An Alternative Lending Checklist

Knowing what to look for helps to ensure surprises won't derail a deal

By Mark Fogel

Alternative lenders have been successful in filling needs in the marketplace by providing flexibility, diversity among product offerings, and adapting to changing regulatory and economic times. Additionally, these specialized lenders, which are a competitive alternative to traditional banks, have been able to serve the needs of small businesses and borrowers by tailoring their programs to reflect smaller loans, or by helping those who are either underbanked or nonbankable.

These attributes, along with convenience and expedited loan processing, have enabled alternative lenders to attain a 3.1 percent share of the nearly $3 trillion in commercial mortgages outstanding in the U.S., according to the Mortgage Bankers Association. These facts, however, beg the question: What should commercial mortgage brokers keep in mind when dealing with alternative lenders and how does a borrower ultimately select such a lender?

When considering an alternative lender, there are a couple considerations for sourcing capital. First, it's important for a mortgage broker to know whether the lender uses a balance-sheet or discretionary-funds strategy, or a loan-securitization model. In-house financing generally results in fast, expedited approvals. A lender that securitizes, however, will approve a loan with the goal of eventually selling it to another party.

Management team

An alternative lender may have experience with all types of commercial property assets. Diversified asset types may include multifamily, retail, industrial, student housing and senior housing — such as assisted-living facilities. An experienced lender will have tailored loan-product offerings for each asset type.

Photo illustration by Karen Steichen

The lender's management team should have extensive tenure, because a strong real estate and asset-management background is crucial for withstanding all cycles of the market. Additionally, consider the lender's track record.

Work with a lender that closes a deal in the promised time frame without re-trading loan terms. This is critical because some deals require the borrower to close within a specified time frame with hard investment dollars. Finally, look for an alternative lender that has multiple repeat borrowers because this essentially serves as a verification of the lender's capabilities.

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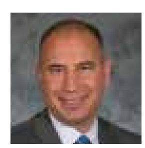

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Platform reach

Alternative lenders may have financing programs with a local, regional or national presence. Be aware of the lender's geographic limitations. If you are looking to borrow in different states, for example, it's especially important to consider a lender with a national platform.

Again, these lenders may have extensive platforms to deal with all asset types. If your client is looking to develop different types of assets, consider using a lender that provides one-stop shopping.

The lender's programs should offer reliability. Certainty of execution on any financing deal results from transparency, maximizing resources and professional integrity.

Product offerings

Loan offerings should include flexible terms. The lender should be creative in structuring the deal financing. In these instances, thinking outside of the box is key. This includes having variable thresholds on loan-to-value (LTV) and loan-to-cost (LTC) ratios.

One of the main reasons to seek out alternative lenders is their ability to go higher on the capital stack — potentially up to 85 percent LTV. A mortgage broker and borrower should make sure any third-party costs, such as construction budgets, are up to date. The devil is in the details, so to speak.

Compare lenders that offer recourse and nonrecourse loans. Your client may not be eligible for a traditional bank loan because of a previous bankruptcy, or because their asset is designed for a reposition play with a two- to three-year window for stabilization. In these instances, a nonrecourse loan option, which most alternative lenders can provide, is a great financing tool.

Your client may also be searching for special types of financing, such as an EB-5 immigrant investor program, tax credits or green-loan initiatives. Developers are getting creative in seeking financing options that lower their overall costs.

Seek out a lender that has a track record of dealing with these programs. Like everything else, if you and your client are counting on these dollars, any unforeseen event could potentially cost you the deal or lower your investment returns.

Process and post-close

The loan-approval process hinges on timing. A lender should be sensitive to keeping the proposed timeline intact. This includes closing the deal as negotiated by actively managing all aspects of due diligence during the underwriting process.

With respect to the required loan documents and legal process, an experienced lender will not seek to recreate the wheel, if at all possible. An existing loan may be able to be assigned to or assumed by a new borrower, for example. These time-saving tips and cost-cutting measures maximize resources and benefit the borrower.

Once the deal is done, a good alternative lender knows the job is not done. Relationship management should be important to them. Most likely, if you are seeking an alternative lender, there may be some challenges associated with your loan. That being said, a strong relationship manager will provide both comfort and expertise every step of the way, from origination to close.

Asset management also is part of the job for a successful alternative lender. Everyone knows that real estate is cyclical. What sets apart any lender is the ability to stay the course when a down cycle hits. This is when an experienced lender can become a strategic partner and, often, either saves money or salvages a deal.

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No one lender will offer everything, and borrowers should not base their decisions on just the economics of the deal. Intangibles like reputation, process, relationship and certainty of execution often seal the deal. In the end, borrowers, with the help of their brokers, have to prioritize what is most important and find the lender that best fits their needs. ■