Getting Financing for Your Project

Normal View

Today's changing economic environment makes it more important than ever that builders and developers make their project funding proposals as attractive to lenders as possible. To do so, builders must pay close attention to preparation and documentation, presentation, and maximizing the lender relationship.

Preparation and Documentation

Ask your lender what he or she wants to see in your loan proposal. Too often, builders prepare a loan proposal after consulting only briefly with their lender. It is usually better to start by asking exactly what your lender wants. Simply asking can give you an insight into what your proposal should look like before you spend time and money preparing one. In order to better prepare your loan package, be sure to listen carefully for areas that the lender emphasizes.

Carefully produce the required documents. In addition to financial information and the loan applicant's track record, most loan requests must include detailed market studies, pro formas, and documentation that all regulatory approvals have been obtained, environmental concerns have been addressed and impact fees have been paid. The standard documents usually required for housing production loans are listed below.

Project Documents:

- Location and description
- Survey
- Appraisal
- Title report
- Market study
- Project feasibility study
- Pro forma analysis
- Site plan
- House plans
- Estimate of project costs
- Development and construction schedules
- Documentation of zoning approval
- Proof of payment of impact fees
- Documentation on infrastructure agreements

Personal and Company Documents:

- Current financial statements
- Company income tax statements
- Personal income tax statements
- Documentation of personal collateral

- Partnership or joint venture contracts
- Personal guarantee
- Company track record
- Company structure
- Personal and business references

Be sure to document costs. Most lenders want to see a detailed cost breakdown. In particular, lenders want to see that your cost estimates are in line with their other projects to calm fears that your project will come in over budget and they will have to come up with more money at the last minute to complete it. Also, lenders want to see whether they stand a reasonable chance of breaking even if they are forced to foreclose on a loan and turn the project over to another builder.

Provide additional favorable information. Lenders will tell you what they want to see if you ask them, but providing additional information can really make a positive impression. This is particularly important if there is an area where you excel. For instance, if you have strong finances, you should provide audited financial statements for your company and your corporate and personal tax returns. If you have access to market research, you should provide additional information on the market and the basis for your sales price and absorption rate assumptions.

Presentation

Present a simple, concise and professional proposal. There is no substitute for a polished-looking, focused and clear proposal. That may mean investing in desktop publishing software or learning how to use your word-processing software more effectively. It also helps to create a cover page and an executive summary. In your presentation to the lender, include information that supports important points or assumptions in your proposal. Be sure to provide summary spreadsheets of profit and loss statements, cost breakdowns, and anticipated cash flows, but also be sure to append full annotations for each line item.

Let your lender know about your experience in the building industry. Lenders want to know your track record. A primary reason that a lender may be unwilling to make a housing production loan is that he or she is not sure if the builder or developer has the experience or financial capacity necessary to complete the project and repay the loan. Provide documentation on the history of your company, highlighting its successes and financial condition. Many lenders require end-of-year company balance sheets and personal tax returns for at least the past two years. Going beyond just the numbers by providing a prospectus that includes photographs of completed projects and a statement of your company's goals and philosophy shows that you are a builder with a vision and an ability to plan and market yourself. Even if you have been doing business with your lender for a long time, he or she may have to present your case to new management, a new bank holding company, or bank examiners who are unfamiliar with you and your company.

Convince your lender that you can complete the project. Many builders can convince their lender that it is possible to start a project, but it still takes skill to convince lenders that the project will be completed as intended. Make sure that your proposal and presentation document the construction schedule for the project, the anticipated schedule of draws, and the anticipated repayment schedule based on reasonable and well-documented sales price and absorption-rate assumptions.

Be flexible and resourceful in making your loan request more attractive. If the lender is reluctant to fund your project based on the original package, offer changes designed to address his or her concerns and make the deal more attractive. If possible, provide more up-front cash. Try shortening the term of the loan that you request. If you are developing land, you may need to secure lot purchase contracts to generate lender interest. Offer a strong guarantor or a second source of repayment. Another approach is to seek sources of community or economic development funds to bolster the project's financial stability.

Consider loan participation arrangements. A lending institution may be unable to provide full funding because of restrictions on capital. Moreover, insured institutions that are working out their own financial difficulties often are limited by operating restrictions, and small community lenders have legal lending limits. Sometimes the loan is too large or the borrower or the borrower's partner or affiliate already has a loan outstanding with the lender. If the loan amount or project is too large and there is a loans-to-one borrower problem, the lender may be able to work with other financial institutions on a participation arrangement.

Be prepared to pursue alternatives if it becomes clear that the lender is not interested in your project. Do not be discouraged by lenders who ask for a good deal of documentation and paperwork on your loan request. In fact, you should expect it. So, if a lender shows a real interest in doing business with you, but asks for a great deal of documentation, try to provide all of it and more. See the process through to its conclusion. However, there is no point in pleading with a lender that is not interested in lending either to you or to home builders in general. Warning signs include unreturned telephone calls and a request for you to submit a worst-case scenario appraisal. If a lender asks you to justify a project based on its value if the market collapses, the lender probably is not interested in financing your project.

Relationships with Lenders

Try to cultivate lasting relationships with your lenders. It never hurts to treat each lender as if he or she is someone with whom you hope to develop a long-term relationship. Treat your lenders with respect and try to bring as much business their way as possible. For instance, if you get a land acquisition or development loan, it will help to get your construction loan and the mortgage financing for your customers all from the same lender.

Do not keep secrets; get your lender involved in problems at the early stages. Hiding problems from your lender is not a good strategy for getting loans. Be absolutely truthful about your past successes and failures, your personal finances, and your company's current financial condition. Also, alert your lender to any potential problem at the first sign of trouble. Problems in keeping to a proposed schedule or meeting the terms of your contract are sometimes unavoidable, and the earlier that your lender knows of a problem, the easier it is for you to work together toward a solution. Also, remember you are in the home building industry for the long haul, and your reputation for trustworthiness is important and will follow you in future efforts to secure housing production loans.

Consider working with more than one financial institution, but keep your lender informed. Although you may have developed very strong ties with one lender, it may be best not to depend exclusively on one lending institution. The bank or thrift where you do business may be under different ownership or management or even out of business next year. Cultivating lasting relationships with lenders takes time, so it's best to begin to develop new relationships before it is a financial necessity. If you decide to pursue relationships with other lenders, explain to your lender why you are developing ties to others and confirm that you still plan to conduct most of your business at his or her institution.

For more information about this item, please contact Michelle Hamecs at 800-368-5242 x8425 or via e-mail at mhamecs@nahb.org.