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Ouch — I Just Learned Something

Loan rejections can hurt, but lenders' reasons are lessons worth remembering

By **Christopher Perez,** director, Commercial Loan Consultants

You have a loan that is about to close, but the lender shoots down the deal at the last moment — seemingly from out of nowhere. Now you must explain to your borrowers why they just spent $3,000 on an appraisal for a deal that won't fund. Not a fun situation for any broker.

You wonder how this could have happened. After all, you qualified the deal in advance and even had the lender's approval in writing. You are perplexed and angry. But you likely aren't justified.

There are many good reasons why loans go sideways once they are in motion. And there are many reasons why lenders have certain guidelines that appear to make no sense. Let's examine the causes.

Complications with appraisals

At the beginning of the loan process, lenders may not accept an existing appraisal, even if it is new. Their reason is simple: fraud.

In the past several years, appraisal fraud has been prevalent in the industry. Sometimes, it can take years to surface. For example, if someone's brother-in-law inflates an appraisal as a favor, it might not turn up until the next time an appraisal is done.

Because of this unfortunate trend, lenders often are particular about only using appraisers on their approved lists. If they do consider an appraisal from a party that is not on their list, they often require that the appraisal had been conducted within the past six months.

Commonly, an appraisal comes in at the expected value, but the lender still cuts the property value. This happens mostly with rural and unique property types, which can take longer to sell than do standard properties. This value reduction happens because the lender is cautious in case it has to sell the property in the event of a foreclosure. Lenders hang their hats on the property value.

Appraisals also can be problematic if a property has more than $25,000 in deferred maintenance. Further, environmental issues can sometimes surface through the appraisal as well. A potential environmental problem is often a deal-killer.

Changes in rates and terms

Lenders sometimes change the rates or terms on loans at the end of the loan cycle. Remember that commercial loans do not have a rate-lock period. This means that if the loan's index (i.e., prime, LIBOR, etc.) increases while the borrowers are in the process of getting the loan, their original offer is subject to change without notice. This is not always the lender's fault. Often, it is a necessary adjustment to react to a change on Wall Street or in the economy.

A change in rates and terms sometimes could be the borrowers' fault. If the borrowers' credit score drops before closing, they may no longer qualify for the loan.

Random issues also can alter a deal. For example, a lender may have too much of one property type in its portfolio and, in an effort to balance out the portfolio, will turn down your loan request on that property type.

Or consider what happened recently with one type of loan. A major commercial insurer decided to pull out from environmentally sensitive properties without notice. As a result, all the lenders using that insurance company could no longer lend on these property types.

Although the insurance company is responsible for killing the loan, the broker and borrowers often only see the lender backing out.

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Title issues

Lenders sometimes flat out kill a deal at the end. Title issues, aside from credit and appraisal, are a big reason for this. Without clean title, which is what establishes true ownership of a property, a lender cannot make a loan.

The title process usually is completed in conjunction with the appraisal, so the reports may not come in until the end of the process. While some title issues will only delay the process, others — such as an easement issue or an issue with a third party who owns access to a piece of the property — could take years to resolve, if at all.

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Although it doesn't always seem like it, your lenders want to help you successfully fund loans. But when you find yourself feeling especially confident about the chances of a loan, remember that your account executive does not have the ultimate say in the final moments.

Something else you should remember is that each loan passes through many departments on the lender's end. These range from processing to legal. All this work carries an additional expense to the lender. Lenders can lose $5,000 to $8,000 per loan on loans that don't fund. That is a big number when you consider the amount of commercial loans that die.

Most lenders do not make rash decisions without good reasons. They are looking to make

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Wall Street happy. They also are seeking commissions, bonuses and solid monthly numbers.

If you consistently have a lender that changes deals on you without logical explanations, however, it's time to go shopping for some new sources.