

enforcement provisions for CDCs. In addition, SBA proposes to increase the "job opportunity average" and to permit CDCs to approve more projects that do not meet the job creation criteria but do meet other statutory goals. The proposed amendments also clarify the regulations governing fees that a small business may and may not be charged.

DATES: Comments must be received on or before August 7, 2003.

ADDRESSES: Address written comments to James E. Rivera, Associate Administrator for Financial Assistance, U.S. Small Business Administration, 409 Third Street, SW., 8th Floor, Washington, DC 20416. You also may submit comments via e-mail to proprule@sba.gov. You also may submit comments electronically to <http://www.regulations.gov>.

FOR FURTHER INFORMATION CONTACT: Gail H. Hepler, Chief, 504 Loan Policy Branch, (202) 205-7530.

SUPPLEMENTARY INFORMATION:

Statutory Basis of the 504 Program

The 504 Program, Title V of the Small Business Investment Act ("Act"), 15 U.S.C. 695, was established by Public Law 85-699 on August 21, 1958. A "development company" was defined as an enterprise formed for the purpose of furthering economic development of its community and environs, and with authority to promote and assist the growth and development of small business concerns in the areas covered by their operations. The law further stated that a local development company is a corporation chartered under any applicable State corporation law to operate in a specified area within a State and be composed of and controlled by persons residing or doing business in the locality. The program was amended in 1980 due to changing business conditions for small businesses. During the late 1970s and early 1980s, the prime interest rate and unemployment rate reached historically high levels. It was generally believed that long-term, fixed-rate money was not available at a reasonable cost to small businesses because of these high prevailing rates and that this was hindering job creation. Congress enacted section 503 of the Act in 1980. The 503 and 504 Programs were intended to provide long-term, fixed-rate financing to small businesses at favorable terms that were unavailable in the commercial marketplace. Congress specified in the Act that this program "foster economic development and create or preserve job opportunities in both urban and rural areas by providing long-term financing for small business concerns * * *". The

statute authorizes SBA to guarantee debentures backing long-term, fixed-asset loans ("504 Loans") made by CDCs. It also authorizes SBA to pool the guarantees and sell interests in the pools to investors.

Rulemaking History

On December 6, 2002, SBA published the ANPRM to solicit comments on the 504 Program. SBA posed specific questions requesting comments on a wide range of topics including the overall 504 Program's effectiveness; CDC organizational structure; ways to increase the 504 Program's geographic coverage to ensure that all small businesses have access to long-term fixed-rate financing; 504 loan and debenture structure; CDC performance requirements; operational and logistical issues; economic development; and CDC participation in other SBA programs. SBA received more than 1,900 responses from lenders, borrowers, government and community organizations, and CDCs.

Discussion of Comments Received in Response to ANPRM

In response to the questions in the ANPRM as to whether the need for the 504 Program still exists, the overwhelming majority of commenters supported the continued need for the program. The comments included approximately 600 letters from banks and other lenders and 590 letters from 504 Program borrowers. A national lender explained as follows:

Nationally, we rely on the 504 Loan Program in many of our markets because conventional real estate financing offers numerous obstacles to small business financing including the following: loan-to-value of 75% or less—more cash out of pocket for the borrower, 20-30% down-payment requirements, shorter amortization periods, ineligibility of special purpose (use) properties, balloon payments, exposure to short-term interest rates, multiple loan and pricing covenants and financial reporting requirements. For our customers the 504 Loan Program continues to be the most viable alternative to conventional small business loan products.

Emphasizing program benefits from the perspective of the lender, a banker stated:

There are a number of unique benefits for our bank and our borrowers when we participate in the 504 loan program. It allows us to continue to serve the banking needs of our small business customers while mitigating a degree of risk that always accompanies small business lending * * *. The 504 allows them to get a long-term, fixed rate financing through support from the government guaranty. With our bank in a first lien position with typically a 50% loan-to-

value ratio, our collateral risk is substantially reduced. The program also allows us to fund projects too large for our lending limit. There is also an active secondary market for 504 first mortgage loans. Most importantly, 504 enables us to meet customer credit needs and retain our business customer's primary banking relationship * * *. The CDC's expertise and working relationship with the SBA means that we save valuable lender time and expense by the CDC handling the application paperwork required for a government loan. The CDC is truly the program expert and monitors the changing rules, regulations and procedures for the 504 loan program * * *. Additionally, the 504 loan program has strengthened our small business community by allowing companies to grow and expand. We are heroes in the eyes of our small business borrowers and we like being able to keep our customers happy while maintaining our loan portfolio at a manageable risk level.

Another response from a bank added the following:

The program also allows us to fund projects too large for our lending limit. Additionally, we can limit our exposure to certain industries * * *. There is also an active secondary market for 504 first mortgage loans, so we can meet our board's liquidity requirements and, in turn, make even more small business loans.

Addressing the question of compatibility of the 504 Program with the loan programs authorized by section 7(a) of the Small Business Act, 15 U.S.C. 632 *et seq.* ("7(a) Program"), a lender stated:

The 504 Program, along with the 7(a) program and a (state) working capital loan program, work to complement each other in our market. The 504 fits quite well in its market niche of providing long-term fixed-rate financing to larger companies for plant and major equipment purchases. It is appropriately targeted to reach those companies in their growth cycle to create jobs, expand the tax base, and improve their communities. Both the 7(a) and State programs target, for the most part, smaller credits to provide working capital and financing for smaller equipment purchases. The 7(a) program is also frequently used for real estate purchases where a variable rate loan is preferred, because of the lack of a prepayment penalty, or where job creation is not the purpose or the targeted outcome. Taken together, along with some specialized private sector programs, the needs of small businesses are, for the most part, being met in our market and filling a void in conventional lending.

Regarding the 504 program's contribution to the economic development of communities, a typical comment follows:

The 504 Program is critical in all economic cycles but of greatest significance in today's economy. The ability of a small business to buy needed equipment and real estate to grow while preserving capital to fund expansion and job growth is crucial in