

Limiting Risk

Paying attention to four factors can keep your loan on the right track

By **David Ross**, senior director, Tremont Realty Capital LLC

FINANCING AFFECTS ALL CLIENTS poised to buy large commercial real estate assets. In most cases, real estate acquisitions are time-sensitive and have specific performance dates. Your financing must not only close, but it also ideally must close with the same terms and loan amount as discussed in the term sheet. Otherwise, you may need to purchase expensive extension options from the seller. Worse, the acquisition may fall through.

To prevent this, borrowers and mortgage brokers must limit the risk involved in the loan process. This requires paying attention to several factors, including the:

- **Funding source;**
- **Value of term sheet;**
- **Information availability;** and
- **Third-party vendors.**

Let's look at all four.

Funding source

When financing a property, it is essential to ensure that the lender is legitimate and reputable. It should have a history of performance and the ability to fund and close the transaction in the required time frame.

Every day, more firms seem willing to issue term sheets for just about any loan request. I suspect that many of these "lenders" are really brokers or intermedi-

aries that will try to place the financing post-application.

This doesn't mean that there aren't legitimate institutions that syndicate or participate in debt and equity behind the scenes. In fact, many major institutions do this. It is important, though, to distinguish between valid lenders and pure opportunists. The real lenders and capital providers have the ability to syndicate and participate loans where necessary and only hit snags occasionally. Opportunistic

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intermediaries that act as lenders often fall flat on their faces. On the closing date, you certainly do not want to discover that you've signed a term sheet with a broker.

Legitimate lenders either manage money or have balance sheets that they can access. It is in your borrower's best interest to make sure that you are aligned



with a capital partner that can and has closed financing transactions in the time frame you desire. Keep in mind that most institutional lenders (banks, Wall Street, life companies, etc.) take 45 to 60 days to close, with obvious exceptions. If you have to close in two weeks, you must find a different type of lender.

Value of term sheet

All lenders conduct a different approval and underwriting process before issuing a term sheet or loan quote. Many will issue term sheets at the drop of a hat. These are worth the paper they are written on and not much more. How can lenders know if their loan committees will approve the deal if they don't have the basic information required to underwrite the deal?

If you are concerned about execution — and I believe that you should be — then work with lenders or capital

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providers that do some homework upfront. They are unlikely to complete full underwriting before having an executed term sheet. But they should still know the deal, be comfortable with the economics as represented and have reviewed the loan with one or more of the people responsible for approval.

The hit ratio with this type of lender is going to be much higher than with others. You must decide if you are in business to collect term sheets or to help your clients acquire properties. If you want to acquire properties, solicit a term sheet that has meaning.

Information availability

Focus on gathering the required information to get to your lender in a timely manner. This is where a lot of transactions slow down or die. When lenders ask for a personal financial statement or three years of property-operating history, find it and get it to them. Most lenders require the same information, so get used to it and provide it. Don't argue, unless it's an off-the-wall request.

You know that you are going to have to provide rent rolls, operating history, borrower financial statements, photos, construction budgets (if applicable), resumes, insurance, real estate tax figures, management contracts, leases, property descriptions, a business plan and other pertinent data. If you don't have this information, it is certainly easier for you to obtain it than it is for the lender.

If there are issues with the property or borrower, disclose them upfront. The lender will find out about them eventually. You will look worse if you were not forthcoming about them. The bottom line is that you don't want to be the cause of your deal falling apart. Communicate information quickly and accurately. Provide clean and concise data.

If possible, financial information should be in electronic form. Nothing should be handwritten. If the seller is the cause of the bottleneck, get your attorney involved.

Third-party vendors

You will have to rely on a host of third-party vendors to close your transaction. Most lenders or capital providers will require an appraisal, a structural engineering report and an environmental report, at the very least.

Then there are the attorneys. The seller, buyer and lender will all have separate attorneys. If there is mezzanine debt or equity going into the deal, then that capital source will also have an attorney. Just one attorney can slow down the whole process. It is important that all parties use attorneys with experience in commercial real estate transactions instead of using residential attorneys.

The lender also should administer the third-party-report providers and do so in the agreed-upon time frame. It is common for appraisers and engineers to ask for extensions. If the appraiser asks for information, provide it. If you get a sense that an appraiser is moving slowly, report it to the lender.

In the business of commercial real estate acquisition, execution is paramount. It trumps interest rates and relationships. It does not matter if you are getting the lowest interest rate on earth if the loan does not close. You will lose the acquisition if you are not focused on execution.

Good commercial brokers will be of great value in controlling the risk. Their job is to vet the lenders and capital providers, to assist with the accumulation and dissemination of information (and with packaging the loan request) and to assist with the third-party vendors. Try to focus on these factors so that your work does not become the Achilles' heel of the transaction. **!!**

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