MINDING YOUR "P"s AND…

By Patrick Niland

Despite all of the exhortations of publishers and professionals, some co-op board members still manage to overlook one or more of the three "P"s when refinancing their building's underlying mortgage. In doing so, they incur the risk of a fourth "P" – financial peril. In today's volatile financial markets, a board must attend to all three of these essential parameters if they are to have a successful refinancing. So what are these three essential elements? Planning, Pricing, and Processing.

Planning

Refinancing an underlying mortgage is, by far, the most important financial decision that a board will ever make. It will affect not only the operating budget of the cooperative and the monthly maintenance of each shareholder, but also the market value of every unit in the building. Therefore, given the significance of this decision, it is remarkable that some boards still give it less attention than they do the selection of new wallpaper for the lobby.

A successful refinancing requires very careful planning. And effective planning requires the involvement of yet another "P" – the co-op's professionals. Most co-ops have a managing agent, an attorney, and an accountant. Some co-ops keep additional professionals "on retainer" -- an engineer, a tax certioari expert, and/or an insurance specialist. Each of these professionals has valuable knowledge and experience that should be incorporated into every one of the board's major decisions. Unfortunately, some boards are penny-wise and dollar-foolish; they ignore this

wealth of information for fear of “running the meter” on fees. That’s a lot like “arming” yourself with an unloaded gun to save money on bullets.

So, for your next refinancing, load up on help. A well-organized professional team (managing agent, attorney, accountant, experienced mortgage broker, licensed engineer, etc.) will pay healthy dividends throughout the entire refinancing process. These experts will ensure that you enter the market at the right time, borrow the appropriate amount, include the proper terms and conditions in your loan documents, and stay focused until the new loan is closed and funded. Whatever they may charge you for this service is money very well spent.

For example, your managing agent and engineer can help you assess your building's present physical condition, as well as likely future repairs. Your accountant and managing agent will give you a realistic picture of your co-op’s past financial performance and its current fiscal health. They also can help in quantifying your future funding needs, recommend the proper loan structure to meet your goals, and lend perspective to the comparison of alternate loan offers. Your attorney should review all of your existing loan documents to see if they are in proper order, and also search for any onerous prepayment penalties or notice requirements which could impede or prevent your refinancing. Lastly, each of these professionals should review your loan application, commitment letter, and new loan documents to ensure that they satisfy the board’s objectives.

Pricing

This is the most misunderstood of the “P”s. Given the hyperbole of certain lender and broker ads which scream sub-market rates

like adjacent gas stations during a price war, it is not surprising that some board members succumb to “rate myopia.”

But a low interest rate alone does not a good loan make. Nor is a loan’s interest rate the only component of its pricing.

Perhaps the best way to think of “Pricing” is to equate it with “payment.” Payment encompasses more than just the monthly payment of principal and interest; it also includes any origination or commitment fees (“points”), tax and insurance escrows, requires operating and repair reserves, and penalties for violating the other terms of the loan (e.g., late fees, prepayment penalties, etc.). All of these elements comprise the “pricing” of a loan, and the board and its team of advisors must evaluate each of them in the context of the board’s goals. Poor handling of these other factors can have a <u>much</u> bigger impact on the co-op’s finances than shaving a few basis points off the interest rate.

Processing

The processing of a loan is often the weak link in an otherwise well-organized refinancing. Some boards use their application to “shop” for a lower interest rate. (Lenders hate this practice and, when they inevitably discover it, usually rescind the application.) Other boards will argue the minor provisions of their commitment beyond its expiration date, thereby losing the “good deal”
they had worked so hard to get. Yet others will forget to give their existing lender the required notice and must pay the new lender a hefty extension fee to reschedule their closing for a later date. Or someone misplaces the existing loan documents, thereby preventing an assignment and forcing the co-op to pay mortgage recording tax on the full amount of their new loan.

There are countless other examples of co-op boards who lost sight of their goal before attaining it. As anyone who follows sports knows, "it ain't over 'til it's over." In refinancing, it ain't over 'til the loan's closed. Remember, a loan application merely tells you what you must do to get a commitment letter; the commitment contains multiple conditions which must be satisfied before you can close your new loan. Neither document should be viewed as a "done deal." However, if you follow the "directions" contained in each, and keep your entire team involved and focused, you will have very few problems on your way to (and during) the closing.

Planning, Pricing, and Processing – the three keys to success in any refinancing. Forget them, and you may suffer the fourth "P" (financial peril). Pay them heed, and you can enjoy the fifth "P" – the post-closing party!