

NEW LENDING POLICY FOR TICS: INDIVIDUAL OWNER LOANS AVAILABLE!

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In a landmark move, Bank of Marin has elected to offer to homeowners in the San Francisco Bay Area individual loans to purchase individual TIC interests. For the first time, each TIC owner will have the opportunity to have an individual loan secured by his or her own TIC interest rather than the entire property. This solves most of the financing problems inherent in the TIC ownership-but opens up some interesting new questions as well.

THE PROBLEM:



As discussed in detail in our article on [Tenancy in Common](#), real property in the Bay Area has become so expensive, with conversion to condominiums often limited and delayed, that the traditional joint ownership method of several persons owning an undivided mutual interest in the same property ("Tenancy in Common" or "TICs") has become increasingly popular as a means to purchase one's first home. The reader is advised to read the full detailed description of that method of ownership in the article mentioned above.

Such ownership creates a unique set of problems (and suggested solutions) including but not limited to the issue of how to finance the property. With two or more owners owning an undivided percentage interest in the property, the financing institutions have required the entire property to secure the loan, with each owner jointly and severally liable for the entire loan.

When any owner wishes to sell or refinance, all the owners would have to go along.

While "partial redemption" loans, allowing a particular owner to be cashed out or brought into the loan, have alleviated some of those problems, the fact remains that each person's interest in the property and credit rating would inevitably be dependent on the performance of the other owners,

The traditional solution has been a very powerful TIC Agreement which gives the owners fast and effective remedies to buy out or stop a poorly performing TIC co owner from affecting the property or their credit. While certainly useful, it made many TIC owners nervous that their own economic well being would be dependent to some extent on a co owner's actions.

Further, such useful tools as equity lines of credit or refinancing became either impossible or complex compared to the relative ease of such economic mechanisms for the individual home owner.

TICs remained popular because the price differential was attractive enough to make up for the added complexity and the use of good TIC agreements minimized the problems, Nevertheless, the banking development described below will greatly improve the usefulness of TICs for many people assuming other banks follow the lead. ***Put simply, the individual TIC interest will act as security for individual TIC loans!***



As reported in **SF gate.com**, in a move that has the potential to substantially change San Francisco's housing market, **Bank of Marin** in the next three to four weeks will become the first financial institution to make individual home loans to people who own apartment buildings in the city as tenants in common.

Despite that drawback of each TIC owner being liable for the entire loan on the entire building rather than merely the TIC unit occupied by that owner, many apartment buildings are converting to TIC ownership because of the city's strict condo-conversion laws: **In San Francisco, only 200 apartment or TIC units per year can be converted to condos, and they must be in buildings with six or fewer units.** In San Francisco, many people buy TICs hoping they will later win the city-run lottery that lets them convert their building to a condominium, a process that typically takes *five to seven years*.

Bank of Marin's move is just a small step. The bank is strictly limiting the number of TIC loans it will make and setting specialized conditions for them. But if other lenders follow suit and individual financing becomes widely available, TICs could become a more viable form of ownership for many people. The need to convert to condo would become less imperative. That could make TICs more popular, which could increase their price. The price rise could be limited, however, if more apartments are converted to TIC ownership. The increase in supply would be good for potential home buyers but bad for renters.

"We are opposed to TICs because TICs are unregulated," says Ted Gullickson, office manager of the San Francisco Tenants Union. "This would make them even more numerous."

Most experts feel that where the impact is going to be most significant is in buildings with more than six units. Up until now, they have seldom been sold in San Francisco as TICs because they could never be turned into condos. Such buildings may skyrocket in value since the need to convert to TICs may be minimized with the new lending rules.

When a group of people buys a building as tenants in common, each owner has an undivided fractional interest in the building. Instead of owning a single unit, as in the case of a condominium, each of the owners might own 25 percent of a four-unit building. A separate contractual agreement generally states who gets which unit.



The group gets a single loan on the property, and each owner is responsible for a proportionate share of the mortgage. If one owner stops paying his or her share, the other owners have to pay it. The joint loan also can make it harder for one owner to sell his or her share without refinancing the entire property.

When you buy a condominium, your right to occupy a specific unit is stated in the deed, a more secure form of ownership than a contract. Condo owners get their own loans and can buy and sell their units just like they would a single family home.

Until now, banks have been unwilling to make separate loans to individual TIC owners. One reason: TIC ownership is rare outside of San Francisco and a few other cities, so there has not been a national market. Also, there is no secondary market for such loans. The lenders that make them have to keep them on their books, at least for now. That will limit the number of such loans one bank can make.

Banks also needed to be convinced they would be able to foreclose on an individual TIC loan. Since this method has not been tried in the past, there is no case law on the subject to reassure nervous banks who are very conservative. But if the Bank of Marin experiment succeeds, it is likely many other banks will follow suit and one can expect a flood of TICs being created...and older TICs altering their financing to individual TIC loans.

Bank of Marin decided to test the market because its customers asked for it. Like other banks, it has been making loans to real estate investors and developers, who buy apartment buildings, fix them up and convert them to TIC ownership. Under its new program, it will make a limited number of fractional- interest loans to individuals who buy units from developers who got their acquisition/renovation financing from Bank of Marin.

Its initial \$20 million loan commitment includes acquisition/renovation loans as well as the new fractional-interest loans. **All of the new loans already have been spoken for.**

The fractional-interest loans are expected to be for about \$300,000 to \$400,000 each, says Bank of Marin's Keith Zimmerman. "We will close on the first ones in three to four weeks," he adds.

The loans will be structured like commercial real estate loans. They will be amortized over 30 years, but the balance will be due in 10 years. The interest rate will be 7 percent fixed for the first five years and will adjust once after five years.

The average rate on a conventional 30-year, fixed-rate home mortgage is around 5.9 percent nationwide.

If the new loans perform well over the next three to four months, Bank of Marin will consider making more, Zimmerman says.

"We have been approached by **First American Financial** out of Irvine about buying the loans on the secondary market," which would free up Bank of Marin to make more individual TIC loans.

Now that Bank of Marin has broken the ice, it's more likely that others will follow. E-Loan executives have been quoted as saying they plan to begin offering fractional loans to TIC owners.

Circle Bank, based in Novato, is "actively looking into providing fractional loan program for TICs but as of this writing, it is not available. We hope to do it sooner than later. I hope it would be sometime this year," said Mark Skolnick, a wholesale loan representative with Circle Bank.

Sterling Bank & Trust, based in San Francisco, is also looking into them. "We are not doing them right now. Could we be doing them in the future?"



That's a good possibility. If we do anything, it would be after January 1," says Stephen Adams, a managing director with Sterling.

The mayor's office is hoping to see more banks offer individual TIC financing.

"We think it's a very positive development," says Matt Franklin, director of the Mayor's Office of Housing.

"One of the drawbacks to TIC homeownership is that it creates additional financial risk for the participants greater than one would encounter in a condo, because the mortgage is shared among many parties. If it is forced into default or foreclosure that would affect everybody's credit rating."

Franklin says he thinks individual financing would shrink the gap between TIC and condo prices, but "it remains to be seen whether products from the financing side make up the whole difference between how the market values a TIC and a condo." Franklin adds that the change in financing will do little to resolve the desperate need for more affordable housing in the city.

"In our view, the key to affordability is more new units," he says.