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The Complete Guide to Bridging Loans

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The Complete Guide to Bridging Loans

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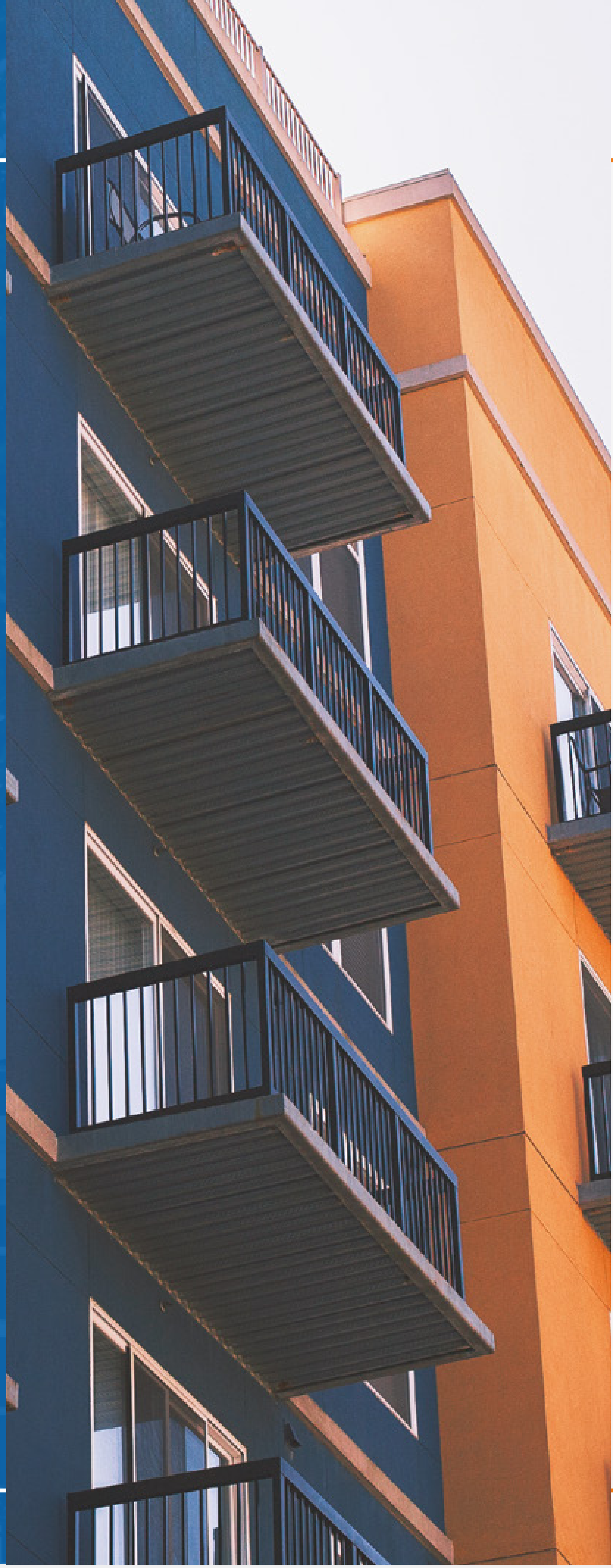

What is a bridging loan?

Bridging loans are a type of short term finance often used to "bridge" temporary gaps in funding.

They allow property purchases and development projects to move ahead quickly when other forms of finance are not available or have fallen through.

Loan terms

Loans terms for bridging finance are usually 12 months or less. Some lenders offer longer terms depending on the circumstances.

Funds can often be available within days, making bridging finance one of the fastest ways to access capital.

How much you can borrow

This depends entirely on the lender, your financial circumstances and the lender's valuation of the property or development in question.

Bridging loans usually start from £25,000. Below this, a personal loan may be more appropriate.

There are no upper limits on how much you can borrow, it is entirely at the lender's discretion.

Interest rates

Interest rates tend to be higher on bridging loans compared to longer term loans or mortgages.

Lenders often allow you to roll up monthly interest payments and repay them alongside the capital at the end of the agreed term.

Fees

Borrowers normally pay:

- A lender arrangement fee
- An exit fee when repaying the loan (in some cases, depending on the lender)
- Additional fees including surveyor, legal and broker fees

Exit plans

Borrowers normally need to provide an exit plan when taking out bridging finance.

This specifies exactly how the loan will be repaid - usually by refinancing or by selling the property on.

When to use a bridging loan

Consider bridging finance if:

- You need a fast way to access funds
- Traditional finance, such as a mortgage, cannot be accessed quickly enough
- A previous source of funding has fallen through
- The property will not be eligible for a mortgage until improvements have been made

Types of bridging loan

There are a few different ways bridging finance can be categorised. Any bridging loan you take out will be subject to the following conditions:

Closed or open bridge.
A closed bridge is where you have a set date for repayment.

e.g. a loan to buy a new home before selling your old one, where you have an agreed completion date for your old home so know exactly when you can repay.

An open bridge is where you have an agreed exit strategy, but not a set date for repayment.

e.g. a development deal where the plan is to refinance or sell. The exact repayment date will depend upon when work is completed.

First and second charge
First charge bridging loans are those taken out on properties that do not already have a loan, such as a mortgage, secured against them.

Second charge bridging loans are those taken out against property where there is already a secured debt, such as a mortgage.

The terms “first charge” and “second charge” show the order of priority of repayment.

e.g. a first charge loan has priority over a second charge loan if the secured property has to be sold to repay the debt and there is not enough to cover both loans.

A bridging loan can be both first and second charge if secured against more than one property.

Regulated or unregulated
Bridging loans are usually regulated by the Financial Conduct Authority (FCA). However, not all bridging loans are regulated.

Regulated bridging loans are those where the loan is taken out as first charge or second charge over the borrower’s home, or that of a partner or family member.

Unregulated bridging loans are usually where the loan is secured as a first or second charge against a property where neither the borrower, their partner nor their family live.

A bridging loan may also be exempt from regulation if secured against the borrower or a connected person’s home where the loan is over £25,000 and intended for business purposes.

Loans may also be exempt from regulation if the borrower is regarded as a high net worth individual.

What can a bridging loan be used for?

Bridging loans have a number of applications, both for private and commercial use.

They are most commonly used for various types of property and development deals.

Typical uses for bridging loans
Bridging loans are often used for:

- Residential property transactions
- Commercial property transactions
- Auction finance
- Renovation projects
- Change of use developments e.g. office conversions, student accommodation
- New build development projects

Bridging loans are popular for property projects because they offer fast, flexible access to large sums of money. This make it possible to move forward quickly with investment and personal opportunities.

When to use a bridging loan
Bridging finance can help with a number of situations, including:

- Quickly securing a property in the UK or abroad
- When a deal below you in a property chain falls through
- Building a house
- Downsizing to pay off an existing mortgage
- Converting or renovating unmortgageable properties
- Buying a property at auction
- Property refurbishment for investment purposes

How much does a bridging loan cost?

Due to its short term nature, bridging finance can be more expensive than traditional longer term finance such as a mortgage.

As well as interest, you will also pay an arrangement fee when you take out a loan and possibly an exit fee when you repay. Other fees may include valuation fees, administration fees, broker fees and legal fees.

Arrangement fees

Charged when you first receive the loan and based on a percentage of the total loan value. 1-2% is typical.

Monthly repayments

Bridging loans are usually offered on an interest only basis with the capital repaid when the loan term ends.

You may have the option to roll up your interest or choose retained interest to help structure your repayments in a way that suits you.

Rolled up interest is where the interest for the full loan term is added to the capital sum so you can pay it all in one go when you repay the loan.

If you repay early, you normally get back the interest on the portion of the original loan term you did not use.

Retained interest is where you borrow more than you actually need, with the extra covering the interest on the total loan for the full loan term.

Again, if you repay the loan early, you may get a refund for the interest on the period of the full loan term you did not use (depending on the lender).

Interest rates

Interest rates on bridging loans will normally be fixed for the length of the loan term, although variable interest rates can sometimes be an option.

How much you pay in interest will depend on a number of factors, including:

- The lender
- The size of the loan
- The length of the loan term
- Your Loan to Value ratio (LTV)*
- Your credit score (although this is not always required)

*Your LTV may be based on the current value of the property and/or the Gross Development Value (GDV) i.e. how much the lender believes the project will be worth once completed.

Exit fees

Not all lenders charge exit fees, but those that do require them to be paid when the capital is repaid.

Exit fees vary but, like arrangement fees, are based on a percentage of the total loan.

A specialist bridging loan broker can provide a range of finance options depending on your requirements.

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Regulated Bridging Loans

Bridging loans secured as a first or second charge on property you, your partner or a close family member live in are normally regulated by the Financial Conduct Authority (FCA).

This type of bridging finance is most commonly used in the following types of property deals:

Time sensitive property purchases

When you find the perfect property, you need to move quickly to secure your new home. Unfortunately, it is not always possible to sell your old house fast enough to free up the funds to buy your new dream home.

A bridging loan allows you to purchase the new property, move in, then sell your old property and use the proceeds to pay off the loan. With ever increasing competition for desirable homes, bridging finance can make the difference in securing the property you want.

Bridging finance can also be helpful if the sale of your old home has fallen through, or if your completion date is too far in the future to facilitate the purchase of a new property.

Downsizing

If you are downsizing because your current home is too large, or because you want to live mortgage-free, a bridging loan could allow you to move into your new smaller home while waiting for your old one to sell.

Once the old house has sold (and your old mortgage is paid off), you simply use the remaining lump sum to pay off the bridging loan, leaving you debt-free.

Auction finance

With most auction purchases you only have 28 days (20 working days) after the sale date to complete the purchase. This is not usually enough time to apply for a mortgage, so bridging finance is used to fill the gap.

Many lenders will be willing to offer indicative terms before the auction date if you have already identified a property you wish to bid on and can specify the maximum bid you are willing to make.

These terms are non-binding, but can give you a good idea before the auction of whether you will be able to borrow the amount you need and how much it is likely to cost you.

YOUR HOME MAY BE REPOSSESSED IF YOU DO NOT KEEP UP REPAYMENTS ON A MORTGAGE OR ANY OTHER DEBTS SECURED ON IT.

Non-regulated bridging loans

If you take out a bridging loan secured on a property not lived in by you, your partner or a close family member, if will likely be exempt from FCA regulation.

Loans may also be unregulated if secured on personal property, where the loan is over £25,000 and intended mainly for business purposes, or if you are regarded as a high net worth individual.

This type of bridging finance is commonly used for the following kinds of property deals:

Property refurbishment

If you are planning a property refurbishment or conversion, it may not be eligible for a traditional mortgage.

This may be the case if the property:

- Is derelict
- Does not have a kitchen or bathroom
- Is valued below £50,000
- Has structural defects

A bridging loan can let you complete the purchase and bring the property up to a mortgageable standard. You can then take out a mortgage or sell the property on to repay the loan.

Auction finance for investment properties

When buying property at auction to rent out or as a refurbishment project to sell on, you usually must complete the purchase within 28 days (20 working days) of the sale. This is not enough time to apply for a mortgage.

A bridging loan can allow you to complete the purchase within the deadline, then refinance with a buy to let mortgage, or complete the planned refurbishment work and sell the property on.

Bridging loans secured on other assets

Bridging loans can also be secured against other high value assets beside property. This type of bridging finance will normally be exempt from FCA regulation.

Other assets bridging loans can be secured against include:

- Stocks and shares
- Boats and other high value vehicles
- A business

Experienced developers may be able to borrow as much as 100% of the costs of their development as a bridging loan

Commercial Bridging Loans

If your company needs short term finance to purchase new premises, buy stock or invest in a new business opportunity, a commercial bridging loan could help.

Commercial bridging loans are similar to other bridging finance, except the loan is secured against assets belonging to a business not an individual.

Bridging finance is used by all kinds of businesses, but is particularly popular with commercial property developers.

Commercial property development finance

If you are a commercial property developer, bridging finance can allow you to move forward with new developments when other types of funding are not available.

It may be possible to secure the loan partially against the new development and partially against existing lots in your portfolio.

Experienced developers may be able to borrow as much as 100% of the costs of their development as a bridging loan.

Finance will normally be released in stages as the development progresses with interest only charged on the installments already received. This helps to keep costs down.

Exit plans for commercial property development bridging finance usually involve selling the completed property or properties.

This can make matters complicated, especially if there are multiple lots which will be unlikely to sell at the same time.

A loan broker with experience in commercial property development finance will often be able to resolve complicated issues such as these, which is why virtually all commercial developers use brokers for their bridging finance.

Applying for a bridging loan

When applying for a bridging loan, there are various things to consider, such as whether to use a broker or not, what information you need to provide to potential lenders and whether you will be able to get the money fast enough to suit your needs.

Using a bridging loan broker

Most people use a specialist broker when applying for a bridging loan for a number of reasons:

- Advice & market expertise
- Speeding up the process
- Getting a better deal on interest rates and fees
- Accessing specialist lenders not available direct to consumers
- Removing the hassle of contacting multiple lenders themselves

Choosing a lender

When selecting a lender for your bridging loan, look for a provider who is:

- Regulated by the Financial Conduct Authority (required for regulated bridging finance)
- A Member of the Council of Mortgage Lenders
- Experienced in lending on property

Information you need to provide

Lending criteria vary from lender to lender, but you will generally need to supply the following:

- Details of your income, expenditures, assets and liabilities (sight of income will depend on whether the bridging loan is regulated or not)
- Bank statements
- Valuation of the project carried out on behalf of the lender
- Detailed cost breakdown
- Timeline for the development
- All relevant planning permission documents
- Building regulations consent
- Your National House Building Council (NHBC) insurance details or an equivalent
- Your plan for repaying the loan (exit strategy)

Applying for a bridging loan (cont.)

Application process

Whether you use a broker or find a bridging loan deal for yourself, there are several stages to the application process:

Initial application – You or your broker approach a lender to discuss your borrowing needs. You will usually receive an agreement in principle telling you how much you can borrow, what interest you will pay and any fees.

Credit check – A credit check will be used to establish your credit history. Even if you have had bad credit in the past, you may still be eligible for a bridging loan, but this is likely to affect the interest rate you are offered.

Valuation – The lender will usually need to have their own independent valuation of your property or project before offering terms.

Agreeing terms – Once all necessary checks have been carried out and all relevant information provided to the lender, they will offer formal terms for the loan. You will need to have these checked by your solicitor and some negotiation may be needed before final terms are agreed.

Release of funds – Once the terms are agreed and signed by both borrower and lender, the money should be released into your account promptly.

How long will an application take?

It can take anywhere from a few days to several weeks to a go from an initial application to the release of funds into the borrower's account.

A good broker will normally be able to significantly speed up this process due to their experience and established relationships with lenders.

Bridging Loan Case Studies

Bridging loan for auction finance

Location: Stoke Newington, London
Loan value: £220,000
Loan term: 6 months
Loan-to-value: 65%

A client in London won a property at auction to refurbish and sell on. They paid a 10% deposit to secure the property and needed to pay the balance within 28 days. They also needed money to fund the planned renovation.

The client approached several mortgage lenders, but none could provide the finance fast enough. If the client could not find an alternative source of finance fast, they would lose the property and their deposit.

We were able to find the client the £220,000 they needed as a bridging loan within 24 hours. This let them complete the auction purchase and left enough money for all of the required refurbishment work.
We secured a 6 month loan term at a rate of 0.99% per month with no exit fee or penalty charge for early repayments.

This gave the client enough time to complete the planned work on the property and resell, while keeping their monthly repayments affordable, resulting in a healthy profit margin.

Bridging loan for downsizing

Location: Reading
Loan value: £196,000
Loan term: 9 months
Loan-to-value: 50%

A recently widowed woman contacted us looking to finance the purchase of a new home. She wanted to move to a smaller property nearer to her children and had found the perfect place.

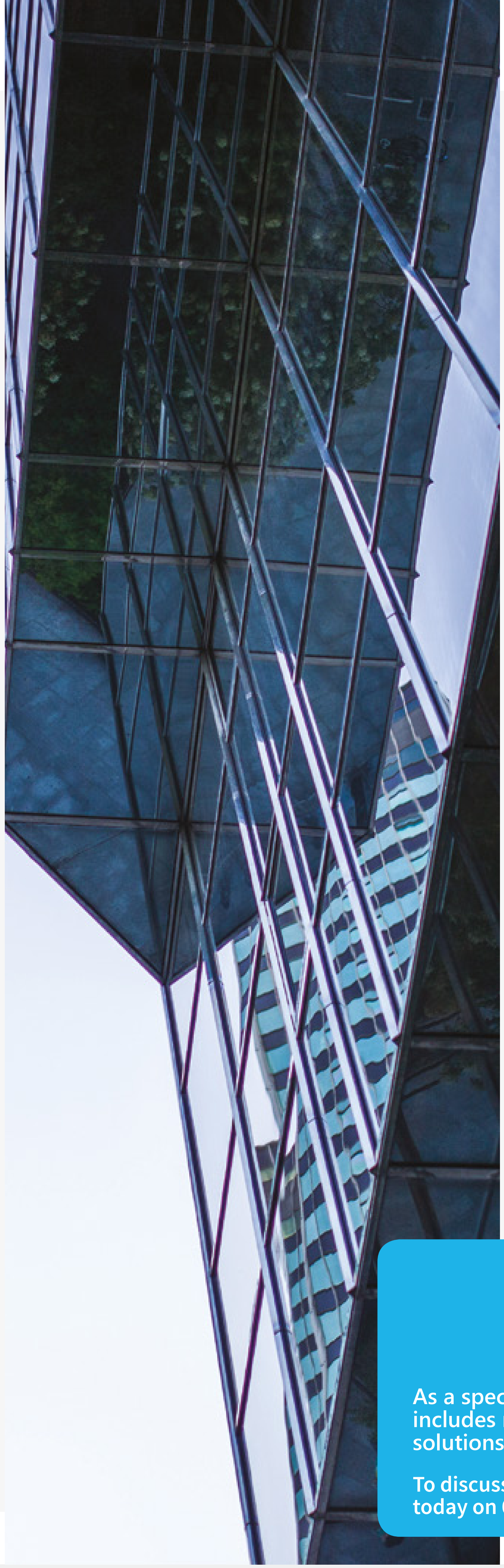
The new property was significantly cheaper than her current home, meaning she would be able to live mortgage-free once she had made the move.

Unfortunately, she did not have a buyer for her old home and was worried about missing out on the perfect property she had found if she waited.

She also wanted to minimise the stress of the move due to her personal circumstances and large volume of personal possessions of hers and her late husband's she needed to sort through.

We found the client a bridging loan for £196,000, covering the cost of her new home, with a loan term of 9 months. This gave plenty of time for a low-stress move and the sale of the old home.

The relatively low loan-to-value ratio helped us secure an attractive interest rate with the interest rolled-up so it could be repaid along with the capital when the client's old home sold.



Bridging loan case studies (cont.)

Bridging loan for buy-to-let refurbishment

Location: Bristol
Loan value: £224,500
Loan term: 12 months
Loan-to-value: 65%

A landlord with an extensive portfolio of buy-to-let properties needed funds to refurbish a property he had recently found.

He had planning permission to add extra bedrooms with the potential to significantly increase the property's rental value. The work was projected to take 9 months.

The landlord had experience buying and renovating properties for rental, but this new property was deemed uninhabitable, making it impossible to get a buy-to-let mortgage.

He needed £224,500 to buy the property and make the necessary improvements.

The landlord contacted us and we quickly found him the money he needed from a lender who specialises in development finance.

We secured a loan term of 12 months, giving the landlord enough time to buy the property, renovate it and then refinance with a buy-to-let mortgage.

We also negotiated no exit fee or early repayment charge. This let the landlord minimise his costs and gave him the flexibility to repay the loan early if the work was completed on schedule.

It also left an extra 3 months contingency in case the renovation work overran.

Please note: These case studies are representative examples based on actual cases.

Get Expert Advice on Your Property Finance Options

As a specialist finance broker, we have access to a wide range of leading UK lenders. This includes many not available directly to borrowers. As a result, we can offer the very best solutions on bridging loans to our customers, providing finance that fits your situation.

To discuss your borrowing requirements with one of our experienced brokers, call Fair Mortgages today on 0117 313 6058 or request a call back.

Bridging Loans Hotline

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