

INCREASING YOUR SUCCESS THROUGH COMMERCIAL LOANS (PART 3)

By: Jeff Long, CPA

This article is part 3 in a continuation of the information in the previous issues of the Journal. By now hopefully you are aware that our company, Financial Resources, makes residential loan originations and can help you make money as outlined in my previous articles. However, in this article I want to continue exploring commercial loans and how you can make the BIG money!

Financial Resources, is a full service residential and commercial mortgage company. We have been in business since 1989. The main office for the company is in New Hampshire and there are branch offices in Oklahoma and many other states. I have worked out of the Oklahoma office for the last 11 years. Recently, I was transferred and promoted to the main office in Meredith, New Hampshire, as the Director of Commercial Lending & Private Mortgages.

There is a lot to know about commercial loans that is why it is my goal to make it easy to understand. My plan is to explore the many facets of commercial loans in a series of articles. In this article I will continue with the basics, in the form of the commonly asked questions and answers, so you can have an overall understanding of commercial loans and increase your confidence level when you find a commercial deal. I will also address the typical documents needed to evaluate a loan request. In future articles I will explore the following but not necessarily in this order:

1. How commercial loans are underwritten;
2. Foundational concepts such as Net Operating Income, CAP rate, Debt Service Coverage Ratios, and how to determine a property's value;
3. How to recognize a good commercial deal from a bad commercial deal;
4. How to ask the right questions when working directly with a commercial borrower;
5. Grade B-C type loans such as Stated Income loans;
6. Hard Money loans;
7. Construction Loans;
8. HUD Apartment loans up to \$100,000,000
9. Marketing ideas on how you can find good deals and make the big money;
10. Throughout some of the articles I will provide you with some case studies to show you the full loan process.

Quick Tests for evaluating a commercial loan:

As I mentioned in the first article, one of our goals for you is to be able to evaluate and screen a loan to see if it is worth your and our time. The initial quick test to see if a deal is worthwhile is to ask yourself if you had the money would you make the loan to this borrower? If the answer is a solid No, then don't waste your time. If the answer is Maybe or Yes, then you should continue with the deal. The second quick test and one of the main ways to screen a commercial purchase loan request is through the down

payment amount and the LTV being requested. With residential purchase loans many consultants are familiar with our and other companies' ability to make a 100% LTV loan, which unfortunately is not the case with commercial loans. Thus when a borrower has between nothing and 10% down to purchase a commercial property you should help him find a 10% down payment, from other sources, or else you should just pass on the loan.

Once you have determined that a loan request has passed these two quick tests, you should then ask yourself, "What information and answers would I want to have if I were loaning the money?" Most likely we will be asking the same questions. Thus, if you can obtain the answers at the very beginning of the loan request, the process will usually go smoother and more quickly. Here are some of the most commonly asked commercial loan questions and answers.

COMMONLY ASKED COMMERCIAL LOAN QUESTIONS

How long does it take to close a loan?

** Commercial loans take 30-90 days. However, with many hard money loans, the loan can close in less than 30 days.

Can commercial loans be made with no money down?

** No, 99.9% of the time. Commercial loans must have a minimum cash down payment of 10%-30% of the purchase price. However, in some cases the seller is allowed to hold back a second mortgage if the borrower does not have more than 10% down.

The appraised value is greater than the purchase price. Can you finance the full purchase price? Example: If the appraised value is \$1,500,000 and the purchase price is \$1,000,000, can we finance the full purchase price at \$1,000,000?

** No, 99.9% of the time. The property value for loan purposes is based on the LESSER of purchase price or appraised value. This principle is based on the theory of what is called, "willing-buyer, willing-seller." The theory asserts that if the seller could truly sell the property for more than the asking price, then she would certainly do so. The theory being, that an intelligent property seller will set the purchase price of her property at the market value and that an intelligent property buyer is not likely to pay more than the market value. The exception to this occurs when the appraiser says that the property value is less than the purchase price. When this happens, we use the appraiser's lower value for determining the LTV and the loan amount.

Is it possible to make a commercial construction loan?

** Yes, we are aggressive with construction loans on apartment complexes, nursing homes and assisted living facilities, where the loan amount is greater than \$2,000,000 at up to 90% LTV. As for construction loans on owner occupied properties we can also make a loan up to 90% LTV if the borrower meets our SBA program guidelines. Outside these property types the borrower will most likely need to have funds available for a 20 to 30% down payment. Additionally, there are programs available for aggressive hard money construction loans up to 50% LTV.

Do you make second mortgages?

** Never, we only make first mortgages. Please do not send us a request for a second mortgage. However, sometimes the answer to a borrower's request for a second mortgage is to make them a cash-out refinance new FIRST mortgage. Usually this is limited to 65-75% LTV. Thus you should explore this option with your borrower. There are a few lenders in the market that make second mortgage loans, however the transaction would have to be very strong. Generally speaking, I would suggest that you don't spend much time working on second mortgage requests.

Who pays for closing costs and appraisals?

** The borrower is always responsible for these costs and points. Some closing costs may be financed on refinance transactions. Appraisals are paid for, in advance, once a commitment is issued. In every loan we make there are loan charges known as points, sometimes the points are as low as 2 and sometimes as high as 9. A point =1%. Many factors determine the number of points charged: type of property, type of loan, loan amount, credit grade of the borrower, etc.

Are there any up front fees?

** Maybe. In some cases we or other lenders will require a due diligence fee to cover third party expenses such as an appraisal, an environmental study and title work. The fee is paid after we have reviewed all documents provided by the borrower and the terms have been accepted. Any unused portion of the fee for these third party expenses will be credited back to the borrower at the closing. Many commercial lenders, including Financial Resources require a \$500 processing fee to be paid after the borrower has accepted the terms. This fee covers some basic expenses for lenders such as Financial Resources. This small fee also serves as a means for the borrower to show his acceptance of the loan terms, theoretically causing the borrower to cease looking for financing elsewhere.

Who works with the borrower?

** We would prefer to work with the borrower once our loan terms are accepted, but if you want to continue working with borrower this is usually all right. However, we do have a policy of only accepting loans that have no more than one person between the borrower and us. Our goal is to avoid a chain of brokers and wasting time on a loan that is not likely to close. If we work with borrower we will send you a fee agreement acknowledging what you will receive upon a closing.

What is the loan process?

(1) Send us a detailed executive summary and requested information. (2) If the loan is more complex or if we have further questions or needs we will request additional information from you. (3) Once we have enough information we will give you approximate loan terms within 72 hours. (4) You or we can then present the terms to the borrower (5) Upon acceptance of the terms, we will issue a Letter of Intent and have the borrower sign an agreement that outlines the terms, costs and the procedural items needed. (6) At this point we would ideally like to work direct with borrower, but you may continue to work direct if necessary. (7) The appraisal, title work and due diligence is completed. (8) The closing.

How does the consultant get paid and what is the COMMISSION range that can be earned?

** Commissions are paid upon the closing of the loan. The standard base commission is 1/2% to 1% (one-half to one point) of the loan amount. However, with the majority of loans we pay closer to the 1% figure. In some cases we can even pay more than 1%. Your level of involvement, the size of the loan, competition, and the borrowers demands are just some of the determining factors that can affect your commission level.

To whom do I send inquiries and executive summaries?

** Fax all summaries and questions to the commercial loan department in our MAIN OFFICE at fax (603) 279-4278. The company phone number is (603) 279-1133. You would be assigned to a specific loan officer who will handle all of your questions in order to speed up the underwriting process and keep communication simple and clear.

The typical items needed in a complete loan package: if we are provided with a thoroughly submitted loan package it can mean a smooth loan process and a closed loan. The following items should ideally be included when you submit a package. If these items are not included in the package, we can still work on the transaction, however the process will take longer.

1. Executive summary with a cover sheet describing the transaction and any peculiar circumstances with the borrower or property. Please tell us the full story. We can provide you with an Executive Summary form if you email us your request.
2. Last two to three years Income & Expense Statements and Year-To-Date Statements from the property *seller* if this is a purchase or the *borrower* if this is a refinance (unless a start up business, for which we will accept projected statements)
3. Previous 2 years corporate tax returns from the *seller* of a property, if this is a purchase, or the *borrower*, if this is a refinance, and 2 years personal tax returns with all schedules from the *borrower*
4. A detailed property rent roll lease summary that shows who the tenants are and the length of their remaining lease.
5. Color photographs of the property. Include, front, rear, street scene, neighborhood, and inside if possible.
6. Personal Financial Statement when the loan is greater than \$1,000,000 or a residential form 1003 loan application when the loan is less than \$1,000,000 on all borrowers who own more than 20% of the company or property
7. The name, social security number, home address and a business experience Resume on all owners of more than 20%. We will pull a credit report on the borrower(s) unless we are provided with a credit report that is less than 60 days old.
8. Copy of a previous or existing appraisal on the property. We want to learn as much about the property as possible.

There is so much information to share but so little time. I look forward to expanding on the many topics, underwriting parameters, loan types, and exciting stories about closed loans. Perhaps the most important issue to you is how you make money from all of this information. The answer is that if you have solutions to other people's problems then you will make money. Adding commercial loans to the services you offer can put thousands of new dollars in your pocket. Thus I would encourage you to continue reading my series of articles. If you have a loan you wish to discuss please call, send a fax or send an email to my assistant Frank Gindoff or myself.

Jeff Long, CPA, is the Director of Commercial Lending and Private Mortgages of Financial Resources, is now in the main office in New Hampshire and can be reached by calling (603) 279-1133, or fax (603) 279-4278 or email jlong@franh.com If you have a residential loan request please contact Cindy Buckmaster in the Tulsa, Oklahoma branch office at (918) 307-1949 or by fax (918) 294-1913 or by email cbuckmaster@franh.com. Consultant Information packages can be obtained by mail upon a faxed request, by email or from the Web site at www.financialresourcesinc.net.