SBA Policy Notice

TO: All SBA Employees and Certified Development Companies

SUBJECT: Revisions to SOP 50 10 6 that Incorporate Changes Made by Economic Aid Act and Interim Final Rule

CONTROL NO.: 5000-808830

EFFECTIVE: July 29, 2021

The purpose of this Notice is to revise the provisions of the SOP 50 10 6 relating to the debt refinancing options available in the 504 Loan Program to incorporate the changes made by section 328(a) of the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act (Economic Aid Act), enacted December 27, 2020, Public Law 116-260, and the interim final rule that SBA published in the Federal Register Vol. 86, No. 143, Thursday July 29, 2021.

A. SOP 50 10 6, Part 2, Section C, Chapter 1, paragraph C.10 is revised to read as follows:

"10. Permissible Debt Refinance without Expansion

13 CFR § 120.882(g)

SBA may approve a Refinancing Project of a Qualified Debt that does not involve an expansion as follows:

a. Definitions.

(1) "Qualified Debt" means a commercial loan that:

a) Either:

i) Substantially all (85% or more) of the proceeds of the existing debt was used to acquire an Eligible Fixed Asset(s) and the remaining amount (15% or less) was incurred for the benefit of the small business seeking refinancing; or

ii) If the Eligible Fixed Asset(s) was originally financed through a commercial loan (hereafter the "original loan") that was subsequently refinanced one or more times:

(a) Substantially all (85% or more) of the proceeds of the original loan was used to acquire an Eligible Fixed Asset(s) and the remaining amount (15% or less) was incurred for the benefit of the small business seeking the refinancing; and

(b) The existing debt is the most recent refinancing of the original loan.

b) Was incurred not less than 6 months prior to the date of application.

c) Was incurred for the benefit of the small business that is seeking the refinancing;

d) Has been secured by Eligible Fixed Asset(s) for at least six months;

e) May include debt subject to a federal guarantee under these conditions:

i) An existing 504 loan if both the Third Party Loan and the 504 loan are being refinanced or the Third Party Loan has been paid in full, and

ii) An existing 7(a) loan if the CDC verifies in writing that the present lender is either unwilling or unable to modify the current payment schedule. The existing 7(a) loan may be refinanced in whole or in part. In the case of same institution debt, if the Third Party Lender or the CDC affiliate as authorized under 13 CFR 120.820 is the 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 modify terms.

iii) The refinancing of a Federally-guaranteed loan provides a substantial benefit to the borrower after Eligible Business Expenses, prepayment penalties, financing fees, and other financing costs are accounted for. “Substantial benefit” will mean that the portion of the new installment amount attributable to the debt being refinanced must be at least 10 percent less than the existing installment amount(s). In calculating the percentage reduction in the new installment payment, prepayment penalties, financing fees, and other financing costs, must be added to the amount being refinanced, but not Eligible Business Expenses. The CDC may request the D/FA or designee to approve an exception to the 10 percent reduction requirement for good cause. PCLP CDCs may not use their delegated authority to approve a loan requiring this exception.

iv) If the loan being refinanced is guaranteed by a Federal agency other than SBA, the CDC must document in writing that the refinancing of the Federally-guaranteed loan is permissible under the other Federal agency’s requirements or is otherwise approved by the other Federal agency.

f) Is not a Third Party Loan which is part of an existing 504 Project, except as provided in paragraph 10.a.(1)e)(i) above; and

g) May consist of a combination of two or more loans, provided that each of the loans satisfies the Qualified Debt requirements.

(2) “Eligible Fixed Assets” are one or more long-term fixed assets, such as land, buildings, machinery, and equipment, acquired, constructed, or improved by a small business for use in its business operations.

(3) “Refinancing Project” means the fair market value of the Eligible Fixed Asset(s) securing the Qualified Debt and any other fixed assets acceptable to SBA. (Additional fixed assets may

be added only when needed to comply with the 90% Loan-to-Value Limitation described in C.10.i., below).

(4) "Eligible Business Expenses (EBE)":

a) Are limited to the operating expenses of the business that were incurred but not paid prior to the date of application or that will become due for payment within 18 months after the date of application. EBE includes accrued expenses such as salaries, rent, utilities, inventory, and other expenses of the business that are not capital expenditures.

b) May not include any other debt of the business, except that business lines of credit and business credit card debt may be included so long as:

i) Loan proceeds are not used to cover any personal expenses;

ii) If the line of credit and/or credit card was used for personal expenses, the Applicant must identify which purchases were for personal expenses and deduct that amount from the amount to be refinanced as an EBE;

iii) The line of credit and/or credit card are in the name of the small business; and

iv) The Applicant and the CDC certify in the loan application that the debt being refinanced was incurred exclusively for EBE.

c) If the Borrower is requesting that the refinancing include EBE, the application must include a specific description and an itemization of the amount of each expense.

d) The CDC must retain in its file the following EBE documentation:

i) EBE must be itemized (a gross figure is not acceptable).

ii) The CDC's credit memorandum must:

(a) Document the nature of the EBE;

(b) Provide the itemization of EBE; and

(c) Include the CDC's certification that the EBE are eligible as defined in this paragraph.

b. The Applicant must have been in operation for all of the 2-year period ending on the date that the application is submitted, as evidenced by the financial statements submitted at the time of application. If the business has been in operation for more than 2 years at the time of application, and there has been a change of ownership in the business, the CDC must determine, under the standards contained in the definition of New Business in Appendix 3, whether the Applicant should be considered a New Business and the application declined. The CDC must document the justification for its determination in its credit memorandum.

c. The Refinancing Project must include Qualified Debt, as defined below. In addition, the Refinancing Project may include Eligible Business Expenses, as defined below. The amount of the Refinancing Project is also subject to the Loan-to-Value Limitations in paragraph Section C.10.i below.

d. In accordance with 13 CFR §120.882(g)(5), the funding for the Refinancing Project must come from three sources based on the current fair market value of the fixed assets serving as collateral for the Refinancing Project, including an amount from the Third Party Lender that is at least as much as the 504 loan (net debenture proceeds), not more than 40% from the 504 loan, and not less than either a 10% or 15% contribution from the Borrower as determined under 13 CFR §120.882(g)(5).

e. If the Qualified Debt is not fully satisfied by the funding provided by the Refinancing Project, the lender of the Qualified Debt must take one of the following actions, or some combination thereof, to address the deficiency:

(1) Forgiveness of all or part of the deficiency;

(2) Acceptance of payment by the Borrower; or

(3) Require the Borrower to execute a note for the balance or any portion of the balance. This note must be subordinate to the 504 loan if secured by any of the same collateral.

f. If the Qualified Debt (including the original loan as defined in paragraph C.10.a.(1)a)ii) above) was for the construction of a new building, or the acquisition, renovation, or reconstruction of an existing building, and such loan would not have satisfied the leasing policies set forth in 13 CFR §§ 120.131 and 120,870(b), Borrower must be able to demonstrate compliance with 13 CFR 120.131(b) for existing buildings as of the date of application for assistance.

g. When the Refinancing Project involves a Limited or Special Purpose Property (see the Limited or Special Purpose Property List at paragraph E, 1.c.i.c) below), the Borrower must comply with the Borrower contribution requirements in paragraph E.1.c , below.

h. Notwithstanding § 120.860, a debt may be refinanced under this paragraph 10 if the Refinancing Project does not meet the job creation or other economic development objectives set forth in § 120.861 or § 120.862. In such case, the 504 loan may not exceed the product obtained by multiplying the number of employees of the Borrower by $75,000. The number of employees of the Borrower is equal to the sum of:

(1) The number of full-time employees of the Borrower on the date of the application, and

(2) The product obtained by multiplying:

a) The number of part-time employees of the Borrower on the date of the application; by

b) The quotient obtained by dividing the average number of hours each part time employee of the Borrower works each week by 40.

Example: 30 full-time employees and 35 part-time employees working 20 hours per week is calculated as follows: 30 + (35 x (20/40)) = 47.5. The maximum amount of the 504 loan would be 47.5 multiplied by $75,000, or $3,562,500.

i. Loan-to-Value Limitations

(1) For projects that refinance only Qualified Debt, the maximum loan to value of the Refinancing Project allowed is 90%.

(2) For projects when the amount of Qualified Debt being refinanced is more than 90 percent of the value of the Eligible Fixed Asset(s) securing the Qualified Debt, the Borrower must provide additional cash or other fixed asset collateral acceptable to SBA so as not to exceed a 90% loan to value of the Refinancing Project.

(3) For any projects that include the financing of Eligible Business Expenses, a maximum 85% loan to value of the Refinancing Project will apply and the Eligible Business Expenses portion of the Project may not exceed 20% of the value of the Eligible Fixed Asset(s) securing the Qualified Debt. The value of the Refinancing Project may not be increased by adding additional collateral.

j. Fees

(1) In addition to the annual guarantee fee assessed under 13 CFR § 120.971(d)(2), Borrower must pay SBA a supplemental annual guarantee fee to cover any additional cost attributable to the refinancing in an amount established by SBA each fiscal year. The CDC should follow the instructions on the Authorization for Debenture Guaranty to ensure the fee is correct.

(2) SBA will review the fee annually to determine whether it needs to be changed and, if so, will issue a notice of any change.

k. Other Implementation Guidelines

(1) Borrower must meet all current 504 Loan Program occupancy requirements at time of application.

(2) PCLP CDCs may not approve, under their delegated authority, the refinancing of an existing loan of the PCLP CDC, or its affiliates (i.e., Same Institution Debt) and must submit the 504 loan to SBA for approval. This requirement is consistent with SBA's long-standing policy of prohibiting its participating lenders from using their delegated authority to approve the financing of same institution debt due to the potential conflict of interest and the risk of the 504 loan proceeds being used to shift to SBA a potential loss from the existing debt.

(3) Loans for Debt Refinance without Expansion must be disbursed within 9 months after loan approval. The D/FA or designee, may approve a request for extension of the disbursement period for an additional 6 months for good cause.

l. Documentation Requirements

(1) Credit memorandum. The CDC must provide an analysis in its credit memorandum that the proposed debt refinancing satisfies each of the requirements of this debt refinancing program, including the requirements described in paragraphs 10.a.(1)a) through g), , 10.a.(4)a) through d), 10.b., 10.d., 10.e., 10.f., and 10.i. above.

(2) In its commitment letter (Exhibit 15 of SBA Form 1244), the Third Party Lender must certify that it has no reason to believe that the following statements in paragraphs a) and b) below are not true:

a) Either:

i) Substantially all (85% or more) of the proceeds of the indebtedness being refinanced were used to acquire an Eligible Fixed Asset (*e.g.,* land, including a building situated thereon, to construct a building thereon, or to purchase equipment) and the remaining amount (15% or less) was incurred for the benefit of the small business seeking the refinancing; or

ii) If the Eligible Fixed Asset(s) was originally financed through a commercial loan (the "original loan") that was subsequently refinanced one or more times:

(a) Substantially all (85% or more) of the proceeds of the original loan was used to acquire an Eligible Fixed Asset (*e.g.,* land, including a building situated thereon, to construct a building thereon, or to purchase equipment) and the remaining (15% or less) was incurred for benefit of the small business seeking the refinancing; and

(b) The existing debt is the most recent refinancing of the original loan.

b) All of the proceeds of the indebtedness being refinanced were used for the benefit of the small business.

c) In addition, if the indebtedness being refinanced is debt of the Third Party Lender, or any of its affiliates (Same Institution Debt), the Third Party Lender must certify in its commitment letter that it is not in a position to sustain a loss on the Refinancing Project causing a shift to SBA of all or part of a potential loss from the existing debt.

(3) Transcripts. The CDC must obtain a copy of the transcript of account, or equivalent, for the Qualified Debt being refinanced and submit and/or retain it as required by SBA Form 1244. See Exhibit 20 of SBA Form 1244. The CDC must determine whether the loan to be refinanced involves a creditor that is in a position to sustain a loss causing a shift to SBA of all or part of a potential loss from an existing debt, and document the justification for its determination in the credit memorandum. It is prohibited for a 504 Loan to be used to pay any creditor in a position to sustain a loss causing a shift to SBA of all or part of a potential loss from an existing debt under 13 CFR 120.884(b).

(4) Appraisal. Appraisals are not required at time of application. Appraisals dated within 12 months of the date the application was approved are required prior to closing, and appraisals must otherwise comply with the requirements for appraisals in paragraph E.2.b, below.

(5) Documentation to Verify Lien(s) at Application. In considering the Borrower's application, the CDC must obtain evidence that lien(s) are securing the Qualified Debt with Eligible Fixed Asset(s), and state in its credit memorandum that it has verified that the lien(s) has been in place for at least 2 years prior to the date of application. The CDC

must retain the evidence of the liens in its records (e.g., Preliminary Title Report, Mortgage Deed of Trust, or UCC-1 filing).

(6) Interim Lender Documentation. The Interim Lender must execute SBA Form 2288R, Interim Lender Certification for Refinancing Program, similar to what is required in all 504 closings.

m. Same Institution Debt

(1) When the loan being refinanced is Same Institution Debt (as defined in 13 CFR § 120.882(g)(15)), and the loan is not part of an existing 504 Project and is held 100% by the lender that will be the Third Party Lender of the Refinancing Project, the Third Party Lender may modify its existing loan documents (Note, Deed of Trust/Mortgage, etc.) instead of requiring the Borrower to execute and record new loan documents for the Third Party Loan.

(2) All modified loan documents must meet SBA's regulatory requirements for a Third Party Loan (see 13 CFR §§ 120.920 and 120.921).

(3) When the loan being refinanced is Same Institution Debt, either an Interim Loan or an escrow account may be used, and:

(4) The Third Party Lender (who, in this case, is also the Lender of the debt being refinanced) must execute SBA Form 2416, "Lender Certification for Refinanced Loan."

(5) The CDC may create an escrow account ("account") at the time of closing of the 504 loan for the purpose of holding the Borrower's cash contribution, if any, and the net debenture proceeds.

(6) The account will be established in accordance with an Escrow Agreement, which must be executed by the Borrower, the Third Party Lender, the Escrow Agent, and the CDC. The account may be held by the CDC attorney, Title Company or other party approved by SBA District Counsel.

(7) The Borrower's cash contribution, if any, must be deposited into the account at the time of closing of the 504 loan.

(8) A copy of the Escrow Agreement must be provided to the SBA's District Counsel with evidence of funding by Borrower's cash contribution, if any, at the time of closing of the 504 loan.

(9) The net debenture proceeds must be wired to the account, and all funds may be released only upon written approval by the CDC and SBA, provided that CDC/SBA have the required lien positions on the collateral as set forth in the Authorization and Debenture Guaranty.

(10) The debt to be refinanced will be satisfied by payment of the escrowed funds to the Third Party Lender.

n. A 504 Project cannot be approved to refinance debt owed:

(1) To an Associate, which is prohibited by 13 CFR § 120.130(a);

(2) To an SBIC or a New Markets Venture Capital Company (NMVCC), which is prohibited by 13 CFR § 120.130(b); or

(3) To any creditor in a position to sustain a loss causing a shift to SBA of all or a part of a potential loss from an existing debt. 13 CFR § 120.884(b)."

B. SOP 50 10 6, Part 2, Section C, Chapter 1, paragraph C.11.a. is revised to read as follows:

"11. Permissible Debt Refinance with Expansion

13 CFR § 120.882(e)

504 Projects may include a limited amount of debt refinancing with expansion, as follows:

a. If the Project involves expansion of an Applicant, any amount of existing indebtedness that does not exceed 100% of the cost of the expansion may be refinanced. The debt being refinanced will be added to the expansion cost to establish the total project costs, if all the conditions discussed below are met. A "Project involves Expansion" if it involves the acquisition, construction, or improvement of land, building or equipment for use by the Applicant."

B. **SOP 50 10 6, Part 2, Section C, Chapter 1, paragraph F.2.a.xii is revised to read as follows:**

"2. Contents of a 504 Loan Application

The CDC must maintain the following documents and any that support the CDC's credit decision in the CDC's loan files. CDC files must be available for review by SBA at any time.

a. The CDC completes or obtains the following:

* * *

xii. For "Debt Refinance Without Expansion" projects:

a) Copies of the transcript(s) of account or equivalent for any debts being refinanced; and

b) Certifications required for refinancing.

Questions

Questions concerning this Notice may be directed to the Lender Relations Specialist in the local SBA Field Office.

Isabella Casillas Guzman
Administrator