Small-Balance Deals Need the Right Champions

Nonbankable borrowers are the bread and butter of the nonconforming lender

By Patrick Seymour

For commercial mortgage brokers who typically close residential or large-balance commercial mortgages, small-balance mortgages for nonbankable borrowers might initially seem too difficult. Because nonconforming lenders, or nonbank lenders, don't face the same kinds of restrictions and regulations that confront banks, the process of closing mortgages for self-employed borrowers who are unable to obtain traditional commercial financing can be much simpler.

This is especially true if you're working with an experienced lender. Certainly, mortgage brokers should focus most of their efforts on their core business, as this is your bread and butter. Brokers looking to expand their product offerings and increase their income, however, shouldn't turn away small-balance business when it comes across their desks.

Mortgage brokers who choose to close these types of deals can expect to work with fewer submission documents, lenders with more flexible guidelines, programs that fit the needs of the self-employed, a quick turnaround time for most deals and higher commissions. As long as you work with the right nonconforming lender, closing these loans is an easy way to earn more.

Less paperwork

In order to submit a commercial deal to a bank or other traditional lending institution, commercial mortgage brokers need to compile a large amount of documentation to comply with regulations. Generally, these lenders are going to require an extensive amount of information just to review a commercial mortgage scenario. In addition to an application, credit report and summary of the deal, brokers will need to provide their borrower's tax returns and other financial information to verify their borrower's income and ability to repay the loan. For some borrowers, particularly the self-employed, this means disqualification from traditional financing.

Although nonconforming commercial lenders do require many of the same documents to fully underwrite a commercial mortgage, there are some who do not use tax returns to underwrite the deal, but need them simply to know the borrower has filed. These lenders are able to verify your borrower's income and capacity to repay through other means, as they are not bound by the same types of regulations that restrict banks and other traditional financing sources.

Flexible underwriting

Because traditional lenders must comply with stricter regulations than their nonconforming counterparts, many borrowers fall outside of their lending parameters for various reasons. A small-business owner whose credit score has taken a hit in the past and is still recovering, for example, will likely have trouble qualifying for a bank loan because most banks have hard guidelines on what they will accept.

Likewise, self-employed borrowers who are behind on taxes and are looking to pay off their balance will be unable to obtain a traditional commercial mortgage because banks require taxes to be current in order to underwrite their loans. Additionally, it can take these lenders up to a week to let a broker know if they're interested in the deal, and there's no guarantee that it won't fall through during the underwriting process.

In contrast, small-balance commercial mortgages are not bound by the same regulations as banks, so they are able to view each borrower as more than a number or tax lien. An experienced nonconforming lender will be able to take the above factors into account when assessing the risks of a deal, and they can consider additional financial information when evaluating a borrower's commercial mortgage request.

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Small-balance commercial lenders can listen to your borrower's story and work with them to provide the best possible financial solution. Additionally, some small-balance lenders underwrite as much of the deal as possible upfront in order to make sure, to the best of their ability, that the deal doesn't fall through later.

A variety of programs

Although banks are able to serve a wide variety of borrowers, many self-employed borrowers are unable to qualify for this type of financing. This has a lot to do with a bank's credit guidelines, but it also comes down to the fact that banks, because of regulations, aren't able to create programs that meet the needs of many small-business owners.

Nonconforming lenders, however, have more freedom in terms of the lending programs they offer. Institutions that focus on small-balance commercial mortgages and the needs of self-employed borrowers are able to create a variety of programs that fit the needs of their clients.

For borrowers seeking a commercial mortgage in a short time frame, banks and other traditional lenders might not be the best outlets. Because of strict underwriting guidelines, it can take months for a commercial mortgage to close. This could be a problem if your borrower needs funds quickly to pay off an existing mortgage, purchase a commercial property within a certain time period, pay off back taxes, exercise a lease-purchase contract or purchase option, or take advantage of a great deal on inventory for their business.

Because nonconforming commercial mortgage lenders require less paperwork and have a more flexible approach to underwriting each deal, they have the ability to close loans in a much shorter time frame. Some lenders can close these mortgages in as little as two to three weeks. If your borrower needs financing quickly, a small-balance commercial lender might be their best opportunity.

Higher commissions

Since the implementation of the Consumer Financial Protection Bureau's qualified mortgage rule, residential mortgage brokers, in particular, have seen smaller commissions. Banks and other traditional lenders, however, also generally cap commissions for commercial mortgages at a lower percentage rate. This makes sense when dealing with borrowers who qualify for bank financing.

For mortgage brokers interested in closing small-balance commercial mortgages for nonbankable borrowers, the fee caps are generally higher. Some lenders allow mortgage brokers to charge as much as 5 percent on each deal, as well as additional fees in yield-spread premium.

Small-balance commercial mortgage lenders allow brokers to charge higher fees because they realize that brokers closing these kinds of deals are taking on riskier borrowers and, as such, might need to do a little extra work to prove that the commercial mortgage request is viable and that the borrower can make their monthly payments.

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At first glance, small-balance commercial mortgages might seem daunting to brokers unfamiliar with them. But the fact of the matter is that they are a simple way to increase income. Because the nonbank lenders who work in this market face less stringent regulatory standards, they can focus on helping mortgage brokers meet the needs of the nonbankable borrowers seeking commercial financing. If you're a commercial mortgage broker who's interested in earning more, find yourself an experienced small-balance commercial lender and get started today. ■