Commercial Loan Overview

A Borrower's Guide

ALB Commercial Capital is dedicated to defining the standards for high quality service, expertise and personalized guidance. We specialize in providing loan programs tailored to our clients Goals. The contents in this guide are for reference purposes and actual loan programs have different guidelines and requirements and therefore it is best to speak with one of our Advisors.

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Commercial Mortgage Underwriting Guidelines and Process
Commercial financing for commercial properties is underwritten on a case by case basis. Every loan application is unique and evaluated on its own merits, but there are a few common criteria lenders look for in commercial loan packages.

Financial Analysis
A key component in making an underwriting evaluation is the personal debt coverage ratio. The PDCR is defined as the monthly debt compared to the adjusted gross monthly income of the borrower in question. Using a PDCR of 1:1.25 a lender is saying that they are looking for a $1.25 in net income for each $1.00 mortgage payment. Typically they will determine the PDCR ratio based on monthly figures, the monthly mortgage payment compared to the monthly net borrower income. The higher the PDCR ratio the more conservative the lender. PDCR's are set by property type and what a lender perceives the risk to be. Commercial properties are composed of several different property types from retail, office, industrial just to name a few. The risk associated with the collateral would depend on the property type, as well as other factors such as age and geographic location. As such, when a lender is underwriting what they would consider a more risk adverse asset then they are more inclined to use higher PDCR's when evaluating a loan request. Another important variable that affects underwriting would be whether we are evaluating a loan request of a commercial Investment property versus an owner user property. Your ALB Loan Advisor can assist you to understand the PDCR policies of each of the major commercial lenders.

Loan to Value
Unlike residential lending, commercial investment properties are viewed more conservatively. Many lenders will require a minimum of 30% of the purchase price to be paid by the buyer. However, some lenders will lend up to 75% of the purchase price to buyers based upon their cash flow and net assets. What a bank/lender will do is subject to their appetite and the quality of the buyer and property. Loan to value is the percentage calculation of the loan amount divided by the purchase price. If you know what the lender's LTV requirements are, you can also calculate the loan amount by multiplying the purchase price by the LTV percentage. Keep in mind that the purchase price must also be supported by an appraisal. In the event that the appraisal shows a value less than the purchase price, the lender will use the lower of the two numbers to determine the loan that will be made.

Credit Worthiness
In many cases the personal credit of the principals will be evaluated.

Property Analysis
Fair market value and fair market rent will be analyzed. Special use properties may require additional underwriting. Age, appearance, local market, location, and accessibility are some other factors considered.

Tenant Analysis
A thorough analysis of the current leases will be conducted. In addition to a commercial lease summary, all tenant leases will be required for review. A thorough analysis of the current tenant(s) will be conducted. Lenders will evaluate the financial strength of the tenant, how many years are left on the current lease, and other relevant information regarding the tenant.

Commercial Mortgage Lending Ratios

Most of real estate lending can be boiled down to the results of three ratios:

- Loan-To-Value Ratio (LTV)
- Personal Debt Coverage Ratio (PDCR)
- Debt Service Coverage Ratio (DSCR)

The bulk of the energy spent "processing" a loan is merely an attempt to verify the numbers that go into the numerator and denominator of these ratios.

The Loan-To-Value Ratio is defined as follows:

> Loan-To-Value = Total loan balances (1st mtg + 2nd mtg) / Fair market value (as determined by appraisal)

For Commercial mortgages, Loan- to- value ratios seldom exceed 80%.

The Personal Debt Coverage Ratio is the second ratio lenders use when underwriting a loan. The Personal Debt Ratio compares the amount of bills that the borrower must pay each month to the amount of income he earns. More precisely, the Personal Debt Coverage Ratio is defined as:

> Personal Debt Coverage Ratio = Monthly Personal Debt / Monthly Personal Income

Obviously someone whose Personal Debt Coverage Ratio is 100% is in trouble. A Personal Debt Ratio of 100% would mean that the borrower's obligations are exactly the same as his income. Personal Debt Ratios seldom are allowed to exceed 50% in practice.

Debt Service Coverage Ratio evaluates the debt coverage of the property itself. The Debt Service Coverage Ratio is defined as follows:

> Debt Service Coverage Ratio = Net Operating Income / Debt Service

Net operating income is the income from a rental property after deducting for real estate taxes, fire insurance, repairs, and all other operating expenses. Debt service is the mortgage payment on the property. Most lenders insist that this ratio exceed 1.2 with a few a allowing 1.15. A Debt Service Coverage Ratio of less than 1.0 would mean that the property did not produce enough net rental income for the owner to make the mortgage payments without supplementing the property from his personal budget.

Initiating Your Commercial Loan Process

To initiate your commercial lending application process, the following information is required by financial institutions. Your ALB Loan Advisor will assist you in preparing this information:

1. Offering Memorandum, Marketing Package or Property overview
2. If purchase - Copies of buyer and seller execut3ed Purchase Contract, along with all offers and counter offers.
3. Operating Statements: Last two years and year-to-date.
4. Commercial Lease Summary, and copies of all tenant leases.
5. Borrower's background summary or resume
6. Last two years personal federal tax returns from the principal borrower(s)- including all Schedules and K-1's.
7. Current personal financial statement of principal borrower(s) including real estate all schedules (dated and signed with original signature)

Lending Institution fees
Various lending institutions have different fee schedules for commercial loan applications and processing. The range of fees varies widely amongst these institutions. Your ALB Loan Advisor will be happy to provide more information on the schedule of fees for each institution. A range of potential fees of several leading institutions is as follows.

- Attorney: $0 - $6,500
- Appraisal: $0 - $3,500
- Lenders Inspection: $0 - $350

Note: That fees differ from lender to lender

How to Get Started
ALB Specializes on providing a full service solution to customers interested in any size multi-family loan. Call us for a free consultation on initiating your loan process.

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