"BORROWING FOR YOUR ASSOCIATION"

Presented by:

Community Association Banc

NOW THAT YOU IDENTIFIED THE COST OF RECONSTRUCTION, WHAT ARE THE HOMEOWNERS' OPTIONS TO MEET THEIR PORTION OF THE ASSOCIATION'S FUNDING REQUIREMENT?

a. **Pay Cash** - earning interest rates on investments is generally below borrowing interest rates. Remember that Uncle Sam usually takes his share of your earned interest.

b. **Borrow funds that are secured on real property** - such as a second mortgage or equity line of credit. Generally, you will receive some tax deduction benefit (check with your CPA). If this sounds like the best option, we have special individual loan programs available.

c. **Participate in the commercial loan** that your homeowner association has received. Interest rates are reasonable and can be fixed over the loan term. No personal information will be required nor is any lien placed on your unit by the bank.

d. **Credit cards** - would normally be the worst option of all due to high interest rates, zero tax benefit and faster payoff schedules. (Unless you have some special package for earning points for free airfare and prizes!).

1. **CAN AN INCORPORATED ASSOCIATION BORROW FUNDS FROM A BANK?**

Yes. Due to the loan collateral requirements, non-incorporated associations would find it significantly more difficult to obtain a loan.

2. **ADVANTAGES OF BORROWING:**

a. Downward slide of property values slowed or eliminated. Structural problems, which must be disclosed to potential buyers, will retard the sales process and lead to falling home prices. Rapidly improving the appearance and eliminating structural integrity problems can slow or eliminate falling home values.

b. Needed repairs/improvements completed quickly. By borrowing the money, total needed funds become available for use much faster than through the traditional special assessment process. *Passing a special assessment will give the board of directors the power to collect the money. There is still the difficulty of collecting from those homeowners who do not have the ability to pay.*

c. Reduced financial impact on homeowners. By participating in the loan, homeowners avoid having to make a lump sum special assessment payment. Homeowners can pay their share over time to reduce the impact on their personal finances.

3. **DISADVANTAGES OF BORROWING:**

a. May increase monthly assessments. A special or increased assessment may be implemented to support the loan. Allocating portions of the reserve contributions can offset some or all of the increase.

b. Interest costs incurred may be high. This depends upon the loan structure. However, construction savings may significantly reduce the final effect on the association's total reconstruction costs if done over a longer period of time.

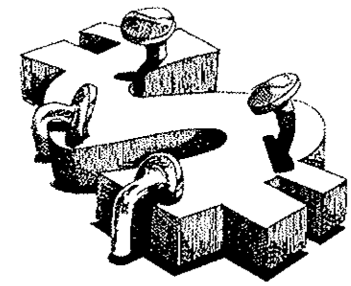
4. **HOW THE LOAN IS SECURED:**

Assignment of association assets that may include but are not limited to monthly assessments. No liens are placed on individual units by the bank.

5. **VOTE OF APPROVAL <u>MAY</u> BE REQUIRED**

Some banks will require that the Board of Directors be directly empowered to assign association assets by a <u>vote</u> of your membership. The vote is considered important because:

1. The membership has explicitly given the board of directors the power to assign association assets and enter into a loan agreement.



2. Membership has been notified of the board's potential action and had an opportunity to discuss the process in an open forum.

6. **TYPES OF LOANS AVAILABLE:**

a. <u>Repair/Replacement</u> of worn out major components such as roofs fences decks, paint, sidewalks, asphalt, etc.

b. <u>Improvement</u> of association facilities such as new pools, sauna, clubhouse, playgrounds, perimeter gates.

7. **GENERAL LOAN PARAMETERS YOU WILL SEE:**

a. Term = one to fifteen years.
b. Fixed and variable interest rate programs available.
c. Points = a fee of one to two percent on committed loan amount.
d. Rate = interest you pay on the loan – 7-10% fixed, or bank's reference rate + 1.5 to 3 % variable.
e. Application fee = $0 to $2,000 (typically refunded if loan is declined).
f. No prepayment penalties for paying before the term ends on variable rate loans. There typically is a fee for prepayment of fixed rate loans.
g. Structure = initially a "non-revolving" line of credit during construction phase of six months to one year. The line of credit is converted to a variable or fixed rate term loan when construction is completed.
h. The loan interest rate can be reduced if the association maintains its other accounts with the Bank.

8. **LOAN AMOUNTS AVAILABLE:**

a. $50,000.00 minimum.
b. Maximum amount varies with the size of the association

9. **APPROVAL PERIOD**

Usually, it will take up to 30 days from the receipt of all required documents for the loan to be approved. Loan documents are completed for signing within one week of receipt of the commitment letter from the bank.

10. **WHAT DOES THE COMMERCIAL LENDER LOOK FOR TO APPROVE YOUR LOAN?**

a. **Size:** How large is your association? Associations under 20 units will find it more difficult to receive a loan as they have fewer units with which to spread the loan payment.

b. **Cash Flow:** Can your association assessments cover the loan payment and continue to fund other reserve items?

*c. **Reserve Study:** Is your reserve study current, prepared by an experienced company, and appear to properly plan for your future needs?

*d. **Delinquencies:** Are there many units or just a few units with large amounts due? **Over 10% of the membership delinquent** should be cause for concern in getting the loan approved.

*e. **Delinquent Policy:** What is the structure of your assessment delinquencies? Do you follow your collection policy for delinquent assessments? Are you diligently collecting dues or are you letting members fall behind?

f. **Financial documents:** Are your financial statements reviewed or audited by a CPA? Do they correlate well with your bank statements?

*g. **Stability:** How stable is your association? Are you suing each other? Is there an attempt to recall the Board of Directors? **Is the owner occupancy ratio more than 70%?**

h. **Managed:** What is the Management Company's experience in common interest development management? Is the management company members of CAI, ECHO, or CACM? Does the management company staff carry professional designations such as PCAM OR CCAM?

*i. **Cooperation:** How cooperative are you in working with the lending officer? Does the loan officer feel comfortable with the relationship?

* = Key points

11. **COMMON QUESTIONS ABOUT THE LOAN:**

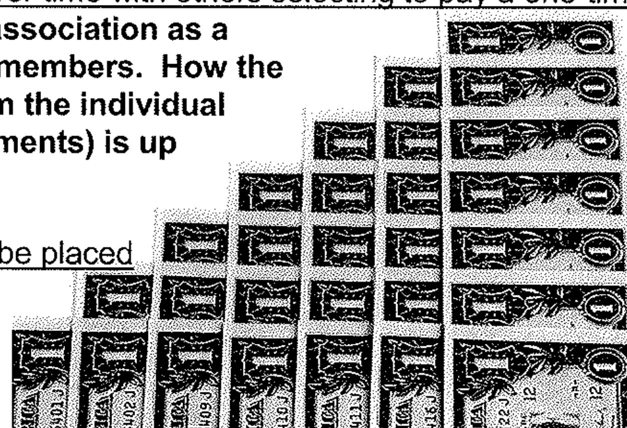
A. Does the bank put liens on individual units? **No.**

B. Do board members sign the note as individuals or as officers of the corporation? **They sign as corporate officers.**

C. Do the homeowners make their portion of the loan payment directly to the bank? **No. The owners don't have a loan. They are making a special assessment payment. The homeowners make their assessment payments to the association. The payment is deposited into an interest bearing account in the association's name at the bank. The bank debits that account each month for the loan payment amount.**

D. Does the bank want association reserve and operating accounts? **Usually. By obtaining the association's bank accounts, the bank can price your loan more favorably and follow the account activity more easily.**

E. Is it possible for only some owners to pay over time with others selecting to pay a one-time assessment? **Yes. The loan is with the association as a corporate entity - not with the individual members. How the association structures the payments from the individual members (i.e., monthly or lump sum payments) is up to the Board of Directors.**



F. If the payment were defaulted, would a lien be placed against the property of all owners or against only those who had elected to pay over time? **The assets of the association, identified as security in the loan agreement, would be used to bring the loan current. The Board of Directors may place liens on units that didn't meet their obligations according to your CC&R's.**

G. Is a proportional interest on the loan tax-deductible by each owner? **No. The loan interest is reported under the association's tax ID number. Members may opt to pay their portion of their obligation to the association from a second mortgage on their unit that may give them a tax deduction.**

H. Is there any tax advantage to the HOA? **Maybe. Tax benefits to the association would depend on their specific tax situation. Your CPA can answer this question for your association.**