

BOND vs. BANK FINANCING

Most of us are familiar with how a traditional bank loan works: The borrower obtains a sum of money from the bank, and it promises to repay the borrowed amount (the principal), plus a charge for the use of the money (the interest), all at a specified date in the future.

A bond program works in much the same way, but instead of the bank loaning the money, the loan funds come from individual investors (the bondholders). The bonds are sold to investors in \$1,000 denominations; the size of the bond issue is equal to the amount of money needed by the borrower. The borrower then makes principal and interest payments to the bondholders through a corporate trustee (usually a bank), which handles all the record keeping and payment functions. Both types of financing require collateral for the loan. Usually the collateral is real property, such as land and buildings.

The Bond Company underwrites your loan by first committing to purchase all of the bonds from you, and then selling them to their investors. By contractually agreeing to buy all of the bonds, they guarantee you the funds you need to complete your project, whether it is new construction, refinancing, renovation or property acquisition.

Advantages of bond financing over a bank loan

FIXED INTEREST RATE

Most banks only offer adjustable rate loans that can expose your organization to substantially increased loan payments if interest rates rise. With bond financing, your interest rate is fixed for the term of the loan. Budgeting is simplified by knowing interest and principal payments are fixed for the entire term of the loan. Concern about rising interest rates is eliminated.

LONG-TERM LOAN, FULLY AMORTIZED

Many bank loans are for only three to five years, with a large balloon payment due at the end of the term. This means you must refinance your loan at a later date. If the financial position of your organization has changed at the time, or if interest rates have risen, you might not be able to refinance. Why expose your organization to this risk?

Most bond issues are fully amortized over a five-to 20-year period, depending on your needs. Level debt service aids in budgeting, and ensures that the loan can eventually be retired without the hassle of refinancing every three to five years.

OPEN-ENDED MORTGAGE

If you need more money, most banks will require you to refinance your old loan. This could mean higher market interest rates, and certainly new loan fees for refinancing your existing loan. With bond financing, the mortgage documents allow your organization to borrow additional sums at later dates without disturbing the original loan or adding financing costs to previous loans. This is especially important for growing organizations that anticipate needing future funds for expansion.

LIBERAL PREPAYMENT PROVISIONS

Many banks have prepayment penalties written into their commercial loan contracts. This can make it unattractive to use excess cash to pay down your loan. Under the bond program, prepayment of any amount of principal with unborrowed funds is allowed without penalty. You can lower the effective interest rate on your loan by specifying prepayment of the longer-term bonds, which pay higher interest rates than the shorter-term bonds. Then, you may also lower your normal loan payments accordingly. They do have some limitations on prepayment of bonds with funds borrowed specifically for refinancing during the first three years of the loan. This gives some assurance to the bondholders that they will have their investment for a reasonable duration.

LARGER PROJECTS


Many banks are reluctant to lend money to nonprofit institutions, especially for multi-million dollar projects. Banks can also require personal guaranties from individuals associated with your organization. Furthermore, banks operate under regulatory guidelines, which usually require the borrower to pledge large amounts of collateral with respect to the loan size. The loan size to collateral value ratio is an extremely liberal 70% to 75% (many banks are at 50%). This means the project of your dreams can be within reach, without personal guaranties to help secure the financing.

Additionally, the years of experience working with nonprofit institutions will help guide your organization through the building process. We offer you ideas, suggestions and most importantly, an attractive financing plan. Our service to clients is one of our greatest strengths.

FINANCING PARAMETERS

IPL uses the following parameters to determine whether we can assist you.

- **33% Income Test-**Your organization's annual debt service should not exceed one third of its income. For example: If a church has general fund income of \$750,000, the annual mortgage payment should not exceed \$250,000. Building-fund monies can be used in the calculation in some instances.
- **75% loan to value ratio-**The percentage of the loan to the value of existing buildings, land, and the project being financed by the loan should not exceed 75%. Example- Appraised or "book" value is \$2,000,000. That amount, multiplied by 75% suggests a \$1,500,000 loan amount.
- **The organization must have an operating history of more than three years.**
- **We have a \$1,00,000 minimum loan requirement.**
- **A fixed-price construction contract is required a new building projects.**



**INCOME PROPERTY
LENDING**

A division of the All Star Group, Incorporated

Arnie Garfinkel
President

2187 So. Garfield Avenue
Los Angeles, CA 90040
<http://www.incomepropertylending.com>

(323) 728 - 7700
fax (323) 908 - 4006
e-mail: arnieg@allstargroup.com

ANSWERS TO COMMONLY ASKED QUESTIONS

Q

DOES THE BOND COMPANY HAVE TO SELL ANY OF THE BONDS TO MEMBERS OF MY PLACE OF WORSHIP?

Answer

No. They have an established investor base of more than 70,000 individuals who find the bonds an attractive investment product. They do not need to sell bonds to anyone associated with your organization, although, they do so if any members wish to purchase bonds.

Q

WHAT IF THEY CAN'T SELL ALL OF THE BONDS?

Answer

The investment sales staff usually is able to sell a multi-million dollar bond issue in less than a week. However, as a firm underwriter they guarantee to buy all of your bonds at specified interest rates, and at a specified date, regardless of how quickly your bonds sell or how many of the bonds are sold.

Q

HOW SOON CAN WE RECEIVE FUNDS?

Answer

They can usually fund a bond issue within 45 to 60 days after our finance committee has approved your loan.

Q

DO WE NEED AN APPRAISAL?

Answer

In many cases they do not require an appraisal, and can use the net book value of your assets for loan to value purposes.

Q

HOW DO WE GET STARTED?

Answer

Please call Arnie Garfinkel at (323) 728-7700. He will answer your questions and ask you to send more specific information regarding your organization. This aids in determining the size loan for which you may qualify.