LesMark Capital, LLC

SELF-AMORTIZING BOND LOAN PROGRAM

Residual Value Insurance (RVI)

In Credit Tenant Lease (CTL) mortgage loan transactions, the loan amount is primarily determined by calculating the present value of the rent stream during the lease term. Monthly rent payments cover monthly debt service, thereby ensuring that the total rent will be adequate to fully amortize the loan. However, if a balloon payment due at maturity is incorporated into the loan, an element of real estate risk is introduced into the transaction. This is because all the rents have been used for debt service, so if the value of the real estate is insufficient to cover the balloon, the loan is at risk of not being fully repaid. Most investors of CTL loans will not take this risk. Residual Value Insurance guarantees to the investor that, if the property is not of sufficient value to ensure the payment of the balloon, the final payment will be made by the insurer.

Balloon payments on CTL loans can be desirable for a number of reasons. Many leases provide the tenant with an early termination right, which would prevent full-term capitalization of the lease, reducing upfront loan proceeds. The addition of a final balloon payment at the end of the lease term also creates greater loan value than the present value of the lease payments alone. By reducing the amount of rent that needs to be used to amortize debt during the primary term, cash flow to the borrower can be increased or, alternatively, additional debt can be serviced. This latter choice is what most often occurs in CTL transactions with a balloon payment. The RVI guarantee is essentially used to lever up the amount of money that can be borrowed based on a given rent stream.

LesMark Capital, or its insurance consultant, will secure residual value insurance at the request of the borrower either directly through a national provider. The underwriting process involves information and data gathering, data analysis, market and field research, appraiser's reference and dialogue between LesMark, borrower and the insurer. Typically, the maximum amount of balloon balance obtainable is the lesser of $25-$60 per square foot, 15% - 20% of the appraised value, or 60% of the land value, which may be reduced by such factors as the type, quality, age and use of the building. The one-time upfront premium payment for RVI costs approximately 5.0% of the insured amount (balloon payment).

In addition, LesMark also has several hybrid investor clients who will permit a modest uninsured balloon on certain property types in strong markets. There is no up-front cost for this execution, but the spread may be increased a bit to compensate for the additional risk.