BRIDGE LOANS

Frequently Asked Questions

Q1: How exactly does bridge financing work?

A1: Bridge financing allows a homeowner to buy a new primary residence without needing to sell their current home first. This type of financing uses both the new property and their existing primary residence as collateral for the loan. After the homeowner sells their current home, they either pay off the bridge financing completely with the proceeds, or they pay down the bridge financing and refinance the remaining balance into conventional financing, known as a "take out loan."

Q2: How do we determine the maximum amount of bridge financing available?

A2: The first guideline is we can finance up to 70% (75% on exception) of the combined values of the current property and the new property, less any current loan amounts.

Maximum Loan Amount = (Current Home Appraised Value + New Home Purchase Price) * 0.70 – current loan balances

The second guideline is that the loan amount can never exceed the purchase price of the new home, regardless of the result of the above equation.

Q3: What are the income requirements? Do homeowners have to qualify with both mortgage payments?

A3: There are no debt-to-income ratio requirements or any minimum credit scores or specific asset requirements for the bridge loan. We do need to make certain that they have sufficient assets and/or income so that making the bridge loan payments does not put them in a difficult financial position. If they will need take out financing after their current home is sold, we do need to make certain that they qualify for the refinance based on their income, assets, and credit.

Q4: What are the benefits to a homeowner of using bridge financing?

A4: The main benefit is that it allows them to buy another property non-contingent upon the sale of their home. This can allow them to make a more competitive offer, can alleviate the stress of needing to sell their home first without knowing where they will move to, and it can allow them to sell their home vacant and staged (which may get them a higher sales price on their home). Many people find a lot of value in being able to buy first and then take some time moving all of their belongings to their new home rather than having just a few weeks to pack up and leave. There are some homeowners that would have the ability to buy a new home without selling their current home first by paying all cash rather than obtaining bridge financing. Depending on where their money is held, this could lead to capital gains and/or income taxes that end up costing them more than the costs of the bridge financing. It is definitely worth it for them to consider bridge financing as opposed to paying all cash!

Q5. How long does the homeowner have to sell their current home?

A5: There are two terms offered: 6 months and 11 months. The term is the length of time the homeowner has to pay off the bridge financing. If a 6 month term is chosen, there should be a very high level of confidence that their current home will be sold and closed within 6 months.

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Q6: ***What are the rates and costs?***

A6: The interest rate on a bridge loan is 8.95% (The Annual Percentage Rate, which factors in closing costs, is 13%-16% depending on loan amount). A bridge loan has all of the standard title, escrow, appraisal, underwriting fees that a conventional loan would have. In addition, a 6 month bridge loan charges 2 points at closing and an 11 month bridge loan charges 2.5 points at closing. (2 points = 2% of the loan amount)

Q7: ***Why are the costs associated with bridge financing higher than a conventional loan?***

A7: There are two primary reasons for this. First, bridge financing carries a considerably higher amount of risk than traditional financing. There aren't any debt-to-income ratio requirements, minimum credit scores, or specific reserve requirements, and there is the risk that a property won't sell. Second, when a lender loans money for a conventional loan, there will be income generated up to 30 year from the interest on that loan. Bridge loan are designed to be short term financing that gets paid off quickly. For it to make sense for a lender to offer bridge loans, points are charged upfront since interest will be collected for a very short period of time.

Q8: ***What are the monthly payments on a bridge loan?***

A8: The monthly payment is the Interest Only payment based on the outstanding balance at 8.95%. For borrowers with considerably more equity than the minimum required, they may be eligible for the "deferred payment option," which means that they do not need to make any monthly payments on the bridge loan. The interest gets added onto their loan balance, and it gets paid off when their current home sells and the bridge loan is paid off.

Q9: ***Are there any pre-payment penalties?***

A9: No, there are no pre-payment penalties. The bridge loan can get paid off as soon as the current home is sold. If the homeowner only has the bridge loan for one month, then they only pay the 8.95% interest rate for one month.

Q10: ***Does the bridge loan just provide the down payment to be used on a conventional loan?***

A10: No, a bridge loan does not just provide the down payment to be used in conjunction with traditional financing. The bridge loan finances the entire purchase.

Q11: ***Do both properties have to be in California?***

A11: Their current property must be in California. If they are moving out of California to another state, there is a different program available with different terms, and it only uses the current property as collateral for the loan.

Q12: ***How is a bridge loan different from a Home Equity Line of Credit (HELOC)?***

A12: A HELOC can be another, potentially less expensive, solution for a homeowner to access the equity in their home. However, since HELOCs use only their current property as collateral for the loan, they will have lower maximum loan amounts. In addition, HELOCs have debt-to-income ratio requirements, so not all people will qualify. If a homeowner has an existing HELOC in place with an available balance, that can be used to make a down payment and reduce the amount of bridge financing needed. For example, if a homeowner has an existing $200K HELOC available and is buying a $1M property, they can use $200K as a down payment and only borrow $800K on the bridge loan. This reduces the amount they pay in points and interest paid.

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