



CHANGES TO 504 DEBT REFINANCING PROGRAMS

IMPROVING ACCESS TO CAPITAL FOR SMALL BUSINESSES

WELCOME / PRESENTER



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CHANGES TO 504 DEBT REFINANCE PROGRAMS

- Refi **WITH** Expansion
- Refi **WITHOUT** Expansion
- Project Structures / Case Studies
- Q&A

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SBA 504 DEBT REFINANCE CHANGES



Changes to 504 Debt Refinance with and without expansion are **PERMANENT** changes



Interim Final Rule issued July 29, 2021



60-day comment period ends September 27, 2021



Implements section 328 of the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act



FEDERAL REGISTER

The Daily Journal of the United States Government



Rule

Debt Refinancing in the 504 Loan Program

A Rule by the [Small Business Administration](#) on 07/29/2021



PUBLISHED DOCUMENT



AGENCY:

U.S. Small Business Administration (SBA).



ACTION:

Interim final rule with request for comments.



SUMMARY:

This interim final rule implements section 328 of the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act, which revises the requirements for refinancing debt in the 504 Loan Program, including: For 504 debt refinancing involving expansions, increasing the amount of existing indebtedness that may be refinanced; and for 504 debt refinancing not involving expansions, removing two limitations on the program, reinstating an alternate job retention goal for the refinancing project, revising the definition of qualified debt, and removing the prohibition against Certified Development Companies ("CDCs") participating in the Premier Certified Lenders Program using their delegated authority to make these loans.



DATES:

Effective Date: This rule is effective July 29, 2021.

DOCUMENT DETAILS

Printed version:

[PDF](#)

Publication Date:

07/29/2021

Agency:

[Small Business Administration](#)

Dates:

Effective Date: This rule is effective July 29, 2021.

Effective Date:

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504 DEBT REFINANCE WITH EXPANSION

504 DEBT REFINANCE WITH EXPANSION

- **CHANGE** – Amount of existing indebtedness that may be refinanced as part of a 504 Project increased from not more than 50% to not more than 100% of the new expansion costs
- **No other changes** – existing requirements remain:
 - Original proceeds of debt to be refinanced must have been used at least 85% for purchase of eligible fixed assets, remaining 15% for any business purpose
 - Debt must be secured by fixed assets
 - Debt can be existing government-guaranteed debt, including SBA 7(a) loan, SBA 504 loan, USDA loan, etc.
 - Debt refi can include prepayment penalties and financing fees
 - Debt refi must meet “substantial benefit test” – savings of at least 10% on the debt being refinanced
 - Applicant must be current on all payments due for 12 months preceding SBA application date

504 DEBT REFINANCE WITH EXPANSION – CASE STUDY I

REQUEST

- ✓ Business's owner-occupied facility appraises for \$1,000,000 as-is
- ✓ Current debt balance is \$700,000
- ✓ Business owner wants to build an addition with new expansion costs of \$2,000,000

Use of Funds

Existing Equity	300,000
Existing Debt *	700,000
New Construction	1,400,000
Equipment	300,000
Soft Costs -	
settlement costs	New 50,000
appraisal & environmental	costs 10,000
contingencies @10%	140,000
interest carry	100,000
TOTAL USES	3,000,000

Sources of Funds

Third Party Loan	1,500,000	50%
SBA 504 Loan	1,200,000	40%
Borrower Contribution	300,000	10%
TOTAL SOURCES	3,000,000	100%

* NEW RULE

- Can refinance existing debt balance up to 100% of new expansion costs
- Is fully added to eligible 504 project

504 DEBT REFINANCE WITH EXPANSION – CASE STUDY 2

REQUEST

- ✓ Business's owner-occupied facility appraises for \$3,000,000 as-is
- ✓ Current debt balance is \$2,500,000
- ✓ Business owner wants to build an addition with new expansion costs of \$2,000,000

Use of Funds

Existing Equity	500,000
Existing Debt *	2,000,000
New Construction	1,400,000
Equipment	300,000
Soft Costs -	
settlement costs	50,000
appraisal & environmental	10,000
contingencies @10%	140,000
interest carry	100,000
TOTAL USES	4,500,000

**New
costs**

Sources of Funds

Third Party Loan **	2,200,000	49%
SBA 504 Loan	1,800,000	40%
Borrower Contribution	500,000	11%
TOTAL SOURCES	4,500,000	100%

* NEW RULE:

- Eligible Debt Refi amount is limited to \$2,000,000 (100% of new expansion costs)
- Remaining \$500,000 debt balance is ineligible and is added to Third Party Loan after eligible 504 Project structured

**** Final TPL Loan = \$2,700,000**



504 DEBT REFINANCE WITHOUT EXPANSION

504 DEBT REFINANCE WITHOUT EXPANSION

- Originally launched as a temporary program responding to Great Recession from 2010 to 2012.
- Brought back in 2016 as a permanent program
- Borrowers can refinance existing debt and cash-out equity for eligible business expenses
- Debt on owner-occupied real estate and/or capital equipment
- Maximum 90% LTV with no cash-out
- Maximum 85% LTV with cash-out for eligible business expenses
- Cash-out amount cannot exceed 20% LTV

504 DEBT REFINANCE WITHOUT EXPANSION

■ CASH-OUT FOR ELIGIBLE BUSINESS EXPENSES

- Expenses payable over next 18 months
- Salaries, Rent, Utilities
- Inventory
- Pay-down/Pay-off business line of credit and business credit card

■ INELIGIBLE USES OF CASH-OUT

- Capital expenditures
- Personal Expenses
- Business Acquisition
- Partner Buy-out



504 DEBT REFINANCE WITHOUT EXPANSION – PROGRAM ENHANCEMENTS

- **Eliminates** the condition that the program is only available when the 504 Loan Program is at zero subsidy
- **Eliminates** the cap restricting CDCs from processing new refinance loans that exceed 50% of prior year dollar volume
- **Reinstates** an alternate job retention standard – all existing jobs measured on a full time equivalent (FTE) basis can be counted as jobs retained by the refinancing project –
 - 1 job per \$75,000 of 504 debenture amount for all applicants except small manufacturers
 - 1 job per \$120,000 of 504 debenture amount for small manufacturers
 - If Project does not meet Job Creation/Retention, CDC can continue to use all available Public Policy and Community Development Goals

504 DEBT REFINANCE WITHOUT EXPANSION

PROGRAM REQUIREMENTS

1. Applicant must have been in business for minimum 2 years prior to SBA application date	NO CHANGE
2. Original proceeds of debt to be refinanced must have been used at least 85% for purchase of eligible fixed assets (land, building, machinery, equipment); remaining 15% for any business purpose	NO CHANGE
3. Loan incurred at least 6 months prior to SBA application date	CHANGE – reduced from 2 years
4. Loan secured by eligible fixed assets for at least 6 months	CHANGE – reduced from 2 years
5. Debt incurred for the benefit of small business seeking financing	NO CHANGE
6. Acceptable repayment history	CHANGE – removed requirement that borrower be current on all payments for 12 months preceding SBA application date
7. May include debt subject to a federal guaranty [SBA 7(a), SBA 504, USDA, EDA, etc.]	CHANGE – previously prohibited
8. Can consist of multiple loans, provided each meets all program requirements	NO CHANGE

504 DEBT REFINANCE WITHOUT EXPANSION

IMPORTANT CONSIDERATIONS FOR EXISTING GOVERNMENT-GUARANTEED DEBT

- **Refinancing must provide a “substantial benefit” to the borrower**
 - Minimum 10% savings on the debt being refinanced – must include prepayment penalties, financing fees, and other financing costs in the amount to be refinanced when calculating 10% savings
- **To refinance existing 504 loan**
 - Must refinance existing 504 loan balance along with any remaining balance on the existing Third Party Loan
- **For an existing 7(a) loan – *may be refinanced in whole or in part***
 - CDC must verify in writing that the present lender is either unwilling or unable to modify the current payment schedule to match the benefits of the 504 debt refinance
 - In the case of same institution debt, if the proposed Third Party Lender is the existing 7(a) lender, the loan will be eligible for 504 refinancing ***only*** if the lender is unable to modify the terms of the existing loan ***because a secondary market investor will not agree to modified terms***
- **For non-SBA federal debt (USDA, EDA, etc.)**
 - CDC must verify that the respective government program allows their loan to be refinanced

504 DEBT REFINANCE WITHOUT EXPANSION – CASE STUDY I

Refinance **without** Cash-Out for EBE

As-Is Appraised Value
Existing Debt **

\$5,000,000
\$4,500,000

USES OF FUNDS		SOURCES OF FUNDS		
	\$		\$	%
Existing Equity	500,000	Third Party Loan	2,500,000	50%
Refinance Existing Debt	4,500,000	SBA 504 Loan	2,000,000	40%
		Borrower Contribution	500,000	10%
TOTAL PROJECT COSTS *	5,000,000	TOTAL SOURCES	5,000,000	100%

SBA REQUIREMENTS

* Total Project Costs = Appraised Value of All Collateral

Additional collateral can be taken if existing debt exceeds 90% LTV on project property alone

**** Existing Debt can be conventional loan, SBA 7(a) loan, 504 financing (combined 1st and 2nd trusts), USDA, etc.**

504 DEBT REFINANCE WITHOUT EXPANSION – CASE STUDY 2

Refinance <u>without</u> Cash-Out for EBE		As-Is Appraised Value	\$5,000,000	
		Existing Debt	\$3,000,000	
USES OF FUNDS	\$	SOURCES OF FUNDS	\$	%
Existing Equity	2,000,000	Third Party Loan	1,500,000	30%
Refinance Existing Debt	3,000,000	SBA 504 Loan	1,500,000	30%
		Borrower Contribution *	2,000,000	40%
TOTAL PROJECT COSTS	5,000,000	TOTAL SOURCES	5,000,000	100%

SBA REQUIREMENTS

* In 504 debt refinance without expansion program, if borrower contribution exceeds SBA minimum requirement, extra can reduce both TPL loan and 504 loan, provided 504 loan never exceeds the lesser of the TPL loan amount or 40%

504 DEBT REFINANCE WITHOUT EXPANSION – CASE STUDY 3

Refinance with Cash-Out for EBE

As-Is Appraised Value \$1,500,000
Existing Debt \$1,000,000

USES OF FUNDS	\$	SOURCES OF FUNDS	\$	%
Existing Equity	225,000	Third Party Loan	675,000	45%
Refinance Existing Debt	1,000,000	SBA 504 Loan	600,000	40%
Cash out for EBE *	275,000	Borrower Contribution	225,000	15%
TOTAL PROJECT COSTS	1,500,000	TOTAL SOURCES	1,500,000	100%

SBA REQUIREMENTS	LTV
Total Financing = max 85% LTV	1,275,000 85%
*Cash Out for EBE = max 20% LTV	275,000 18.3%

504 DEBT REFINANCE WITHOUT EXPANSION – CASE STUDY 4

Refinance with Cash-Out for EBE

As-Is Appraised Value = \$1,500,000

Existing 1st mortgage = \$750,000

Existing 2nd mortgage = \$250,000 **

USES OF FUNDS		SOURCES OF FUNDS		
	\$		\$	%
Existing Equity	225,000	Third Party Loan	675,000	45%
Refinance Existing Debt	1,000,000	SBA 504 Loan	600,000	40%
Cash out for EBE *	275,000	Borrower Contribution	225,000	15%
TOTAL PROJECT COSTS	1,500,000	TOTAL SOURCES	1,500,000	100%

SBA REQUIREMENTS		LTV	** NOTE
Total Financing = max 85% LTV	1,275,000	85%	To be eligible for 504 debt refi, 2nd mortgage loan must meet all SBA requirements – minimum 6 months old, at least 85% of proceeds used to acquire eligible fixed assets, etc.
*Cash Out for EBE = max 20% LTV	275,000	18.3%	

504 DEBT REFINANCE WITHOUT EXPANSION

CASE STUDY 5

- Appraised Value = \$1,000,000
- Small business owner owns building free and clear
- Wants to tap into equity to get \$500,000 out for renovations
- **NOT ELIGIBLE** – there must be QUALIFIED DEBT on every 504 Debt Refinancing project

CASE STUDY 6

- Appraised Value = \$1,000,000
- Existing 1st mortgage debt is a \$500,000 line of credit used for various business operating expenses
- **NOT ELIGIBLE** – the line of credit does not meet the definition of QUALIFIED DEBT, as it was not used to acquire ELIGIBLE FIXED ASSETS

REQUIRED DOCUMENTATION

- **Note and Lien Instruments**
 - Bank promissory note
 - Recorded mortgage documents for CRE
 - Recorded lien documentation / UCCs for equipment
- **Payment transcript for most recent 12 months**
- **Documentation to support 85%/15% test** – i.e., settlement statement, etc.
- **If existing SBA debt:**
 - Copy of authorization
 - Substantial benefits test – 10% savings in monthly payment on debt refi amount
 - If refinancing existing 7(a) loan, written verification –
 - New TPL lender is different from existing 7(a) lender – written verification from existing 7(a) lender of unwillingness or inability to modify existing payment to match savings of 504 refinance
 - New TPL lender is same as existing 7(a) lender – written verification that 7(a) loan was sold into secondary market and secondary market investor will not allow payment modification



RECORD 504 LOAN VOLUME, LOW RATES & MORE!

Loan Activity through 7/30	FE 2019	FY 2020	FY 2021
# of Approvals	4,971	5,710	8,179
\$ of Approvals	\$4.1 billion	\$4.7 billion	\$6.8 billion

504 Term	Rate
25-year	2.90%
20-year	2.79%
10-year	2.64%



New loans approved through 9/30/2021

- ✓ Waiver of 1.5% CDC Processing Fee
- ✓ Waiver of 0.5% Third Party Lender Fee
- ✓ 3 months of Cares Act payment subsidies, capped at \$9,000 per month



QUESTIONS

