding Company* and *Operating Company*, the *Real Estate Holding Company* must lease 100% of the rentable property to *Operating Company* with any other leases being structured as sub-leases from the *Operating Company*;
- (b) *Borrower/Operating Company* must immediately occupy at least 60% of the rentable property;
- (c) *Borrower/Operating Company* will lease long term no more than 20% of the rentable property to one or more tenants;
- (d) *Borrower/Operating Company* must plan to occupy within three years some of the remaining rentable property not immediately occupied or leased long term;
- (e) *Borrower/Operating Company* must plan to occupy within ten years all of the rentable property not leased long term.
- (f) Loan Proceeds can be used for the building shell, but cannot be used to specifically build out space for an unrelated tenant.

Existing Building:

- (a) If there is a separate *Real Estate Holding Company* and *Operating Company*, the *Real Estate Holding Company* must lease 100% of the rentable property to *Operating Company*;
- (b) *Borrower/Operating Company* may lease up to 49% of the Rentable Property
- (c) Loan proceeds can be used to renovate the building shell and mechanical systems, but cannot be used to specifically improve or renovate any of the property to be leased to an unrelated tenant.

SUBORDINATION OF TENANT LEASES:

The SBA requires that any lease on the property be completely subordinate to the SBA mortgage. In other words, the SBA will have the option to foreclose out all tenants if there is a default on the loan.

- The lease should NOT contain any non-disturbance language.
- The lease should NOT contain any attornment language.

The following language should be added to the lease:

“This lease and all rights of Tenant hereunder shall be subject and subordinate to the lien of any and all mortgages that may now or hereafter encumber the Premises, or any part thereof, and to any and all renewals, modifications or extensions of any such mortgages. Tenant shall on demand execute, acknowledge, and deliver to Landlord, without expense to Landlord, any and all instruments that may be necessary or proper to further evidence the subordination of this lease and all rights therein to the lien of any such mortgage or mortgages and each renewal, modification or extension thereof, and if Tenant shall fail at any time to execute, acknowledge and deliver any such subordination instrument, Landlord, in addition to any other remedies available and consequence thereof, may execute, acknowledge and deliver the same as Tenant’s attorney in fact and in Tenant’s name. Tenant hereby irrevocably makes, constitutes and appoints Landlord, its successors and assigns, its attorney in fact for that purpose.”