



SBA 504 DEBT REFINANCE PROGRAM – UPDATE 10/12/11

The U.S. Small Business Administration (SBA) recently authorized a temporary 504 debt refinance program. Here are some of the details of that program:

What are the qualifications for refinancing?

- 100% of the proceeds of the original debt must have been for the benefit of the small business—at least 85% used for 504 eligible purposes and the remaining 15% or less for other business purposes. The original debt may have been refinanced one or more times prior to the 504 refinance application and other funds advanced.
- If there is additional real estate equity (beyond the required 10% equity), SBA allows for the financing of eligible business expenses (expenses incurred prior to the application or to be incurred within 18 months of the application) as part of the refinancing project. Such expenses include working capital or payoff business LOC. It is not yet known whether the funds may be used for business expansion.
- The debt to be refinanced must have been incurred more than 2 years prior to the date of application. If the borrower intends to access equity, it may be possible to waive this requirement as long as the original debt is more than 2 years old.
- The existing loan must be current with no payments more than 30 days past due in the last 12 months under either the original payment terms or modified payment terms (including deferments).
- The business must currently occupy 51% of the real estate financed by the original loan and securing the existing loan.
- The business must have been in operation for 2 years (not a start-up).
- The refinance must be of a commercial loan, and may consist of one or more commercial loans.
- The existing loan has to be secured by 504 eligible fixed assets.
- Refinancing project can include professional fees and interest on the interim loan.
- The existing debt can be a loan from either an institutional lender or from others such as seller financing.

What debt does not qualify for refinancing?

- The loan to be refinanced cannot be a federally guaranteed or a 504 loan. (The original loan financing the assets may have been a federally guaranteed or 504 loan.)
- Debt owed to an associate of the borrower, SBIC, New Market Venture Capital Company.
- Debt where the creditor is in a position to sustain a loss and refinancing would cause a shift to the SBA of all or a portion of that potential loss.
- A loan for residential, personal, household or consumer purposes.

Bank and 504 combined LTV cannot exceed 90% of the appraised value of the fixed assets to be refinanced. The new bank loan can be less than 50% but not less than the new 504 loan. If existing debt to be refinanced is more than 90% of the appraised value of the fixed assets, the borrower can contribute cash or pledge other fixed assets acceptable to the SBA (commercial property, personal residence, and equipment) to cover the equity shortfall (see examples below).

The job requirement for debt refinance is the creation or retention of one full time job for every \$65,000 of SBA debenture financing. However, there are other provisions in the policy that would generally allow this requirement to be waived.

Funding details:

Funding must be structured as follows:

Bank -	not less than SBA loan (first lien position)
SBA -	not more than 40% of appraisal (second lien position)
Borrower -	not less than 10% of appraisal (cash, equity in eligible 504 fixed assets, equity in other fixed assets)

An SBA 504 refinance loan must be approved by the SBA on or before 09/27/12 and must fund within 6 months of approval. The on-going SBA Guarantee Fee that is included in the effective interest rate of all 504 loans is slightly higher (+.294%) for refinance loans. The one-time loan funding fee of 2.65% of the SBA loan is the same for refinance loans and is financed in the SBA loan.

Documentation needed to qualify debt:

In addition to the typical information needed to underwrite an SBA 504 loan, SBA requires the following information on the debt to be refinanced:

- Copy of current note and recorded lien instruments (DOT, security agreement, UCC1/UCC3).
- If current financing is a refinance, a copy of the original note and recorded lien instruments with documentation of the use of proceeds, e.g., copy of purchase contract, settlement statement, invoices from the original purchase. If this documentation is not available, the borrower can sign a certification as to the original use of funds.
- If the same institution is refinancing its own debt, a loan transcript covering the entire history of the loan being refinanced and Lender certification that it has no knowledge of a default by borrower.
- If it is not same institution date, a loan transcript showing the debt has been current for the past twelve months.

Example:

In 2003, a borrower purchased a building for \$650,000 to house his business operations 100%. He carries a conventional bank note with a balance of \$500,000 and is current on all his payments. Refinancing would mean better terms and smaller payments. An appraisal values the real estate:

1) Appraisal value of \$600,000 – debt refinance only

Appraised value of property	\$600,000
Balance of Debt	\$500,000
SBA 504 loan (up to 40% of appraisal)	\$240,000
Bank Loan (remaining balance--not less than SBA loan)	\$260,000
Borrower Contribution	\$100,000 (equity in the project)

2) Appraisal value of \$600,000 – debt refinance with maximum cash advance for business expenses

Appraised value of property	\$600,000
Balance of Debt	\$500,000
SBA 504 loan (up to 40% of appraisal)	\$240,000
Bank Loan (50% of appraisal)	\$300,000
Borrower Contribution	\$ 60,000 (required equity)
Additional advance to borrower	\$ 40,000

3) Appraisal value of \$1,000,000 – debt refinance and \$100,000 advance for business expenses

Appraised value of property	\$1,000,000
Balance of Debt	\$ 500,000
SBA 504 loan (under 40% of appraised value)	\$ 300,000
Bank loan (equal to SBA loan)	\$ 300,000
Borrower Contribution	\$ 400,000 (remaining equity)
Additional advance to borrower	\$ 100,000

4) Appraisal value of \$450,000

Appraised value of property	\$450,000
Balance of Debt	\$500,000
Bank Loan (50% of appraised value)	\$225,000
SBA 504 loan (40% of appraised value)	\$180,000
Borrower Contribution	\$ 95,000 in cash necessary to pay off the existing loan)**

** Borrower could pledge additional collateral to make up the appraisal shortfall.

For further information or questions with respect to eligible 504 debt refinance, please don't hesitate to contact Ann or Silvia at 383-3473.