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Community Facilities Guaranteed Loan Program

Community facilities are often hard to finance because the nonprofits and governmental entities that plan them do not have long-term funding contracts that match the term of the loan they are requesting. For example, the state may provide one-year contracts for social services year after year, but the requested loan term may be 15 or 20 years. This is problematic for the lender. A lack of consistent funding with the same term as the loan, as well as a lack of adequate collateral, is part of the difficulty.

In rural areas, a USDA Rural Development (RD) program provides a credit enhancement to help finance community facilities. In the Community Facilities Guaranteed Loan Program, RD guarantees up to 90 percent of loss of principal and interest on loans made and serviced for construction or improvements of community facilities that provide essential public services in rural areas. Eligible lenders are banks, savings and loan associations, bank-affiliated mortgage companies, farm credit banks, and insurance companies.

A broad range of community facilities are eligible for guaranteed loans. These include cultural and educational facilities (such as schools, libraries, art museums, and theaters), transportation facilities (such as airports, municipal garages, street improvements, rail, or bus service), recreational facilities (such as parks, health clubs, and campgrounds), community health services (such as assisted-living facilities, hospitals, nursing homes, and medical and vocational rehabilitation centers), community support services (such as child or adult day care and business incubators), public buildings and improvements (including community centers), and fire, rescue and public-safety facilities.

Eligible applicants are municipalities, counties, special-purpose districts, nonprofits, and tribal governments. Eligible nonprofits, which are broadly defined, must have

significant ties to the local rural community, have a broad membership base, be controlled by members of the community, and have articles of incorporation and by-laws. Applicants must have the legal authority to borrow and repay loans, pledge security for loans, and construct, operate, and maintain facilities. They must also be financially sound and have the ability to organize and manage the facilities effectively.

Projects must be located in rural areas with population of up to 20,000. Because of differences in how state laws define municipalities, lenders should contact their state RD offices to determine community eligibility for the program.

In this flexible program, RD sometimes provides below-market direct loans or grants in combination with guaranteed loans, enhancing the financing package available to an applicant. Combining guarantees on bank loans with direct loans or grants reduces the overall interest rate, improves cash flow, and may make possible a larger amount of financing. Direct loans and grants can be combined with guaranteed loans for all eligible purposes except recreation loans, which are eligible only under the guaranteed loan program.

Benefits of bank participation include a reduced credit risk as a result of the guarantee. The program enables banks to help finance specialized facilities when borrowers lack sufficient collateral to fully fund a project. The guaranteed portion of the loans can be sold on the secondary market, increasing the lender's return.

Applicants and banks that are interested in using the program may submit a pre-application to determine project and sponsor eligibility. RD will recommend that a full application be prepared if the project appears to be eligible and funds are available.

Product Type	Primarily commercial real estate loan but can also be used for fixtures, furniture, and equipment. Banks typically assign responsibility for the community facility program to a commercial real estate department or government lending department. RD is not involved in the construction phase of a project unless direct loan funds are included in the permanent financing of a project.
Lender Eligibility	Banks that are regulated by federal or state bank regulatory agencies are eligible for the program. Lenders may charge a fee for the servicing.
Lender Roles	In addition to making RD-guaranteed community facility loans, banks may make construction loans to nonprofits or governmental agencies that receive community facility direct loans and may refinance community facility direct loans.
Underwriting	No minimum equity is required, and the maximum loan limit is determined by project feasibility. The interest rate is negotiable between the lender and borrower and may be fixed or variable. The lender may charge a pre-payment penalty.
Lender Requirements	The lender must retain a minimum of 5 percent of the total loan amount. This amount must be part of the unguaranteed portion of the loan. The lender is responsible for servicing the loan.
Repayment	The repayment period is limited to the useful life of the facility, but the maximum term for all loans in the community facility program is 40 years. (Guaranteed community facility real estate loans tend to be for 15 to 20 years, while loans for fixtures, furniture, and equipment tend to be for five to 10 years.) Loan repayment must be based on tax assessments, revenues, fees, or other sources sufficient for operation and maintenance, reserves, and debt retirement. Financial feasibility studies prepared by an independent consultant are normally required for start-up facilities or those that will result in a significant change in the borrower's financial operations.
Security	The lender determines acceptable security, which is approved by RD. Such security can include real estate, equipment, accounts receivable, and insurance income. Tax-exempt notes or bonds cannot be used for guaranteed loans. If the real estate appraised value is less than the loan amount, RD is willing to guarantee a loan based on sound security, repayment ability, and financial projections. RD is willing to subordinate a direct loan to a guaranteed loan.
Guarantee	Guarantees are backed by the full faith and credit of the U.S. government and can be sold on the secondary market. They are issued by the Rural Housing Service of USDA Rural Development; the agency pays cash in the event of a loss. Guarantees cover up to 90 percent of any loss of principal or interest. The guarantee fee, which is 1 percent of the guaranteed portion of the loan, is paid by the lender and may be passed on to the borrower.
Documentation	Loans are primarily processed on the lender's forms. The lender determines financial-reporting requirements. If a pre-application is submitted, a borrower provides historical financial statements, financial projections, organizational documents, information on existing debt, budgets, site information, information on potential environmental issues that may affect project viability, and evidence of public support. A bank provides an application for federal assistance and certification of the need for a guarantee. If a full application is submitted, the bank provides an application for loan and guarantee, a proposed security package, environmental information, and its credit analysis. The borrower provides cost estimates, copies of permits, certifications, and recommendations of appropriate regulatory agencies, financial feasibility reports, and preliminary engineering and architectural reports.
Applicant Requirements	Applicants must be financially sound and unable to obtain needed funds from other sources at reasonable rates and terms and must have the ability to organize and manage the facility effectively. They must demonstrate that the proposed community facility has substantial community support.
Proceeds	Loan funds may be used to construct, enlarge, or improve community facilities and may include land-acquisition costs, professional fees, and purchase of equipment. An existing debt may be an eligible purpose if the refinancing is less than 50 percent of the total loan and is associated with the project facility.
Application Processing	Applications are handled by USDA Rural Development field offices. After a pre-application is submitted, about 45 days are required to determine applicant eligibility, project priority status, and funding availability. After a full application is submitted, the time needed to process the application depends on the scope of the project, environmental review, and legal issues.
CRA Test	For specific information on CRA eligibility, lenders should contact their respective regulatory agency.
Program Information	In Pennsylvania, contact Gary A. Rothrock, Community Programs Director, USDA Rural Development, One Credit Union Place, Suite 330, Harrisburg, PA 17110; (717) 237-2281; gary.rothrock@pa.usda.gov. In New Jersey, contact Michael P. Kelsey, Director, Business and Community Programs, USDA Rural Development; 8000 Midlantic Drive, Suite 500; Mount Laurel, NJ 08054; (856) 787-7751; michael.kelsey@nj.usda.gov. In Delaware, contact James E. Waters, Business and Community Programs Director, USDA Rural Development, 4607 South DuPont Highway, Camden, DE 19934; (302) 697-4326; jim.waters@de.usda.gov. For information on this and other RD programs, see www.rurdev.usda.gov .