

☑ **WHAT ARE TRIPLE NET (NNN) PROPERTIES?**

A “triple-net” (NNN) property is a commercial investment property typically leased to a single tenant. The name refers to the lease structure, specifying that the landlord is responsible for property expenses net of taxes, insurance, and maintenance. In other words, the tenant is responsible for all property expenses, and the landlord investor is due the net base rent amount. Triple-net properties are great options for investors that want to diversify funds into commercial real estate, but also want to be a “hands-free” landlord. The simplicity of the properties allows them to be a more liquid investment compared to multi-tenant commercial, multifamily or special purpose properties.

In searching for NNN investment properties, **HARBORWEST** recommends you should always have the lease structure specified and investigate the actual lease. The structure may be a double-net (NN) lease with the investor responsible for maintenance, or a single-net (Net) with the investor responsible for insurance and maintenance. And unless specified as Absolute NNN, the investor may still be responsible for capital expenditures including the roof, structure and parking lot as major repairs and replacements are needed over the term. You should complete your full due diligence with your buyer’s agent and contract attorney on this topic.

Popular NNN properties are nationwide retail tenants with thousands of locations. This includes companies like CVS, Walgreen’s, Dollar General, AutoZone, DaVita Dialysis and McDonald’s among other well-known options. Many of these are considered “credit tenants” if they are investment grade rated BBB- or higher by Standard & Poor’s (S&P).

☑ **WHICH FACTORS ARE MOST IMPORTANT TO NNN FINANCING?**

Financing triple-net (NNN) properties is a specialty within commercial real estate lending. Personal financial and credit qualification are assessed for each borrower, but there are specific property qualification factors that **HARBORWEST** recommends our investors consider when pre-screening potential NNN investment properties:

- **TENANCY.** Your primary question should be, who is the tenant? You are not purchasing a property, you are purchasing a leased income stream that is collateralized by a property. The tenant’s financial health to uphold that lease agreement is the most important factor to lenders. Tenants are more desirable if they are larger, higher investment grade, with strong store sales history or public financials. Larger tenants will also have more data for lenders to assess. “Mom n’ pop” tenants and non-credit tenants usually fall into a different lending bucket than the types of tenants described herein.
- **OPERATOR.** Your next question should be, is this a corporate guaranty or a franchisee tenant? Corporate guarantees are always preferable and carry more strength. If the tenant is a franchisee, you’ll want to investigate how many locations the franchisee operates, where those locations are in respect to the subject property, and how long they’ve been in business. You’ll want to ask if the lease specifies that tenant financials and store sales are to be made available upon request, and if there is a personal guaranty from the franchisee.

- **LEASE TERM.** How long is the remaining lease term? Marketing can be misleading, as the remaining term in the current lease period is different than the potential lease term if options are exercised. Tenants are not lease responsible to accept any option period. A vacant (dark) property seriously escalates the risk of loan default, so lenders prefer their loan term to expire prior to the lease term or be co-terminous with the lease. In general, the longer the lease, the more attractive loan terms will be offered. Typically (7+) years remaining is the hinge point for the most competitive loan programs.
- **COLLATERAL.** This is the most overlooked and misunderstood factor. You'll want to verify upfront if the property is Fee Simple (own the land and building), Leased Fee (own the land / ground lease), or Leasehold (own the building, but not the land). Most listing are fee simple and accepted by all lenders, Leased Fee (ground lease) properties are less desirable but still lendable, and Leasehold properties are more difficult to finance with minimal options. If a listing is a ground lease, typically with triple-net properties on long-term leases, the building ownership will revert to the ground lessor should the tenant vacate.
- **INCOME.** Each individual property will have a net operating income (NOI) which is the net income due to the investor after all expenses are paid. The lease structure will determine this number and is used as the basis for all lender calculations. Each lender will have their own unique underwriting guidelines to determine the required down payment, maximum loan amount or loan-to-value (LTV), and subsequent lease terms including the interest rate. In general, the higher the capitalization rate ("cap rate") and net operating income (NOI), the stronger the cash flow which equates to better interest rates and higher available LTV's.
- **LOCATION.** The last, but equally as important, factor when evaluating a NNN property for eligible financing is the location. Typically, a listing will note population size within a 1-mile, 5-mile, 10-mile and 25-mile radius. Properties located in more populated areas and larger MSA's (metropolitan statistical area) are more desirable to lenders as the retail tenant will see higher customer traffic. The 5-mile figure is most referenced, with most lenders wants to see 10,000 or more people within that radius.

WHAT DOES A NNN LOAN STRUCTURE LOOK LIKE?

Each lender has competing appetites for different tenants, locations, property profiles and deal hurdles. The market is constantly changing and **HARBORWEST** can ensure our clients are educated on their qualification for specific program terms, but also what can be negotiated and customized to meet their goals. **CONTACT OUR TEAM** for a complimentary consultation.

- Maximum 75% LTV, industry average 65% LTV, determined by NOI & deal risk
- Loan term (due date) typically 10 years, or co-terminous with lease end date
- Fixed rate period options of 5, 7 or 10-years fixed, on an increasing scale
- Principal with interest payments standard, interest only payments uncommon
- 25-year amortization standard, with 30-years available for strong requests
- Stepdown prepay penalty structure is standard, with no penalty options available
- Full recourse standard, with partial or non-recourse available on limited basis
- Property reports required including appraisal, environmental and survey