Get the Facts Before You Act

Setting the Stage

This Forest Hills co-op board was led by one director who was determined to pay off the underlying mortgage, which would come due in three years. Money was tight and, like many boards, this one had refused to raise maintenance as expenses increased. There was little money for upkeep, and the property had started looking its age.

Following the Action

The board was soon faced with a citation by the city to immediately perform facade work, costing over $200,000. When I had my regular meeting with the property manager on this building, he told me that the board wanted to assess the shareholders for the Local Law work over a 12-month period. I told him that this was too much for the shareholders to handle and instead that he should recommend refinancing. He told me that one longtime board member had convinced the rest of the board that the prepayment penalty was too high and that they should wait the three years to be mortgage-free.

At the annual meeting it was chaos. Shareholders complained about the lobby, the elevator, and the hallways, all of which needed repairs. Then the shareholders were told about the required work, and the board voted on an eight-month assessment, with an average monthly payment of $410. That led to more yelling and questions.

As the meeting concluded, the board started to leave. I asked them to wait, sat them down, and said there was no need to put such a burden on the residents by assessing them for a short period of time for a capital improvement that would last over 30 years. I requested their permission to explore refinancing options. One board member, with the loudest voice, stood up and said it was a waste of time because the prepayment penalty was too much. I said that it was worth researching, because their current mortgage had a rate of 7.85 percent, with a small balance of $350,000 and I was seeing mortgage rates under 4 percent. So, whatever the prepayment was, it would be repaid quickly with the savings on the lower monthly payment of principal and interest. This raised some eyebrows around the table, and these individuals said I should look into it.

I came back with a spreadsheet of bank offers all in the range of 3.50 percent interest rate and a prepayment penalty that was only $35,000. They settled on a new mortgage with NCB for a 10-year term on a 20-year amortization. NCB was attractive to them, because of the mortgage tax savings on the large proceeds from the new mortgage of $1.9 million.

The co-op ended up closing the loan at 3.55 percent, and after closing costs, had proceeds of $1.5 million and was saving $21,000 a year in debt service. The board cancelled the assessment, completed the city's required work, made the needed repairs, and still had a healthy reserve account, without a burden to the current shareholders.

Doing It Right

The lessons? Do not let one person feed you information unless he or she has the facts right. Get involved and informed about your building. This isn't a single-family home where you want to have a mortgage-burning party. Look to use the value of your property to fund capital improvements. Listen to the complaints; they will tell you how shareholders feel on the condition of building. Study your budget carefully, reviewing line-by-line items, and make realistic assumptions that will maintain the quality of the building while protecting your investment. ■

Use the value of your property to fund capital improvements.

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