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# Non-Traditional Real Estate Mortgage Financing: What Is It and How Does it Work?

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## Background:

Your business has an immediate cash need. This shortfall may be due to the cancellation of a major order, new regulatory requirements requiring additional licensing costs or investment, the acquisition of another business, or an expansion of the existing company. As a result, you are cash-strapped and your existing traditional bank is not willing to extend further financing. If your business is service-based, it may lack tangible assets (such as inventory, receivables or equipment) to support a loan from a non-traditional asset-based lender.

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## What is Mortgage Financing?

Assuming your existing business is viable, and that additional cash injection will bring it back on track, real estate mortgage financing would be an apt choice. It can be treated as either an additional equity injection or a shareholder loan. In summary, mortgage financing is a way of leveraging your personal real estate asset to source financing for your business. The existing traditional lender may view this favourably as you put “more skin in the game”.

For example, your house is worth $700,000, against which you have a traditional mortgage of $400,000. This leaves you with $300,000 in equity. Against this $300,000, there are non-traditional mortgage lenders that can lend up to a certain amount. The size of the loan is determined by the loan-to-value ratio, as described below.

Some key features:

- Appraisal – Lenders require an estimation of the real estate value from an appraiser of their choice, and at the expense of the borrower. This could take a week or two to conduct or, in more urgent situations, within a matter of a few days (albeit, at a higher cost).
- Loan-to-value (LTV) ratio – Lenders will only lend up to a certain amount of the appraised value, typically 70% to 85%.
- Term – Mortgage lenders typically provide short-term financing solutions, up to 12 months, with renewal options.
- Repayment structure – Repayments can be made with either monthly interest plus principal, or

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interest only. Lenders are generally open to early repayment.

- Interest cost – Non-traditional mortgage lenders are more expensive, charging interest in the range of 8% to 12%. Primarily, this would be driven by the location of the property and how high the existing traditional mortgage is as a percentage of the total property value. These loans are more expensive than traditional mortgage solutions because the lenders are willing to sit behind existing traditional lenders and, inherently, assume more risk.
- Other costs – These generally include lender fees (3% to 10%, depending on the loan size) and legal fees (depends on the lawyers chosen).
- Quick approvals – These lenders have less stringent loan qualification requirements than traditional banks and, as such, can respond with a quick "Yes" or "No". They will generally lend where businesses are under-performing, provided they feel the business or owner can adequately service the debt.
- Security – These lenders will place a charge on the real estate and sit behind the existing mortgage lender.
- Exit strategy – Lenders will want to know how the loan is going to be repaid, whether through the sale of the real estate, cashflow from the business, or personal net worth.
- Ability to make monthly payments – Lenders consider several factors, such as personal credit scores, income of the borrower, dependency on the business as the source of debt service, and rental income from the property (if any).

## Conclusion:

Assuming you are comfortable with using your home or other real estate as collateral, non-traditional mortgage financing may be considered an alternative source of business financing—particularly when an owner is looking for a quick and cost-effective solution to source a more pressing need. It can act as an additional lifeline or bridge solution until you can secure a more permanent solution from a traditional source. Due to the large number of mortgage lenders in the market, there are a wide variety of flexible and innovative solutions available.

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At Isaacs Advisory, we have extensive experience advising, structuring, and sourcing a wide range of traditional and non-traditional financing solutions of $100K to $1 million for our clients.

For more information on raising financing solutions for a start-up, early stage, growth, in-transition or business in distress, please contact Dheeraj Nair at 647-673-4969 or dnair@isaacsadvisory.ca.