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Libor Change Threatens Fixed Rates

Current and Future Loans Impacted

Chris Tollinchi
Financial Analyst

Identifying and Fixing the Problem

It's official. Libor, the standard index controlling over $350 trillion of financial instruments, is scheduled to be replaced by 2021. That is the target date agreed upon by several international governing bodies that include an arm of the Fed. If you have a bank loan with a fixed rate using a swap or are considering such a loan in the future, your fixed rate could become "unfixed" and take an unexpected jump.

Without some proactive attention, there is the possibility that a bank without a conscience could use this event to improve its profits at a substantial cost to the borrower. We have seen loan documents where some banks state that the Libor replacement would be the Wall Street Prime Rate while others use the 10-year Treasuries Rate. The most likely Libor replacement is an index known as SOFR (Secured Overnight Financing Rate). It has the closest value to Libor but it is not equivalent.

As an example, let's take a $15 million loan with a 10-year fixed rate. The most favorable outcome would be an additional cost of $100,000 using SOFR while a replacement using the Wall Street Prime would have an incremental cost of roughly $2 million. Neither is good and one is disastrous.

4 Steps You Can Take To Protect Yourself

So, what are the things you can do to stop this financial global warming from impacting you? Here are four basic recommendations:

1. Be Aware

If you have a loan with a fixed rate, send it for review to a US Government registered Swap Advisory Company. CMAC Partners is one such company but others may be found at https://www.nfa.futures.org/basicnet/. That advisor should be able to examine the replacement provisions both in your loan and your swap and assist you in assessing your risk. If you are considering new financing, look to see if Libor is the basis for a floating rate loan or a loan fixed with an interest rate. Do not let the complexities dissuade you.

2. Negotiate New

Do not move forward with a Libor-based loan until you have negotiated Libor replacement language that creates symmetry between the loan and swap documents and provides you with reasonable assurance of negligible impact. Because this issue is new to many banks, you or your advisor may have to take the lead in providing that language. CMAC's Andy Johnson* has been working with banks for more than two years regarding Libor language. A large national bank has now adopted Johnson's language in its dealings with its proactive clients.

3. Renegotiate or Refinance Existing

Right now the market is highly competitive. It's a good time to sit down with your bank and renegotiate loan terms. That includes loan and swap language on Libor replacement. If you can't reach terms that are suitable to you and your swap advisor, consider refinancing. Remember that you are not tied to that bank by either a negative or positive swap value. You can take those values and move them along with your business. Your certified swap advisor can explain how. In the end, not only may you may end up with a more stable loan but one with lower pricing and greater longevity.

4. Get It In Writing

We have heard too often the refrain from bankers "Don't be concerned. This is way too big for our bank to do something that would negatively impact all these borrowers." Good, then get it in writing. The reality is that the bankers speaking directly to the borrowers are not the policy makers. Even a little tilt in the bank's favor (we can be sure it's not going the other way) can mean substantial loss to the borrowers.

*Andy Johnson is a principal at CMAC Partners where much of his work is implementing suitable replacement language for clients which either mitigates or eliminates the Libor replacement risk. Mr. Johnson may be contacted by phone (407) 264-7264 or by e-mail at andy@cmacpartners.com

On the Back...

On the Inside...

Bringing East Coast Competition to Tulsa, OK with Outstanding Results

The stakes were high as a planned major expansion coincided with a looming loan maturity that would have required refinancing within a very short timeframe. Against this backdrop, Tulsa Bone and Joint selected CMAC Partners to arrange the replacement financing and the new financing for this project in one consolidated debt request for a medical campus that would now reach 150,000 sf. The physicians had always personally guaranteed their real estate debt, but were interested in exploring the possibility of non-recourse financing while increasing their leverage, a challenging proposition.

CMAC Partners approached a number of local, regional and national lenders with this financing request. Surprisingly, in the end it was an out-of-market lender that proved to be the winner on all counts with rates materially below its closest competitor. This lender's medical specialty group was eager to land a marquee client in Oklahoma and Tulsa Bone and Joint, as one of that state's premier specialty groups, fit the bill. It is a practice made up of some of the top professionals in the orthopedic field and run by a highly effective administrative team. The bank also impressed Tulsa Bone and Joint with its depository offerings and flexibility of transition, and the decision quickly became clear. CMAC feels quite confident that Tulsa Bone and Joint now has real estate financing with the lowest spread for any owner-occupied medical group in the entire state of Oklahoma and challenges anyone to suggest otherwise!

Tulsa Bone & Joint | Tulsa, OK

The loan structure also offered some unusual benefits which one would not see in a plain vanilla financing. Although the construction loan was relatively typical, the bank also agreed to allow the refinance loan facility to remain interest-only for 2 years during construction. It will then term out over a 10-year subsequent term (12 years total) with a 25-year amortization. This custom financing not only allowed the refinance facility to nicely match the construction loan, but also allowed for enhanced cash flow during the construction project – a time when surplus cash flow is always welcome.

Real Estate Roll-Ups

Bringing Disparate Ownership Together Takes Center Stage

In a recent orthopedic meeting, no fewer than a half dozen groups approached CMAC's team in search of solutions for an issue that is growing more and more common. "How do we roll up properties that have diverse ownerships so that all of the partners in the practice can have an opportunity to own the real estate as one". Sometimes the disparate ownership is a result of growth within a single practice while a growing number of cases are generated by the merger or acquisition of practices that have pre-established ownership in their real estate.

There is good reason for these groups to seek common ownership. The benefits are immense. Of primary importance is that it allows the practice to make decisions relative to office utilization based solely on what is good for the whole, without concern that the decision may have an economic benefit for one set of doctors while another group suffers an economic disadvantage.

Moreover, it provides an opportunity for all partners in the practice to share equally in the fiscal benefits of real estate ownership where each is already contributing to the real estate income through the practice. Full partner participation also brings the benefit of unifying the practice and eliminating any "have vs. have not" issues or perceived inequity from those that feel the rent is too high. The practice becomes one-minded (at least as far as its rental rates go).

Admittedly, the WHY is easy. It's the HOW that takes a little more work. The biggest challenge is finding a way by which each subset of owners feels that they have received appropriate value for their respective properties in the process of this amalgamation. Once that is addressed, the tax considerations of the different methodologies must be considered.

Fortunately, those seeking solutions do not have to reinvent the wheel. There are others that have come before, and utilizing those experiences can go a long way in deciding what process will best fit your situation and the best methods of implementation. There is no "one plan fits all". But there are a number of now-established protocols where at least one of many should fit.

This very issue hit the CPOMP (Congress of Physician-Owned Medical Properties) agenda at its 2019 conference in Orlando. With CMAC Partners citing examples from case studies of its own clients, physicians discussed the pluses and minuses of various approaches. The takeaway here is that a practice faced with this issue is far from alone. The way has been paved and you need only reach out through organizations like CPOMP to connect with others who have traveled this road.

SALE / LEASEBACK ALERT!

Windfall for Some Partners Leaves Other Partners Footing the Bill

THIS ARTICLE ORIGINALLY APPEARED IN AN EARLIER EDITION AND HAS BEEN BROUGHT BACK BECAUSE OF ITS TIMELY IMPORTANCE.

Greg Warren
Managing Partner

I hate to admit it, but I am old enough to clearly remember The Steve Miller Band singing "Take the Money and Run". I just didn't know that it described the physician-partners who walk away from a debt obligation and leave the repayment for the rest of their partners or, worse, those that may be future partners.

The stage is set whenever a group of partners agrees to pay an above-market lease rate so that a REIT or some other buyer will pay a higher purchase price. The premise is simple. The buyer pays an increased purchase price in return for the seller agreeing to an increased rental rate over the lease term, which is often 15 years or longer. It is likely that idea is flawed from the beginning, as an analysis would show that the present value of the increased rental payments is greater than the premium received. However, there are much greater problems that may occur that can have very serious practical, ethical and even legal implications.

The problem occurs when one or more of the selling members leave the practice (tenant) prior to the maturity of the lease. Let's remember that the retiring member received a premium payment in exchange for their promise to pay a premium rent over the term of the lease. However, when the member leaves the practice prior to the lease term expiring, that member is no longer repaying his or her portion of the rent premium that is still due. That partner or those partners have just ducked out from paying their portion of the tab that is due on the premium received and left that to be paid by those remaining in the practice.

That means the remaining partners' original benefit from the incremental sales value will be mitigated or eliminated by the portion of the premium they now pay (through the practice) on behalf of the partner(s) that "took the money and ran". It is likely that the increased rent will cost the remaining partners more than they received in the first place. Beyond the issue of the original partners is the valid concern of new partners who may question why the practice is paying an above market rent. Moreover, some attorneys feel strongly that the practice is obligated to disclose the over-market rent when recruiting a new physician with the expectation of a partnership. An astute doctor contemplating partnership will see that his or her income would be diminished by that rental premium that had been monetized earlier by the preceding partners.

Although there are methods of re-equalizing the benefits and obligations attached to an above market sale / leaseback, the best thing that a group can do is to recognize that whatever premium they receive will be paid back

with interest to the purchaser over the course of the lease and to make sure that the sale / leaseback occurs at true market rates. If that's not possible, talk to your attorney about claw-back provisions for those retiring prior to the lease term to avoid the outcome as described in this example.

EXAMPLE

A group of 10 partners sell their 40,000 sf building at what amounts to a 6 cap. The market rent is $20 psf but the partners agree to pay a lease rate of $23 psf. That increases the rent / NOI by $120,000 and increases the sales price by $2 million. The lease is for 15 years with 2.5% annual increases. After 5 years, 2 of the partners retire from the practice and no longer share in the obligation to repay the inflated portion of the rent.

The Outcome

In this case, the partners who retire after 5 years will realize a gain of $140,156 while those remaining for the full term will suffer a loss of $17,952, a difference of $158,108.

A Developer as a JV Partner - The Considerations

James Winchester
Finance Associate

The secret that was never much of a secret is out... physician-occupied property is a real estate investment that is constantly near the top of the pyramid when considering returns on risk. Just take a look around at the REITs that want to buy these properties and the banks willing to lend against them. It's no wonder that any developer would love to have the opportunity to invest in such projects occupied by strong practices.

Sometimes there can be a very good reason to join with a developer as a joint venture partner in a property that you will occupy. Other times, you may be better off passing or seeking a partner offering superior terms. The purpose of this article is to help physician owners decide whether or when it is advantageous to have a developer as a JV Partner.

As we go through this analysis there are some very basic rules to always keep in mind:

1. Don't conflate development and investment. They are mutually exclusive and should stand apart. A reputable developer will develop for a fee and will not tie his fees or performance to an interest in the project.

2. In an income-producing property, the value is, for all intents and purposes, the lease. If your group is leasing the majority of the space, you are bringing the majority of the value and that needs to be recognized in any JV negotiation.

3. In any JV, never pay more than you could otherwise negotiate as a renter. Any over-market rent or rent escalator is taking money directly from the practice's pocket with some portion of that going elsewhere.

4. Whenever possible, turn your negotiation into a competition. While the developer may be the most convenient JV partner, you should never lose sight that there are others that might be considered, depending upon the circumstance.

Okay, with those basic rules laid down, let's look at the factors to weigh when considering your developer as a JV partner.

Who's got control?

What is important to realize here is that the developer and your practice may have very different objectives. Control allows you to utilize your property in the manner that is most beneficial to your practice and its partners. From most developers' perspective, your project is a real estate investment. There are numerous ways to marry the objectives such that the developer receives an adequate return while the practice retains control and therefore assures the facility will always be there for the good of the practice. Always make sure that even if the developer owns enough shares to block a supermajority vote, the Operating Agreement stipulates that he or she cannot do so.

Covering the cash equity required

If you find that you need to raise additional capital or simply wish to reduce your investment, don't limit your resources to your developer. There are many sources that are ready to invest and they should be well vetted and made to compete against one another. Again, factors such as control and the ability to buy back your interest should be considered along with the cost. A "Capital Shock Absorber" can bring needed capital during the start of a project when new partners are being recruited, or in the years where there are several retiring partners / redemptions, and the other partners don't want to put up the cash. Investigate the opportunity to pre-agree that the developer is willing to be bought out down to a minimum investment.

Shedding guarantees

If risk aversion is a priority, a strong development partner may be able to guarantee the debt and relieve the practice or its members from that requirement. This is often a good quid-pro-quo when considering the respective value brought by the partners.

Investment experience factor

Some developers bring value above and beyond that of just completing the development of a building. If we wanted to explore an exaggerated metaphor of this situation, we could investigate a start-up seeking a willing investor to support the company's founding vision. Any entrepreneur would tell you that the experience and connections that investors bring to the table are worth far more than the check that they may or may not write. If a developer is willing to nurture and support your real estate venture and has the proficiency to add long-term value, then it may be worth considering giving them a slice of the pie. Look for someone who wants to build value with you and has lots of references to prove it.

Leasing unoccupied space

If you are building a project that is speculative in that there is a decent amount of unleased space, a partnership with the developer may be an appropriate way of sharing the risk and assuring yourselves that the risk is warranted.

The developer's land

This last one is perhaps the poorest and most overused reason to either utilize the owner as the developer or to enter into a JV. The land should be valued and negotiated on its own merits. Steve Dobias of Somerset CPAs shares the following advice with his physician clients. "When considering the purchase of a site, do not go out to visit the site in a lab coat." When a seller sees a doctor on site, the price of the land just went up.

Hopefully, some of what is discussed here can be kept in mind and help assure that any developer JV entered into is equitable and for all the right reasons.

Reducing Personal Risk While Increasing Real Estate Debt

MOB/ASC Refinance Creates Layers of Benefits for the Owners – Some More Obvious Than Others

Andy Johnson
Principal

I know, it sounds strange, doesn't it? Counterintuitive even. Well, a real estate holding company comprised of physicians from Desert Orthopedics and Bend Surgery Center, in Bend Oregon have refinanced their primary facility and thus reduced risk as one of the many benefits of this unique refinancing transaction. How was the risk reduced? Asset protection! Increasing debt monetizes equity; cash goes into the owners' pockets. If the lender can never reach back into those individuals' pockets, those owners now have better protected assets than exposed equity in a financed building.

As we all know, when a building is used as collateral for a loan, the lender has a lien against the building. In the doomsday scenario (foreclosure) the bank can take that real estate. However, a bank's rights to collect certainly does not end there – commercial (entity) and personal guarantees often act as another potential source of repayment for bank.

Bend Surgery Center | Bend, OR

An oft-coveted distinction for an owner-occupied medical real estate loan is to have no personal guarantees. The elimination of hat contingent liability helps the worriers amongst us sleep better at night. Non-recourse financing (from a personal owner standpoint) is often accompanied with a guaranty of the related practice and/or surgery center tenant to provide sufficient credit support for the bank. So, this operating entity that the physician may well also own does typically have a layer of exposure.

However, in the case of the Bend Surgery Center/Desert Orthopedics financing, that was not the case! This pure non-recourse financing only required the guaranty of the sub-entity building owner entities. This absence of meaningful guarantees makes a cash-out refinance that much sweeter – not only are the owners receiving a cash windfall, the funds are also forever out of the reach of the bank whether held by their practice or by them personally.

All that said, a truly successful refinance rarely accomplishes just a single objective. In addition to asset protection, the cash out enables the ownership groups to more easily re-syndicate ownership. They had struggled for years with the unaffordability of integrating new partners, but that is no longer the case. Additionally, despite borrowing significantly more debt, an unusually long amortization (30 years) and aggressive pricing helped to keep the monthly payment low resulting in a greatly improved return on equity. The ownership was thrilled with the obvious economic outcomes. The additional asset protection was certainly an added intangible benefit that was less blatant, but also tremendously valuable.

“Bespoke” Financing Creates Optimized Outcomes

Custom Fit for Borrowers

Andy Johnson
Principal

The Gentlemanual describes the process of procuring a bespoke suit as follows: “A unique, perfectly tailored suit is not an immediate thing… to get a perfect bespoke suit; you will have to work (with your tailor, of course) for it”.

The same is true for medical real estate financing. A borrower can get a loan off the rack with a predictable term, repayment structure, and basic elements. But it is rare that these standard lender offerings will provide features that are completely in sync with the borrower’s and related operating entity’s complex goals and objectives. Most often, there are some adjustments that should be made to make that financing fit really well.

CMAC has found that, more often than not, medical borrowers tend to go to banks and accept an “off the rack” financing proposal that might work fine for some other businesses but could definitely use some tweaking to make it a much better physician-owned real estate fit.

Well, that’s changing. CMAC Partners, the physician’s financial tailor, is reporting significant interest in creating bespoke financing across the country, which is giving physicians a better fitting product than ever before. Here are three adjustments that seem the most frequent:

1. Cash is king:

Strong cash flow from a real estate investment is often top of the list for borrowers. CMAC has therefore been tasked on a number of recent financings with minimizing the monthly payment during a refinance process. What would be the off the rack option? It would be a 20 or 25-year amortization (some of the longer repayment structures typically available on commercial financing). CMAC has gone a step further with two recent closings with unusually long 30-year amortizations for medical borrowers in Bend, Oregon and Denver, Colorado.

Additionally, CMAC has been able to negotiate and close upon two recent refinance facilities that allow the real estate debt to sit interest only for 2 years – a Urology group in Tennessee and an Orthopedic group in Oklahoma. For those groups, minimizing the equity in the building to allow for more affordable future partner buy-ins was important – these custom repayment structures accomplished that beautifully.

2. Taxes matter:

A key goal for many borrowers is to mitigate or eliminate personal guarantees and CMAC accomplishes this routinely for its borrowers. However, a cardiology group in Colorado had a more complex objective. They wanted to minimize personal guarantees, but their CPA had informed them that eliminating the guarantees would have tainted the “Qualified Non-Recourse” status of the loan and would have resulted in a sizeable taxable event for the physicians

in varying degrees. Having consulted with the borrower’s advisors, CMAC determined the minimum level of guarantees to avoid the taxable event altogether.

CMAC then encouraged lenders to allow this minimum level to be selected by owners if they wished, or choose any amount of guarantee above this as needed to avoid the taxable event. Each owner had only to guarantee the minimum necessary percentage with different owners guaranteeing different amounts. Truly a custom structure and it fit this group like a tailored glove.

3. Planning for future acquisitions:

CMAC has now arranged several “reducing revolver” facilities for borrowers who are very active in real estate acquisitions. One such loan this year refinanced multiple properties owned by one borrower. Anticipating the eventual addition of some properties and the sale of others, using 1031 exchange, the Borrower wished to avoid repeated re-negotiations and additional financing costs. Under this structure, the Borrower will be able to draw up to the aggregate limit of $33 million but only pay interest on the amount actually borrowed. The only collateral is the ever-changing pool of properties.

These are just three of hundreds of unique financing structures that I have negotiated on behalf of my clients. With an ever-evolving repertoire of loan features that can be integrated into a real estate loan and with the right fiscal tailor, your loan should fit you like a glove and put you in a better financial position than was thought possible.

CASE STUDY

Renter to Owner: Changing the Doctor’s Mentality

Overwhelming Participation a Result of Good Education

Let’s play Jeopardy. The category is “Physician-Owned Real Estate” and the answer is “Make It Mandatory in Your Practice’s Operating Agreement”. The question? “How do you get all the members of your practice to become owners in the practice’s real estate?”

Wouldn’t it be easy if we could turn back the clock and have the foresight to include such a provision? Everybody’s on board. Problem solved. Unfortunately, most of us don’t have that luxury and instead face the unenviable challenge of convincing our partners to come on board. The risk is that such an opportunity could turn into a divisive issue unless a preponderance of the partners decide to invest.

Tennessee Orthopaedic Alliance, Nashville’s leading orthopaedic group, had historically leased the property from which it practiced. However, in 2018, the group’s leadership decided to invest in a satellite office to be constructed in a Nashville suburb. The decision was not initially embraced by many of the partners who were quite comfortable as a tenant with a renter’s mentality and viewed such an investment as uninteresting or even an unnecessary risk.

So how did TOA manage to bring 45 of 50 partners on board? – they educated them! The TOA leadership arranged a series of meetings so that every partner had the opportunity to attend. Present at those meetings was the project developer along with CMAC Partners who put together a presentation that detailed the investment, the returns, the methods of buy in and buy out and the risks. The partners were able to ask any and every question that came to mind and, in the end, were able to make fully-informed, individual decisions as to whether or not to invest.

The decisions by some were further facilitated by personal bank loans made available through CMAC such that most of the cash needed for each partner’s investment could be borrowed, knowing that the cash flows from the rent would pay both the monthly payments on the personal loans and the taxes on the cash flows… even in the first year. Each year thereafter, those partners would continue to gain equity through repayment of the loan and would realize cash out as rents escalated.

The financing was concluded at a lower-than-estimated loan spread that provided outcomes that surpassed those that had been presented. TOA is already anticipating its next project and CMAC will be ready to participate in the fiscal education of its members when the time comes.

Tennessee Orthopaedic Alliance | Nashville, TN

SOUTH DENVER CARDIOLOGY

Littleton, CO

$21,840,000

Restructured financing for more sustainable partner integration with cash-out to partners and enhanced cash flow. Fixed 10-year rate.

UROLOGY ASSOCIATES

Nashville, TN

$13,500,000

Negotiated significant rate reduction with incumbent bank on 12-year fixed rate. Substantial savings and cash-out for the physician partners.

RENO ORTHOPAEDIC CLINIC

RENO, NV

$7,280,000

Refinance of satellite location with new financing for construction. 100% loan-to-cost. No cash-out-of-pocket from the physician partners.

COLUMBIA ORTHOPEDIC GROUP

Columbia, MO

$35,000,000

Arranged 100% financing for expansion project while simultaneously simplifying debt structure and collapsing negative swap and redemption of bonds.

AUGUSTA ORTHOPAEDICS

AUGUSTA, GA

$7,515,000

Refinanced an MOB and ASC with a fixed-rate over a 10-year term without any personal guarantees to the individual owners.

OSS ORTHOPAEDIC HOSPITAL

York, PA

$53,700,000

Refinanced existing debt over a 12-year term with cash-out to the partners to fund new MOB project without personal guarantees from the physician partners.

PALM HOLDINGS

Boca Raton, FL

$33,000,000

Negotiated a "Reducing Revolver" loan to refinance multiple properties with ability to add additional properties and draw up to the aggregate limit.

BEND SURGERY CENTER

Bend, OR

$17,600,000

Refinanced and extended for 10 years without any personal guarantees while distributing cash to physician-owners.

Blend & Extends - Everyone Wins…But the Bank Wins More

By JP Conklin, President, Pensford

Swap modifications create an opportunity for banks to generate additional revenue. Most borrowers are aware that swaps generate revenue at execution and in the event of an early prepayment, but banks also capture revenue when things like the start date, amortization, or balance are modified. But without a doubt, the opportunity to generate the most revenue comes in the form of a Blend & Extend.

A Blend & Extend ("B&E") usually arises out of a situation where a loan and swap are close to maturity, most commonly less than two years. The bank offers to simultaneously extend both the loan and the swap. Frequently, the bank will be able to lower the fixed rate, making it look very attractive to the borrower. The borrower gets a new long-term fixed rate and avoids paying the swap breakage cost.

Everyone wins... but the bank wins more.

Let's consider an example. In 2011, let's say a borrower locked in a 10-year fixed rate at 5.75% on $25,000,000. Assuming a typical credit charge at closing, this swap would have generated about $650,000 in swap revenue for the bank.

Today, the borrower is interested in refinancing to take advantage of lower spreads, but there's a breakage cost associated with the swap. If the borrower terminates this swap today, it would cost approximately $700,000.

The lender comes to the borrower and proposes a new 10 year rate at 4.90% and reassures the borrower it won't cost any money to break the swap. Get a new 10-year loan, lower the rate by 0.60%, and pay nothing out of pocket. The bank keeps the loan and the borrower extends the loan with a lower rate.

Everyone wins… but the bank wins more. This creates an additional $650,000 for the bank. That's a total of $1.3mm in swap revenue for the bank since 2011.

If real estate values have increased and the group wants to increase the loan amount, the bank can actually lower the rate even more. For example, if the loan amount increases to $33,000,000, the rate could be lowered to 4.75%. Extend the loan, lower the rate, and take cash out.

Everyone wins… but the bank wins more. The bank probably won't lower the rate to 4.75%. Instead, they will lower the rate to 4.85% and generate $950,000 of additional revenue instead of "just" $650,000.

Blend & Extends have several moving parts, which makes it challenging for borrowers to isolate and identify each piece of potential profit. This makes it easier to focus on the rate being lowered and believing they are getting a fair deal. Some of the moving parts include:

-true breakage cost of the existing swap
-true breakeven rate on the new swap
-true cost of blending the existing breakage into the new swap
-reasonable and fair swap revenue on the new swap

It is important to work with a firm that can help isolate, quantify, and negotiate each component of this structure. As a client of ours once said, "I'm fine with the bank making money, I just don't want them running around the trading floor high fiving each other."

A great deal is one where everyone wins… but there's no high fives.

PENSFORD

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JP Conklin is President and founder of Pensford in Charlotte, NC. Following his tenure as Head of West Coast Derivatives for Wachovia Bank, JP left to form Pensford in 2009 to help borrowers create hedging strategies that strike a balance between flexibility and cost while mitigating exposure to interest rates. JP has negotiated and executed over 800 derivative transactions with a notional balance in excess of $75 billion. His unique experience and institutional contacts also provide insight into less well known factors, such as counterparty credit hedging, calculating hedge exposure, back to back swaps, and ISDA negotiation. This translates into increased transparency and improved pricing for Pensford clients.

What CMAC Clients Have to Say...

My deepest thanks to you for your skill and partnership in this project. I echo the gratitude from Barbara and Brian. I know I would not hesitate to engage you again in the future. Warm thanks.

Dr. Jeff Douglass
The Oregon Clinic

It was a pleasure working through this transaction with the CMAC team. It was a massive undertaking with everything involved but it made the process for me much easier with you on our side! It is always a pleasure working with such diligent and professional people like yourselves.

Amy Gunsaullus, Finance Manager
Palm Holdings

If anyone is looking to do some refinancing or new construction or remodeling ... these folks saves us $1M on a refinance and shortened the term of the loan. They did all the work for us. Good, trustworthy, smart folks.

Rob Blair, CEO & President
The Spine Hospital of Louisiana

You did an amazing job with these complicated loans.

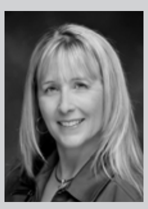
Dr. Renny Uppal
Reno Orthopedic Clinic

I really appreciate you facilitating these efficient calls. You make a cumbersome process seem streamlined! A big thank you to CMAC as well! You all have been wonderful to work with.

Sami Spencer, CEO
Missoula Bone & Joint

Thank goodness I have people like CMAC looking over the documents and making sure all is in order! Thank you!

Cindy Keene, CEO
Lewiston Orthopedics



My partners are still smiling; our deal is progressing nicely and we continue to receive compliments about the outcome. I wanted to thank you all for your patience with our process. You certainly tailored a process that resulted in us meeting our goals completely. We reached the conclusion with even stronger bonds to our bank and an excited and cohesive group of active partners.

Dr. Charles Eckstein
Urology Associates, P.C.

Your team is the best!

Debbie Eldredge, EVP & COO
Pacific Cataract & Laser Institute

Thanks for walking through this process with us. Took time but we finally got over all of the hurdles. Great job on the rates and SWAP documents. Appreciated the input as well as the overview of all the legal financial documents. Look forward to working together in the future.

David Blaeuer, CEO
First State Orthopaedics

It is clear CMAC has a genuine interest in seeing our real estate endeavors succeed. I don't think we'd be where we are with this project without the hlep of CMAC, especially regarding the swap and having a team who truly handles these kinds of deals and can provide valuable feedback on business terms.

Chuck Williams, CFO
Tennessee Orthopaedic Alliance

How to Use Your Swap Values

Positive or Negative – You Can Help Yourself

Liz Allport
Partner

Here's a bit of a secret. Your interest rate swap carries a constantly changing value over its life and sometimes those values (positive or negative) can be very useful. It all depends upon your objective. The chart below shows what you can do with a meaningful value in either direction. However, like the warning that magicians offer to kids, "don't try these tricks at home or without supervision." In the case of swaps, beware of modifying or terminating without the advice of a professional. Here's something to always keep in mind. Every time a bank touches a swap, it creates an opportunity for unseen additional bank profit at the expense of the borrower. Your swap advisor will make sure that you receive maximum value with no or minimal expense.

Use the Positive Value to	Use the Negative Value to
Pay down principal* The borrower may choose to apply the positive value of the swap against the loan balance and either float or replace the swap at current market rates. This reduces overall interest expense and can be very helpful if the borrower is looking to reduce its debt to get under a certain Loan-To-Value threshold.	Reduce monthly payments (option 1) The borrower could reduce its monthly payment (often dramatically) by terminating the swap and adding it to the principal balance. Now, instead of having to pay the negative value during the remaining term of the swap (probably the same as the loan term), the negative value is spread over the amortization of perhaps 20 or 25 years.
Make partner distributions* The swap could be terminated and the proceeds could be distributed to the ownership group. Again, the swap could be replaced at market rates or the debt could float.	Reduce monthly payments (option 2) The borrower could reduce its monthly payment by blending the negative value of the swap into a longer-term swap, thus effectively extending the repayment period.
Fund new construction Swap proceeds could be used to fund all or a portion the equity requirement on a new project, eliminating or mitigating the need for a capital call.	Avoid paying for the unwind out of pocket when refinancing When refinancing, the swap unwind can be blended into the new fixed rate as opposed to adding it to the loan amount.
Lower the rate on new financing The positive value of the swap could be applied to the fixed rate of a new loan to lower the rate.	
*It should be noted that the termination of a swap may be limited under the terms and conditions of some loan agreements. If you are unsure, CMAC will review your documents and advise you.	

CASE STUDY

Colorado's Top Cardiology Practice Solves Fiscal Puzzle in a Heartstopper!

South Denver Cardiology | Littleton, CO

How does Colorado's preeminent cardiology group go from contemplating the sale of its iconic building to executing a new strategy that benefits all partners in less than a year? Through a highly innovative financing package that leveled the playing field for every doctor in the practice. This was an outcome that could have only happened with great leadership from the group's long-standing executive, its savvy medical director and the expertise and persistence of a determined team from CMAC Partners.

Why sell?

It seemed like the best possible alternative at that moment. South Denver Cardiology (SDCA) had run into two primary issues. The first was that there had been a substantial buildup of equity that had not been realized by the longtime owners. The second was caused by the unique waterfall ownership structure that allowed for the second set of members to buy in without cash equity, creating some real complexities as the third group of partners considered membership. The system involved layers of distributive rights. The mounting concern was that inequities between ownership levels could begin to divide the objectives of the group as a whole.

The Solution

Ironically, it was SDCA's original developer who introduced CMAC Partners to SDCA with the objective of finding a solution that would allow the group to maintain its ownership in the building. The only way to reach this outcome involved assisting each of the current ownership levels to capitalize on their respective equity buildup and bring in the new partners at a minimized equity requirement.

After several months of hard work on all sides, CMAC was able to present proposals that provided a truly exceptional outcome. In the end, the original partners were each able to receive a very substantial distribution. The second level of owners also received a good sum of cash while applying sufficient value to equalize their standing with the original owners. Finally, the newest level of partners came in with a much smaller equity need and all members are now able to enjoy the same benefits moving forward.

The extraordinary part of this financing was that CMAC was able to structure this unique and highly competitive package with SDCA's own incumbent lender. This was a great example of what good people working together can accomplish. While CMAC may have found the path, it was the long-standing relationship between SDCA and its lender that made the problem-solving journey possible and created present value savings in interest expense of more than $1.5 million along the way. Now that's teamwork!

Shared Benefits Payouts Hit $100,000

$5,000 per and Everyone's a Winner

Sirena Madden
Principal

In the mid-1900s Groucho Marx had a game show in which he told the contestants to "Say the magic word and a duck will give you $100". Well, inflation has upped the ante a bit. It's now $5,000, there's no duck and there's but a single secret word, it's "CMAC". In fact, so many people have been repeating it that CMAC has now paid out more than $100,000 to those reciting it while saving millions for those hearing the magic word for the first time.

The dollars are paid out under a program in which it is easy-to-participate, known as "The Shared-Benefits Program. To get started, one needs only to make an introduction between CMAC and an independent group of physicians and let CMAC take it from there.

The great part is that payments starts almost immediately with a $1,000 check once the group is deemed qualified. By the way, "qualified" just means that the doctors have a controlling ownership interest in their practice's real estate. Another $1,500 is paid out if the group engages CMAC and then $2,500 additional is paid at the time of the loan closing. All that while the new CMAC client is reaping benefits worth 6 or often 7 figures. It truly is a win-win-win.

Say the Secret Word

Truth be told, most of those saying the secret word have been past CMAC clients who already understand the benefits CMAC can bring and are eager to share their experiences. However, a growing number are just people who have heard about us and our results, and are happy to make an introduction. Whatever group you fall into, it's a great time to speak up and say the magic word. To make it happen just call Sirena Madden at (407) 264-7258 or email sirena@cmacpartners.com.

Sell versus Hold

The Solution When Both Answers are the RIGHT Answer

THIS ARTICLE ORIGINALLY APPEARED IN AN EARLIER EDITION AND HAS BEEN BROUGHT BACK BECAUSE OF ITS TIMELY IMPORTANCE.

Peter Kokins
Business Development

It's a great time to be a physician-owner of the medical property housing your group, ASC or hospital. The continued credit worthiness of healthcare tenants has translated into aggressive purchase offers for those properties and the perpetual question; do we hold or do we sell?

Unfortunately, there generally is not a clear-cut answer because what may be the proper decision for one partner may be the wrong decision for another. Here is what is generally known.

SELL

If a partner is going to be leaving the real estate entity within the next three to four years, it may be best to sell. Further upside is limited in that short time frame and this could be a missed opportunity if the market turns.

HOLD

If a partner is going to be in the real estate another 7 years, it is generally better to keep ownership, taking continued cash flows, as the returns would not be able to be matched outside the closely held investment.

Those in the middle might find reasons to go either way. Unfortunately, the building, much like the baby in the story of King Solomon, can't be divided with half being sold and the other retained… or perhaps it can?

The continued low interest rate and high loan-to-value environment enabled the creation of unique financing structures that can provide assurance of a buyout at the offered price while retaining ownership for the remaining members at returns that continue to eclipse other like investment options. As important, the management of the property continues under the sole discretion of the practice partners to be run for the benefit of the practice.

The price is generally set in accordance with the agreed cap rate of the bona fide offer, making sure that the lease terms are within market. The buyout can come immediately or at a date set in the future and at an agreed price that is in line with the current offer. And the financing is structured to accommodate the terms of the buyouts. For further information, contact Peter Kokins at 407-264-7255 or at peter@cmacpartners.com.

Design Dollars… How Every Second Counts

FACT: Flow design solutions that save as little as 1 or 2 minutes on each patient visit will create a significant economic impact. It's why we have spent years perfecting flow design solutions that save our clients just a few seconds here and there throughout the patient visit process. Consider this example of just how much a few seconds matter.

Assuming a typical provider sees a patient on average every 15 minutes, that nets 32 patients visits a day. If the flow design can save a minute per patient throughout their visit, 32 minutes can be saved throughout the day. An extra 32 minutes equates to 2 extra patient visits per day without changing anything but the flow design. These 2 extra patient visits are therefore at little to no additional cost and thus can be considered pure profit. An extra 2 patient visits a day nets 480 additional patient visits a year at no additional cost. This indeed represents significant additional revenue. If the flow design can save 3 patient visits per day the additional annual patient visits jumps to 720. And if the flow design can save 4 patient visits per day the additional annual patient visits jumps to 960. That represents an approximate 6-12% revenue increase with no additional costs.

The nice part about good flow design is that the providers and staff do not even know it is happening to them. They simply go about their day as usual but because they are moving 6-12% more efficiently they can do more in the same amount of time. The facility represents only 8-12% of a clinic's overhead costs while staff represents a staggering 40-60%. We have estimated that particularly well-designed flow design solutions allow the 8-12% to make the 40-60%, 6-12% more efficient. The same savings can be replicated for ASCs and hospitals. Make every second count!

John A. Marasco, AIA, NCARB

As a principal/owner of Marasco & Associates (Denver, CO), John oversees the design/development of over 250,000 square feet of healthcare architecture annually. Mr. Marasco is a nationally known lecturer on the design/development of healthcare facilities from physician practices to hospitals.

CMAC Gives Back

Every year, CMAC Partners collaborates with non-profit organizations that are working to build a stronger and supportive community. Hailing from Winter Park, Florida, the CMAC team participated with three local organizations to help those in need in the Central Florida area.

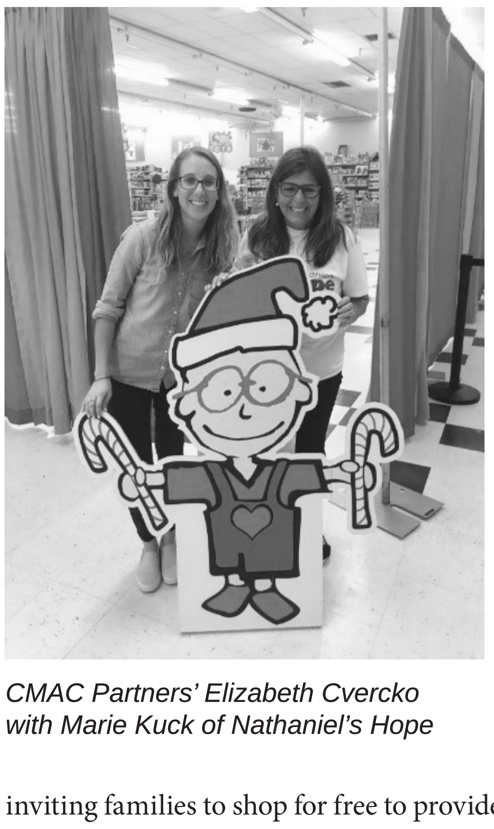
Second Harvest Food Bank

Second Harvest Food Bank of Central Florida is a private, nonprofit organization that collects, stores, and distributes donated food to more than 550 feeding partners in six Central Florida counties. Second Harvest offers programs such as a 16-week culinary training program to help at-risk, economically-challenged adults learn valuable life skills, in order to set them on a path to self-sustainability. CMAC contributed to and attended one of Second Harvest's Chef's Nights, "Wine, Cheese and Chocolate: A Perfectly Paired Dinner," hosted by three local wine, cheese, and chocolate vendors. The evening benefited the Darden Foundation's Community Kitchen's Culinary Training Program.

CMAC Partners' Sirena Madden at Second Harvest's Chef Night

Nathaniel's Hope

Marie and Tim Kuck lost their son in 2001 at the early age of 4 years old. Born prematurely, Nathaniel suffered from multiple birth anomalies, beating the odds time and time again before ultimately losing his battle. Through their personal experience, his parents saw first-hand how demanding it can be to raise a child with special needs and decided to found Nathaniel's Hope in Orlando, FL. The organization has evolved to offer multiple programs to benefit families with children who have special needs. One such program is "Christmas with Nathaniel's Hope." Every year, Nathaniel's Toy Shop opens, inviting families to shop for free to provide their kids with a wonderful Christmas. The CMAC team stepped up to donate toys. We visited the Toy Shop and met Marie Kuck, who works tirelessly to help families celebrate the lives of their children with special needs while making things a little easier for their families.



CMAC Partners' Elizabeth Cvercko with Marie Kuck of Nathaniel's Hope

SOS - Support Our Scholars

CMAC Partners donated to a worthy program called: SOS Support Our Scholars. This non-profit organization provides financial and emotional support to disadvantaged young women who are at the top of their graduating classes in high school. Each scholar is paired with a mentor who remains with her throughout her college journey. CMAC's donation will be used to sponsor a young woman in the State of Florida throughout her college career. This young lady had been orphaned and was homeless, yet excelled in her high school studies through hard work and determination. CMAC will follow her journey through her four years of college, making sure she has the resources to buy books, clothing, and take part in extracurricular activities.

SOS SUPPORT OUR SCHOLARS
Changing Women's Lives One Degree at a Time

It's What You Don't See That Matters

How Obscure Loan Terms Could Cost You Millions

It's the biggest no-call of all time. This one play that went unseen meant that the New Orleans Saints sat home in 2019 while the Los Angeles Rams went to the Super Bowl… but what's that got to do with your loan? It's a perfect example of how much of an impact what you don't see can have upon your real estate investment. Let's mention just three to demonstrate how much of an impact those terms can make.

#1 – SWAP SPREAD – is the iconic "killer no-see-um". Borrowers will work with great diligence to negotiate a loan spread and never even realize that there is a swap spread that will also be added and which can also be negotiated. While you see the loan spread (it's stated right in your promissory note), the swap spread is rarely even mentioned in the loan documents. Rather, it is simply included in the fixed-rate cost presented by the bank. How big of a deal can it be? In instances when the borrower does not have a swap advisor, banks might add up to 40 or 50 basis points to the cost. On a $20 million loan with a 10-year term, that's added bank profit of $800,000 that you will be paying over the term of the loan. It's tantamount to the bank proposing an origination fee of $800,000, or 4 points. This swap spread can be reduced much closer to break even when using a registered CTA (Commodity Traders Advisor) like CMAC Partners. A registered CTA knows what the swap cost should be and how to negotiate so that the borrower has transparency.

#2 – BREAK FUNDING – is a term that is now frequently used and applied along with its cousin "Yield Maintenance" in lieu of the more traditional prepayment penalties (e.g. 2% of the remaining principal balance). However, the outcomes can be very different and every buyer needs to be aware of just how the Break Funding or Yield Maintenance formula proposed in their loan document is calculated. If you are not represented, our best advice is to ask your banker to walk you through the formula and then provide you with four examples which should be attached and made a part of your loan agreement. Request examples of short-term and long-term prepayments (e.g. 2 years and 5 years), assuming a 50-basis point swing in either direction from the curve. Once you understand the potential exposure, you will be in a much better position to negotiate and decide which type of prepayment penalty works best for you.

#3 – COST OF FUNDS – is a fancy way of a bank saying that they will charge you whatever they feel is appropriate. They might as well be a car dealer selling you some agreed amount "over invoice". Proceed with caution! Make sure that any Cost of Funds agreement contains a clearly defined benchmark in the document such as a 10-year Constant Maturity Treasuries rate, Wall Street Prime, or 30-day Libor. Once you have that benchmark and the bank's spread from that benchmark, you will be in a position to negotiate a loan spread that meets your objectives.

These are just a few of many examples of loan terms which can be invisible to the borrower. Best advice? Get advice! CMAC Partners will review loan documents for CPOMP members for a low flat fee as a benefit of membership. Go to CPOMP.org.

CPOMP Emerges: Empowerment and Enlightenment of Physicians

Physician-owned real estate has been a rapidly growing segment among the ancillary income streams available to physicians. Of those, it may represent the largest investment of all. Yet until 2018, physicians who owned their real estate operated within a veritable vacuum when it came to having some sense of how to control and optimize all of the elements that determined just how productive that investment would be. Then came CPOMP. Let the knowledge sharing and leverage begin!

The Congress of Physician-Owned Medical Properties (CPOMP) is an invitation-only organization comprised exclusively of physicians and medical groups that have, or are planning, meaningful investment in the real estate from which they practice. CPOMP got its start in the spring of 2018 when physicians and executives of 62 independent practices met in Orlando, Florida. They exchanged information and discussed issues that pertain to physician ownership of real estate and the relationship between the real estate ownership and the related practice. Among the topics covered were:

- Partner Integration – Methods of Buy-ins and Buy-outs
- How to Improve Cash Flow
- Accounting, Tax, and Legal Issues
- Financing – Who Is Getting What Terms
- Real Estate Considerations in a Merger, Acquisition, or Integration
- Planning a New Project

The combination of peer-led panels and networking resulted in a collaborative and educational atmosphere that increased the awareness of all in attendance. It resulted in a commitment to continue to exchange information, to grow the organization and to leverage the combined strength of CPOMP for the benefit of all members.

Since that initial meeting, membership has grown dramatically. The CPOMP team has begun a sustained effort to create additional communication and information-sharing benefits through its website. The site now includes features such as a Resource Library, Discussion Boards, Service Provider Reference Portal, and Strategic Partner Discounts. The third CPOMP Annual Meeting will take place April 2020 in Orlando, FL.

Visit www.CPOMP.org or email info@cpomp.org for information about membership for your group.

CMAC Partners

The CMAC Team would like to thank its readers and contributers. We hope this newspaper serves as a valuable resource to you and your practice.

Top row: Elizabeth Cvercko, Andy Johnson, & Shannon Simmons
Middle row: Peter Kokins, James Winchester, Sirena Madden, & Liz Allport
Bottom row: Chris Tollinchi, Inga, & Greg Warren

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