CircleBLoans

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Tenant In Common (TIC) Financing for Homeownership

A BRIEF HISTORY,

by Mark Skolnick

The TIC housing concept has been around the Bay Area since after World War I, when soldiers came home en masse and housing was scarce. Although the TIC platform was studied, it never took hold because financing was problematic. After WWII the story repeated itself, and about 25 years ago the concept caught on in Berkeley. San Francisco followed soon thereafter, and as housing costs rose and rent control laws tightened, San Francisco became the epicenter for the modern TIC movement. Still, until the advent of the Fractional TIC Loans, where each TIC partner receives a separate note and deed, TIC's never really took off. Some real estate companies (until recently), even prohibited their agents from transacting in TIC's, due to earlier issues that have since been solved. TIC's are now established as a legitimate type of housing, and with Circle Bank on the leading edge, finance products are expanding to meet this growing market.

There are now two basic kinds of loans for properties owned as Tenants In Common; Group Loans and Individual Loans. Group loans all have one thing in common: shared liability on the mortgage. Until the fall of 2005 group loans were the only type of financing available for TIC owners, and this was the main reason why the TIC market did not significantly expand until fractional loans became available.

Early on, TIC owners were hamstrung by having to use traditional loan products; for 2-4 unit properties a variety of loan programs have always been available, but typically without proper assumption clauses. TIC owners of properties with 5 or more units, including mixed use with a commercial component, paid the highest price; they were saddled with appraisals and loan products geared toward commercial income properties; these properties were valued based on their rental income potential, and in a city like San Francisco with rent control it was especially complicated.

Starting in late 2003, we at Circle Bank began seeing more purchases of apartment properties at irrationally high prices, where it was obvious the rents would never catch up to servicing the loan amount. One of our hallmarks is offering highly leveraged loans on income properties, even when the rents do not support the loan request, as long as we believe in the buyers' game plan for turning the property around. In order to do this, the buyer must be able to demonstrate provable tax reported net income that is enough to support debt-to-income ratios of up to 50%, including the negative cash flow on the subject property. This type of lending is part of our core business.

The Buyers of these building shared with us their plans to not rent the property but to convert it into a homeownership opportunity, where the units would be sold to separate individuals who would hold title as Tenants In Common. The economics of these transactions made sense only in this light. In response, we took the step of developing loan products that took into consideration the present as-is value of the income property, and the future 'bulk' value of the individual TIC units. This approach allowed us to lend more to the TIC 'Converter'(Developer) than what had been the norm. It also led us to providing 'TIC Friendly' financing (without restricting the loan to an amount based on the rental income potential of the property) for the groups of buyers who would be living in the property as owners (cotenants).

This step helped uncork the pent up demand for TIC properties, but not completely. Although we were lending based on a hybridized value that took into consideration the combined purchase of the TIC units, and we allowed for unlimited assumptions so individual owners could more easily sell their units, many of the other major problems of TIC's remained unsolved. These problems stemmed from having only one loan with joint and several liability, where every TIC member was fully responsible for paying the loan, notwithstanding default provisions outlined in the TIC Agreement. Having one group loan is a big problem if values are rising and the loan balance is relatively low, and a sale occurs. This could trigger the need for a refinance, the costs of which may be born the one seller. Also, what happens if certain members no longer qualify for financing? These problems and many others needed to be solved.

The solution was to issue **individual loans**, in spite of the fact that there is only one Assessors Parcel Number (APN). Separating the co-tenants from one another financially solves many problems and alleviates most fears and concerns associated with TIC ownership. **The three biggest advantages to individual TIC loans are:**

1) The elimination of shared liability
2) The increase in the marketability of the individual interests...they become easier to buy and to sell, and
3) Simplicity- if an owner needs to refinance, he/she simply applies for a new loan, and if the unit is being sold, financing the sale does involve the co-tenants, as can be necessary when there is a group loan. There are no internal group politics or acrimony to worry about (as may occur in situations if there are strained personal relationships, or some members may no longer qualify or don't care to help facilitate a process that may benefit only the selling party.

In conclusion, Fractional TIC lending is central to the surge in market acceptance of this type of housing. Now, TIC's are seen not just as entry level housing, but as value-added properties across all market segments, from entry level to luxury. The TIC concept is spreading throughout the Bay Area and Southern California, and Circle Bank is there for you to help you increase your business in a, as well as all other areas of investment property finance.

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