

Commercial Real Estate Loans for Fractured Condo's

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FRACTURED CONDO'S are *everywhere* in Florida (...and the Southwest). A fractured condo is a residential condominium complex where some of the units were sold as condo's, but the bulk of the units remain unsold and are rented out as apartments. Typically the rental units are put in a rental pool that is run by a large management company.

Fractured condo's have a lot of problems because renters don't treat the property with the same level of care as the owners. In addition, renters are often younger, louder and more raucous.

In most cases, because of the by-laws of the development, the management of the homeowners association remains in the control of the original developer, despite the fact that he might own less than 50% of the units. If the developer declares that his unsold units are no longer for sale, he may lose control of the homeowners association. On the other hand, if the developer keeps his units for sale... *financing won't be available from any lender that is prohibited from lending on real estate that is for sale.*

One of the largest problems for fractured condo's is that most developers, in order to sell their condo's, often set their initial homeowners association dues artificially low. Therefore the homeowners association starts out under-funded.

A few bridge loan lenders will finance fractured condo's at LIBOR plus 3.5% to 4.0%. They will underwrite the deal to a breakeven cash flow (DSCR=1), which unfortunately will only be about 60% of the cost of the condo's. Someone will have to take a very painful haircut.

Notes from Quest: Bear in mind that, if equity component percentage is required by the lender, if the lender requires a Debt Service Coverage Ratio of greater than 1, or if it uses a high capitalization rate to impute value to a project, the available loan amount could be reduced further. Also, the equity contribution required from a buyer would rise. In any event, this can a difficult type of project to fund unless someone is really willing to "take a bath", to put it mildly. Anyone considering buying such a project needs to be very careful, and very cautious, when "running the numbers" to determine the feasibility of funding the deal. However, Quest has found lenders who will fund fractured condo's when the numbers are right. This includes the vacancy factor being small enough to assure adequate income.

Also, there is a large correlation between the amount of the loss, that the developer or seller will suffer, and the quality or original anticipated prices of the units: A luxury condominium project will suffer a greater relative loss because the individual units would never have garnered enough rent to have made them good rental investments. A less luxurious project needs a smaller drop in value for it to be a possible profit center.

Looking for a Fractured Condo project loan? Call Quest. Perhaps we can help you!

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