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Gap Financing Leads to Economic Development

By Andrew W. Gordon, President, Arizona MultiBank CDC

The 18 banks that formed the \$10 million Arizona MultiBank Community Development Corporation (MultiBank) found success when they joined together 16 years ago to form a single entity. The entity was designed to spread risk and expense and concentrate expertise in the delivery of a special brand of community development financing. Today, MultiBank lent its initial investment nearly four times and continues to actively support emerging and underserved local markets in Arizona.

Started by the Arizona Bankers Association, MultiBank is a nonprofit corporation formed with a stock-like capital debt security, funded on a long-term basis by Arizona lenders, and certified by the U.S. Department of the Treasury as a community development financial institution (CDFI) and community development entity (CDE). To add to the financial strength and stability of the corporation, the maturity of the investment automatically renews unless a majority of the investors notifies the members that the investment should be wound down in no less than five years. There are two classes of bank investors. One class comprises those investing less than \$500,000 and only some of them are represented on the board of directors. The second class invests \$500,000 or more, sits on the board, and is empowered with a unique and stronger voice (in the form of a veto) to prevent material changes in the mission, structure, and investments of the corporation. Otherwise, all directors, a majority of which is made up of community representatives, have an equal voice in MultiBank's governance. Three banks, JPMorgan Chase, Bank of America, and Wells Fargo Bank, have invested more than a combined \$500,000.

MultiBank provides financing and access to technical assistance for the advancement of small businesses, low- and moderate-income housing, nonprofit organizations, and economic development. Part lender and part intermediary, MultiBank provides direct financing in the form of debt, debt with equity features, and credit enhancements to facilitate conventional financing and to leverage other private and public funds. Since December 1992, MultiBank has responded to financing needs in Arizona with 370 loans totaling \$39 million. Loans range from \$500 to \$1 million for community development projects and, including loans from investor banks and borrower equity, total project investments exceed \$157 million.

Over the years, the combination of MultiBank's mission, capitalization, and corporate structure has enabled it to succeed and remain nimble and responsive to community needs. This has happened despite significant changes in the overall banking market, such as the rise of interstate banking and ownership changes among its original investor banks.

A Part of the Community

Today, MultiBank has grown its original investment into \$39 million in loans. It supports worthy projects that typically do not qualify, in whole or in part, for traditional bank financing. About half of its deals are referred by MultiBank investor banks, with the rest coming from existing borrowers and an informal network of contacts, such as SBA-supported small business development centers and area nonprofit organizations.



Three employees of Carefree Assisted Living, in Cottonwood, Ariz., take a break from serving 22 elderly residents. Carefree received gap financing from MultiBank.



Rim Country Lanes obtained a facelift with the financial support from MultiBank.



Three Native American human services providers are sharing this building in downtown Phoenix. The building was renovated with gap financing from MultiBank.

MultiBank's in-the-trenches financing also serves as a de facto research and development activity that helps to create perspective for its investor banks in shaping their lending products. These products are aimed at underserved markets and new customers. Ironically but appropriately, the better MultiBank performs its job, the faster its customers pay off their CDC loans and move into traditional bank financing products. MultiBank provides only project financing; while the borrowers execute their business plans and build their financial footings, investor banks support them with more traditional bank products and services, such as checking, savings, and investments.

"One indication of MultiBank's success is when one of our investor banks pays off a MultiBank loan *because* the borrower has become bankable," explained Bank of America Senior Risk Manager and MultiBank Chair John Philips. "We are always pleased when one of our borrowers has grown to the size and quality that the bank, which originally brought the deal to MultiBank, can ultimately meet all the customer's credit needs. MultiBank can then look for another borrower to help grow and move on to becoming a successful enterprise, increase employment opportunities, and contribute to an expanding local economy and a more positive environment in which to live and work."

MultiBank intentionally invites competition in its community development market. Generally, if another public or private lender can finance the deal with comparable or better terms, we encourage the customer to take it. We find, however, customers often prefer MultiBank's value-added lending that attracts synergistic relationships among funding sources and technical assistance. MultiBank borrowers definitely have dreams to bring to life; however, in general, they lack sufficient equity, a sufficient operating history, and adequate assets to attract a traditional lender to finance their project.

Expanding Senior Care

Expanding senior care was the case for MultiBank client [Carefree Assisted Living](#), Cottonwood, Ariz. Carefree began as a relatively small operation licensed to provide assistance with daily living tasks, such as bathing, dressing, and eating, to six residents who shared a single-family home.

Carefree operates in a county with the state's second highest proportion of residents over 65 and the highest prevalence of residents over 85. The owners saw increased demand from seniors who wanted to live in a home-like environment. With help from MultiBank, they made plans to construct a new 22-bed facility in their rural community. The new project included setting aside four beds for indigent elderly, including veterans.

The deal was risky because the owners had never run an operation of that size. Further, their ability to service the debt relied heavily on income and operating expense projections, rather than an established cash flow. The fact that the building was to be new construction also added a layer of risk. Carefree had the building designed so that it could easily be remodeled into executive suites, should the assisted living facility fail.

Despite the challenges, Wells Fargo Bank and MultiBank saw that Carefree would be filling an important community need and agreed to finance the new facility.

Carefree Assisted Living

As the following chart illustrates, Wells Fargo provided 53 percent of the total project costs for land acquisition, development, and construction financing. MultiBank financed 27 percent of these costs in a subordinated lien position. The interim financing supplied by Wells Fargo and MultiBank converted to permanent mortgages once construction was completed. Wells Fargo refinanced both loans within five years, enabling MultiBank to redeploy its funds for another worthy community development project.

Sources	Uses				
	Funder	Land and Off-Site Improvements	Building Construction	Total	Percent
Wells Fargo		\$171,000	\$219,000	\$390,000	53
Arizona MultiBank		0	200,000	200,000	27
Borrower Equity		0	148,500	148,500	20
Total		\$171,000	\$567,500	\$738,500	100

Source: Arizona MultiBank CDC

Community Benefit

Two employees of a large computer chip fabricator in Arizona wanted a change of lifestyle and discovered the opportunity to purchase, renovate, and reposition the somewhat run-down [Rim Country Bowling Lanes](#), Payson, Ariz.

The wife-and-husband team had no prior experience running a bowling alley, but they were committed to upgrading the

facility. Also, they planned to use their technical know-how to incorporate educational and family-oriented computer activities at the bowling alley.

The deal presented challenges on several levels. To be successful, the \$910,000 project needed to be fully funded, including working capital. Unfortunately, the money the couple saved for their dream was not enough to qualify for the bank's SBA loan. Their experience at the chip maker was a long way from the lower-tech world of running a bowling alley. Further, traditional lenders tended to shy away from lending on single-purpose buildings, such as bowling alleys.

Rim Country Bowling Lanes

As the following chart indicates, MultiBank's \$125,000 subordinated loan sufficiently stretched the owner's equity of \$230,000 to enable Compass Bank to make a \$555,000 loan for the acquisition of the business and special-use real property. Five years after funding, Rim Country Bowling Lanes paid off the original financing.

Sources Funder	Uses			Percent
	Business and Real Property Acquisition	Improvements, Equipment, and Working Capital	Total	
Compass Bank (SBA)	\$555,000	\$0	\$555,000	61
Arizona MultiBank	125,000	0	125,000	14
Borrower Equity	44,000	186,000	230,000	25
Total	\$724,000	\$186,000	\$910,000	100

Source: Arizona MultiBank CDC

Bringing Together Native American Services

Another MultiBank loan, to [Native American Connections](#), emphasized the CDC's commitment to transactions that connect people, places, and services unique to the Arizona market.

This project reinvigorated a mostly vacant, six-story building into a one-stop social services and development center, adjacent to a new light rail system in Phoenix. The building is now the new home of the three largest nonprofit Native American service providers in Phoenix. Native American Connections focuses on culturally appropriate behavioral health and the development of affordable housing with support services. The Native American Community Health Center provides primary health care and medical services. The Phoenix Indian Center's programs include education, workforce development, cultural and language preservation, and family counseling.

The three nonprofit entities, joined together to purchase an 85,000 square foot building and, with planning, coordination, and \$8.2 million established a permanent geographic center and presence for the urban Native American community. In addition, they hope to transform the building into a tourist destination where artisans and vendors can sell their arts, crafts, and other merchandise, and to provide space for cultural amenities and a small businesses incubator program.

Native American Connections

As the following chart illustrates, debt for the acquisition and renovation of the office building included \$6 million in new markets tax credits (partially purchased by two bank investors in MultiBank, M&I Bank, and First National Bank of Arizona) and a subordinate loan of \$1.2 million from the Local Initiatives Support Corporation (LISC). Equity for the project was partially provided by the manager of the building LLC, which was funded by MultiBank's subordinate loan of \$500,000, Wells Fargo's existing equity equivalent loan of \$250,000, and \$141,000 of borrower equity. By MultiBank taking a subordinate lien on collateral, other than the assets of the building securing the new market tax credits and LISC loans, all the pieces of equity and subordinate financing could come together and make the dream of the project a reality.

Sources Funder	Uses	
	Land, Building, Improvements, Reserves, and Fees	Percent
New Markets Tax Credits	\$6,056,000	74
Local Initiatives Support Corporation (LISC)	1,221,000	15
Arizona MultiBank *	500,000	6
Wells Fargo Equity Equivalent Investment *	250,000	3

Equity *	141,000	2
Total	\$8,168,000	100

*Equity was partially funded into the project by Native American Connections, manager of the building LLC.
Source: Arizona MultiBank CDC

What's Next

Looking ahead, MultiBank is evaluating its role in financing sustainable industries in Arizona, especially small businesses growing "green collar" jobs. For the past three years, MultiBank has been working with Navajo officials on a start-up tribal enterprise that primarily uses fly ash. Fly ash is a by-product of a coal-fired-power generating plant on the Navajo reservation used to make a "green" aerated concrete block for construction of new energy-efficient homes on and off the reservation. Also, in response to Arizona's high mortgage foreclosure environment, MultiBank is involved with private and public partners to find ways to make vacant residential properties available to workers in livable neighborhoods who might not otherwise know about these homes and might not typically qualify as owners or renters.

No matter which projects it funds in the future, the real value of the MultiBank will continue to be the synergies that arise from the joint efforts of its board, investors, and community partners.

"MultiBank's investment committee and lending staff have well over a century of combined experience lending to Arizona businesses and have seen, at one time or another, many projects similar to those reviewed at MultiBank," said MultiBank Chair Philips. "We meld that knowledge with MultiBank's distinctive credit culture of 'disciplined flexibility' and find ways to say 'yes'."

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