

# HOW TO AVOID THE PITFALLS OF THE COMMERCIAL MORTGAGE APPLICATION

This FREE report, prepared by commercial mortgage professionals and posted on [www.GetLowRate.com](http://www.GetLowRate.com), highlights the five primary reasons why banks decline commercial mortgage applications. Five reasons described below will be important for a typical commercial mortgage scenario. We will suggest possible solutions to convert the declined loan into an approved commercial mortgage.

1. The first reason a commercial loan is declined or counter offered to a lower loan amount is that the cash flow is not sufficient to support the requested loan amount.

Generally, the fair market value of the commercial property is determined by an appraisal. In most cases, a commercial lender will NOT accept an appraisal from a residential appraiser (hired by the general public or a mortgage broker) unless that appraiser was designated in advance by the lender. Usually, the bank itself will assign a staff appraiser to do the evaluation of the property. This is to prevent collusion between the borrower and the appraiser to assign an inflated property value.

When the appraisal report is submitted to the bank, the underwriter will determine the value of the property based on the LOWER value obtained by the sales/market approach (comparable sales in the same neighborhood) or the income and expense analysis approach (comparable rental income of properties recently sold and properties currently in operation in the same neighborhood). In a purchase transaction, if the income from the property does not support the contract price, the appraised value will be lower than the purchase price. Therefore, if the lender in its initial letter of intent agreed to lend the borrower 75% of the contract price (75% LTV), and the appraised value is reduced by the bank based on the income and expense analysis approach, the lender will base its 75% on the appraised value and not of the purchase price.

On the contrary, if the appraised value is higher than the purchase price, mortgage professionals are often asked by real estate agents and buyers to base their loan on the appraised value rather than the purchase price. The buyer or agent claims that a super deal was negotiated and that the property is worth more than the purchase price. The lender will always base its maximum loan amount on the LOWER of the purchase price or appraisal. A lender's opinion is that an appraisal is really no more than an estimate of fair market value; and if the property sells for "X" amount of dollars, then it is probably only worth that "X" amount of dollars.

Possible solution #1:

- A) Bring additional personal funds to the closing table (quite often the borrower just does not have them).
- B) Renegotiate the deal based on the appraisal report (assuming willingness by both parties).
- C) Request a cross collateralization from the lender (use other real estate owned by the borrower as collateral). The borrower should avoid cross-collateralizing assets as a condition for obtaining a loan unless it is last resort to buy a desired commercial property.

2. The second reason a commercial loan is declined or counter offered to the lower loan amount is the loan underwriters find something on the tax return that disqualifies a borrower under the bank's lending guidelines. This "something" maybe insufficient net income, or "something else" that will produce a similar result.

Possible solution #2: A borrower applying for a commercial loan should apply for a "Stated Income" (no tax returns, no income verification, no IRS Form 4506) commercial mortgage. Please be advised that this strategy will not work for all commercial mortgages since there is a maximum loan amount of \$2-3 million for most Stated Income Commercial Mortgage Programs.

3. The third reason a commercial loan may be declined is due to property type or special requirements imposed that make the loan impractical for the commercial borrower. Not all lenders deal in all property types. For example, fewer banks are making loans to bar/restaurant properties. Similarly, auto service businesses are frequently given unnecessary (and expensive) environmental reporting requirements. There are many "special purpose" properties such as funeral homes, churches, and campgrounds that most traditional commercial lenders will not include in their business lending portfolio.

Possible solution #3: Commercial borrowers should seek options outside traditional banks. Commercial lenders do exist that are interested in special purpose properties. If you are interested in submitting a request to find such a special purpose lender, please log on to [www.GetLowRate.com](http://www.GetLowRate.com), click on "Online Application," and submit a form with your question(s). We will find up to six lenders that will be interested in funding your loan.

4. When a business is refinancing its current commercial mortgage and wants to take a significant amount of cash out for various uses, it is not unusual for the bank to restrict what the funds are used for and to limit the amount of cash to as little as \$100,000.00. Even though the bank might make the loan, if it won't provide the amount of cash needed by the commercial borrower, this is equivalent to declining the loan.

Possible solution #4: As mentioned in Possible solution #3, there are options available elsewhere. A commercial borrower should find a lender or a commercial mortgage broker who will find a bank that allows a borrower to take as much cash as possible without any restrictions on its use.

5. Another main reason a commercial application maybe declined is a bank will not lend without adequate collateral in the form of a lien on other real estate owned by the borrower.

Possible solution #5: Commercial mortgage borrowers should seek lenders that do not “cross collateralize” assets as a condition for obtaining a commercial loan unless it is last resort to buy a desired commercial property. Commercial mortgage borrowers should avoid unnecessary connection between business and personal assets.

Please remember if you are in a process of buying, refinancing, or selling commercial real estate and need professional and candid advice, please log on to [www.GetLowRate.com](http://www.GetLowRate.com), click on “Online Application,” and submit a form. We will email or call you back within 24 hours of your submission.