



“How Brokers Can Make Money from Real Estate Receiverships”

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California Real Estate Receiverships

Newport Beach, CA

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Receivers

"I am most encouraged with the strength of our business so far in 2009.

We are profitable through the first two months of 2009 and are having our best quarter-to-date performance since the third quarter of 2007."

Citigroup Chief Executive Vikram Pandit in memo to staff



Receivers

"What really got the market going was the Vikram Pandit memo from this morning.

Any little hint of good news and this market was going to take off."

Stephen Massocca, managing director at Wedbush Morgan in San Francisco



Receivers

"It was like some kids saying the emperor has no clothes, and then after he says that, he says now that the emperor doesn't have any underwear either."

Warren Buffett on severity of U.S. home price declines and effects



Receivers

- **When used?** During disputes; To operate an enterprise (General Motors, etc.) or real property (during foreclosure).
- **Start** – Typically, concurrent with an event, such as delivery of a Notice of Default.
- **End** - When the purpose of the receivership has ended (i.e. maintenance of property - during foreclosure, until a loan workout; until note is sold (if successful in discharging receiver).



Rents, Issues & Profits (Real Estate) Receiverships

- **Purpose?** – Protect rents and the asset value (for the lender/plaintiff) from diminishing during in a non-judicial foreclosure action.
- **What's the worry?** – That owner/borrower/defendant (“O/B/D”) will “waste” the loan collateral (real property). She/he might..
 - Cash out the asset bank account (including deposits)
 - “Pocket” the rental income vs. pay loan payment interest
 - Stop “watering the grass”, and maintaining the asset
 - Not pay vendors (including real estate agents)
 - Let entitlements expire



Rents, Issues & Profits – (cont)

- Avoid / Reduce Liability
 - Avoid “mortgagee in possession” and the attendant liabilities i.e.
 - ❖ Construction Defect (residential)
 - ❖ Environmental
 - ❖ Injury / Property Casualty
- Minimize deficiency (O/B/D);
- Maximize return of loan (lender/plaintiff)



The “Process”

- Lender (Bank or CMBS Special Servicer) requests their legal counsel draft an “appointing order”
- Either lender or lender’s counsel identify a receiver matching the needs of the real property / loan collateral (product type, location, complexity, value)
- Appointing order is submitted to a judge in the court of jurisdiction (county in which asset is located)
- Judge can either :
 - “accept” the recommended receiver;
 - “substitute” for a receiver of their preference or
 - “reject” the appointment of a receiver entirely



Fiduciary

- The receiver is an “officer / agent of the court”; a fiduciary
- Receiver is a neutral party; although the lender (typically the plaintiff in the action) routinely nominates / recommends the receiver
- Receiver reports to the court (presiding judge); keeps the plaintiff / lender and OBD apprised of their actions
- Receiver is “an individual” (in most states i.e. CA, AZ, NV, etc.) . Illinois and other states will allow a *company* to be a receiver

Upon Appointment of Receivership Estate, Receiver...

- Takes “effective” control of the asset / loan collateral (borrower retains title)
- Notifies OBD (by submission of the appointing order); and requests / demands all documents (leases, operating expenses, plans, permits, etc)
- Existing contracts with OBD are voided.
Notifies the tenants (that rents are to be made payable to the receivership “estate”)
- Notifies IRS, Property taxing authorities; Utilities – for billing
- Notifies 3rd party service providers – Receiver will typically “re-hire” property management, leasing, landscaping, etc



Upon Appointment..(continued)

- Task – to preserve the asset value until end of the receivership estate (typically 4-5 months)
- Bill “the estate” hourly (rate in the appointing order) monthly
 - From funds transferred from borrower’s account
 - From Rents
 - From lender/plaintiff via Receivership Certificates
- Can modify and execute leases (for up to 12 months - longer with an amended order)
- O/B/D – usually retains title



During Receivership Estate

- Receiver Employs –3rd party consultants (asset or property management, leasing / sales agents, construction managers, contractors, architects, legal counsel, etc.)
 - 3rd Party vendors are “at will”.
- Receiver Evicts – files Notices to Pay or Quit, Unlawful Detainers, Summons & Complaint, to wit they are assigned to new owner
- Receiver Sells – (Most common in single family) upon agreement of the parties to the action and court.
 - Plaintiff – to avoid liability,
 - Defendant – avoid foreclosure on record



Upon Termination of Receivership Estate

- Provide Court Receiver's "Final Report and Accounting" (of income and expenses) to the court
- Provide New Owner (typically lender / plaintiff) – *Stabilized* asset and documentation to be used by REO or OREO depts. for disposition
- Notify All Parties – tenants, IRS, utilities, vendors, etc. of title transfer and new owner (and/or P.M contact information)



Impact of Credit Crisis on Commercial Assets

- \$6.7 trillion in commercial real estate that is privately owned
- *Maturing* during 2009-2014:
 - **Banks** -1.3 - \$1.7 trillion (50%);
 - **CMBS** - \$700B (22%);
 - **Life insurance** (9.5%),
 - **Government** sponsored entities / Agency (9.5%);
 - **Savings** institutions (9%),
- Lenders – “extend and pretend”; 12 months



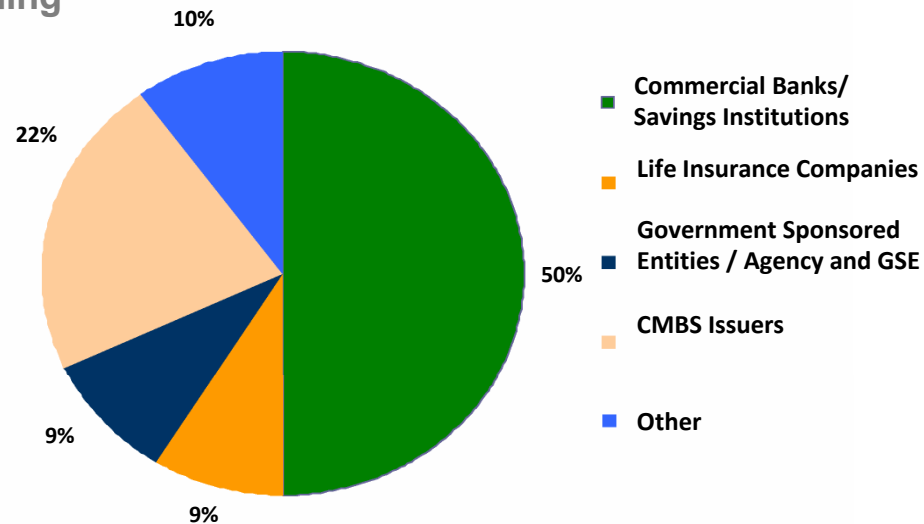
Impact of Credit Crisis on Commercial Assets

- McKinsey Research - estimated total CRE loss at commercial banks over the next 2-3 years to be \$430B, (*less than 10% had been taken by 8/30/09*).
- 2009 default rate (2.88%); forecasted default rate for 2010 (5.2%), most of which will require receivership.
- CMBS is moving to Special Servicers from Master Services “before” default, as values decline; mortgage-over-value (\$1.6B/mo as of 12/08). *One week, by committee.*



Outstanding Debt

\$3.4 Trillion Debt Outstanding



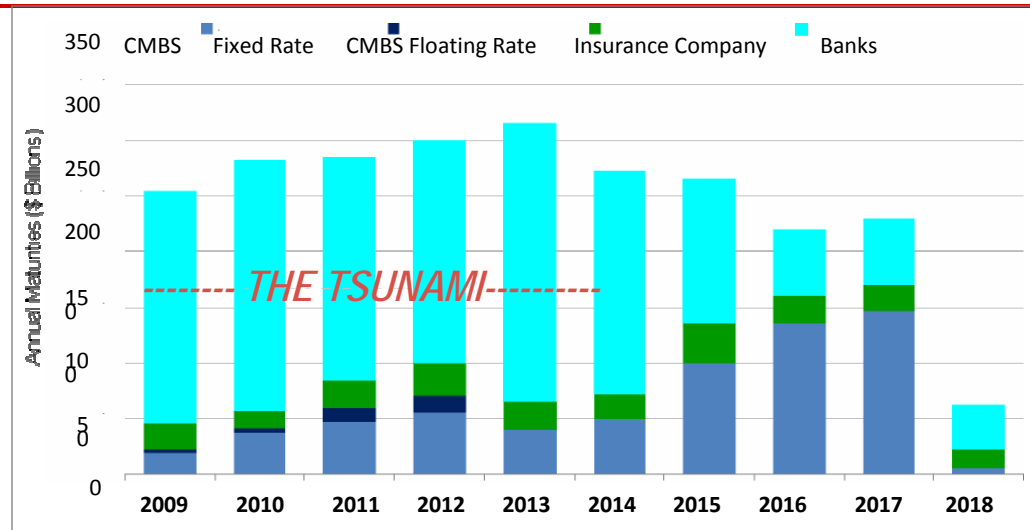
- The banks account for about 50% of the outstanding real estate debt. CMBS accounts for over 20%, with life companies and government agencies both accounting for less than 10%.
- During the four years of 2004 – 2007, the commercial real estate loan volume exceeded \$1.4 trillion, more than three times the loan volume during the prior four year period of 2000 - 2003.
- McKinsey Research recently estimated the total CRE loss at Commercial Banks over the next 2-3 years to be \$430B, of which less than 10% has already been taken.

California Real Estate Receiverships



Maturity Profile of Banks, CMBS and Life Companies

Estimated maturity profile of commercial mortgages in CMBS, life company and bank portfolios

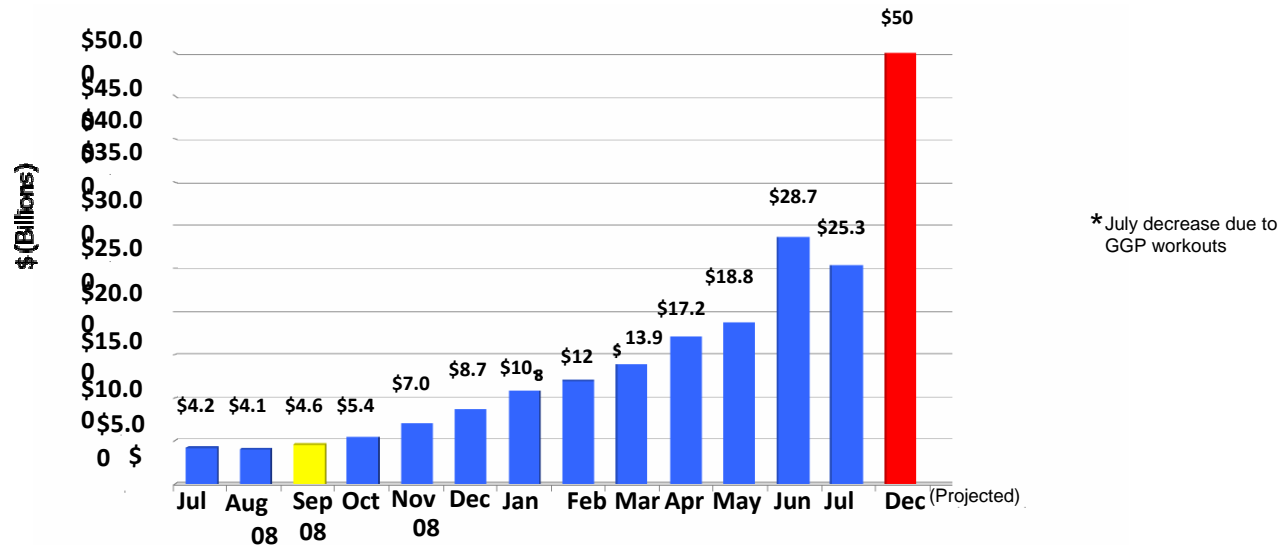


- Loan maturities from CMBS, life companies and banks are expected to total \$1.4 trillion over the next 5 years; the same amount that matured over the last 15 years (1994 – 2008) when capital was abundant.
- Banks have \$1.7 trillion, CMBS has \$700 billion and life insurance companies have \$200 billion in direct loans maturing through 2018.
- The period of 2010-2013 will be one of unprecedented stress and disruption in the U.S. real estate capital markets, a time when lenders could be forced to take massive losses on their commercial real estate portfolios



Monthly CMBS Delinquency

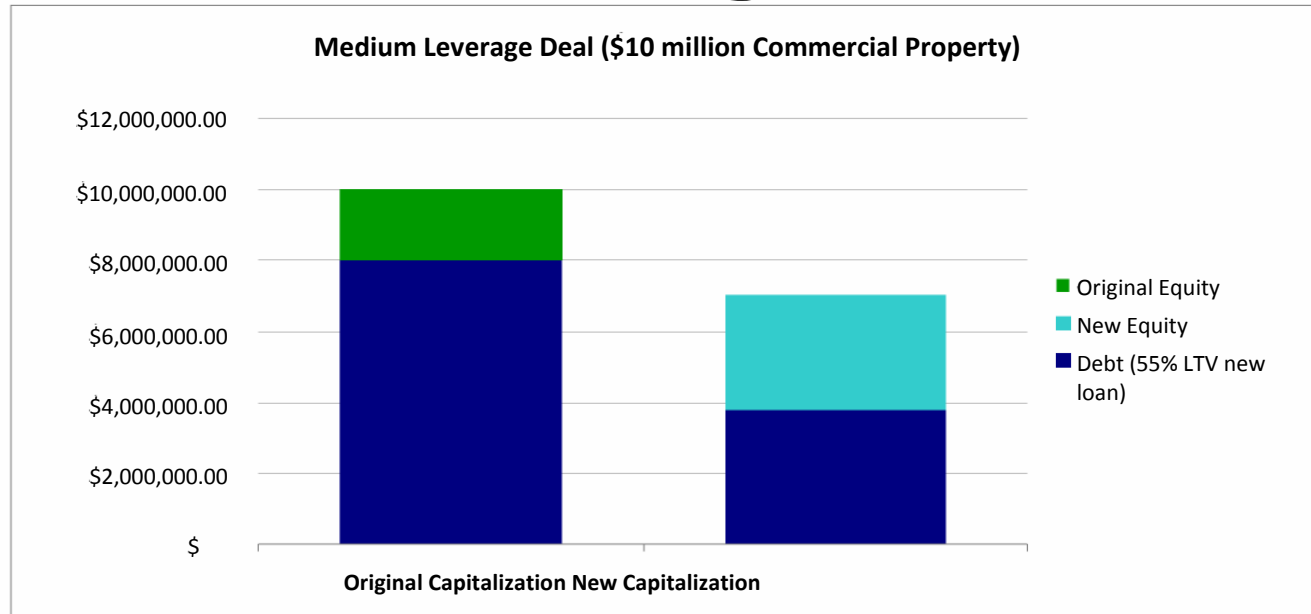
**Monthly CMBS
Delinquency Balance**
(source: Realpoint)



- CMBS delinquency is about 6.5% of the outstanding debt. This figure is more than 6 times what it was 12 months ago.
- This delinquency figure is expected to exceed \$50 billion, or over 7% of outstanding debt, by end of '09, an increase of about \$40 billion for the year.
Only 38 percent of June CMBS loan maturities paid off, and most of those were small loans originated 10 years ago.
- Non-maturity loan defaults are increasing.



Refinancing Shortfall



- Two major trends prevail: (1) commercial real estate values have declined, and (2) loan-to-value ratios have declined.
- The de-leveraging problem depends on the extent of leverage which was used in the past...institutional vs. non-institutional product/sponsorship.
- This chart depicts a \$10 million “commercial” property, where the investor borrowed \$8 million (80% LTV) and assumes value of the asset has decreased 30%...a new loan of only about \$4 million is achievable.

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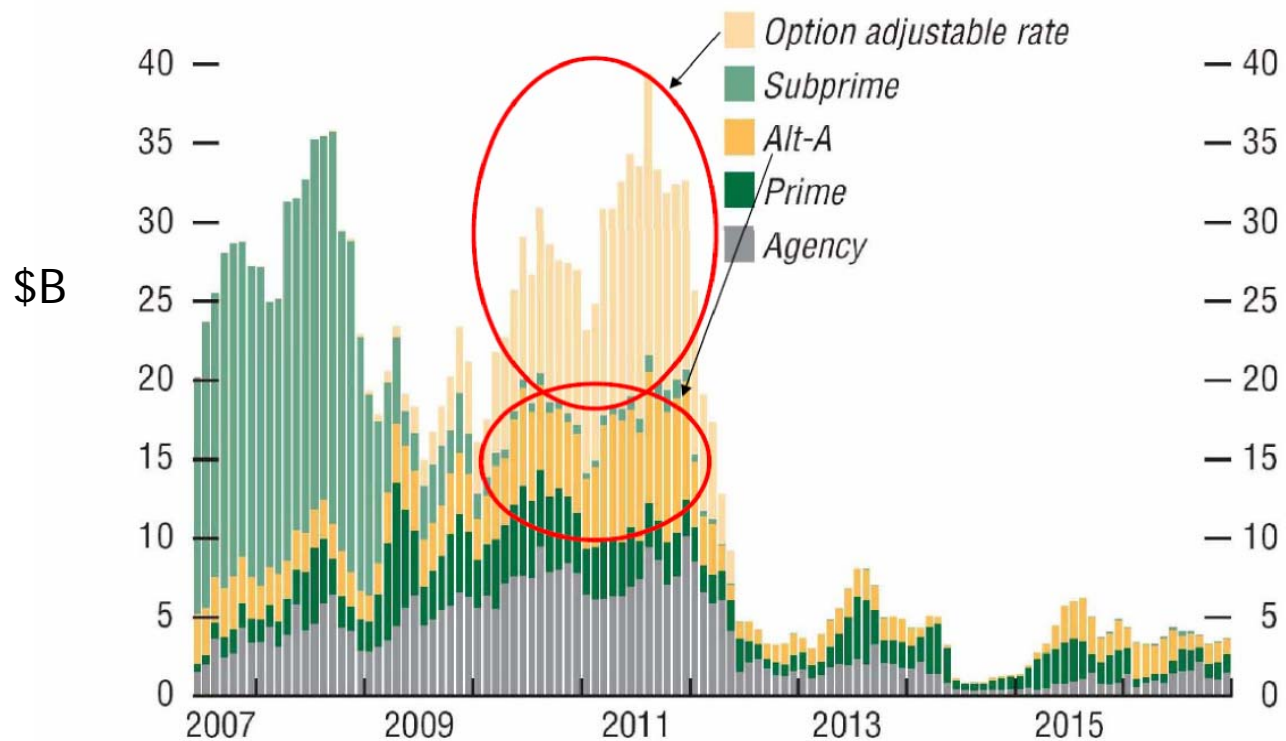
We All Know the Cause

- The increase in value of commercial real estate in the years 2004–2007 was primarily due to cap rate compression, in part due to high leverage levels.
- The potential refinancing of all these loans will be adversely affected by three diverging trends:
 - A decrease in the value of the property due to cap rate inflation.
 - A decrease in the LTV ratio for a new loan.
 - A decrease in NOI at the property due to market fundamentals / job loss.
- Low transaction volume since mid-2008 has made it difficult to determine “actual” market cap rates...sales volume nationally is down about 80% from a year ago and 90% from 2007.



Housing market not out of the woods

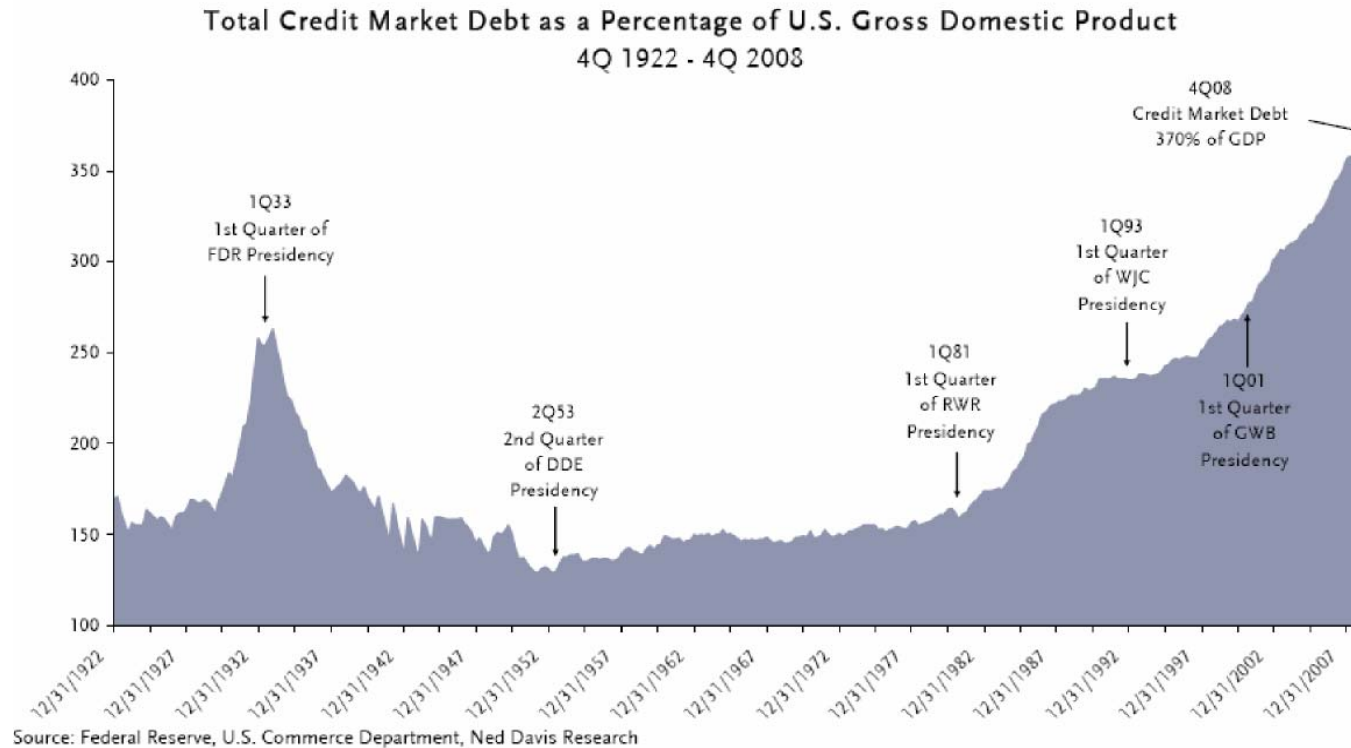
- Monthly Resets on troubled mortgages will pressure housing for two more years



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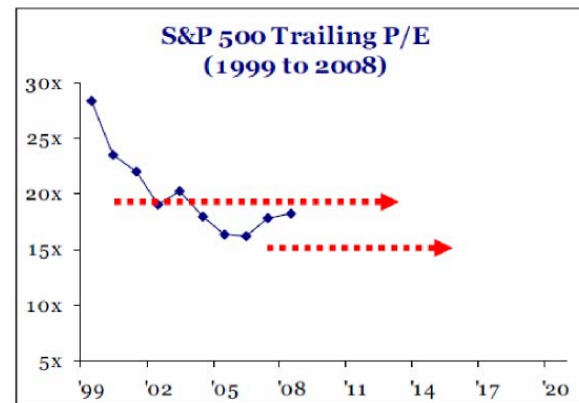
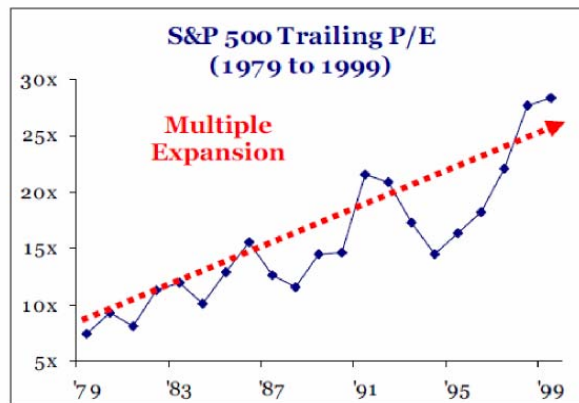
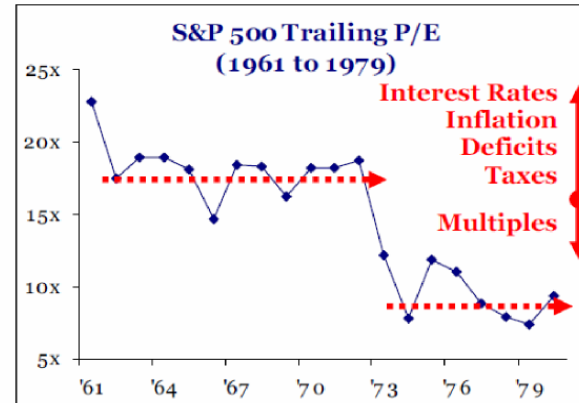
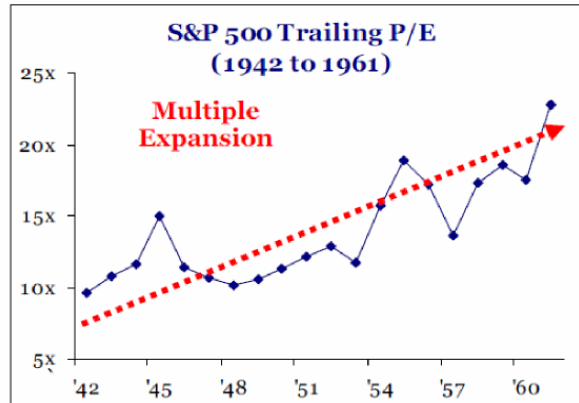
Too much debt is the long term problem



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Investors should not count on multiple expansion

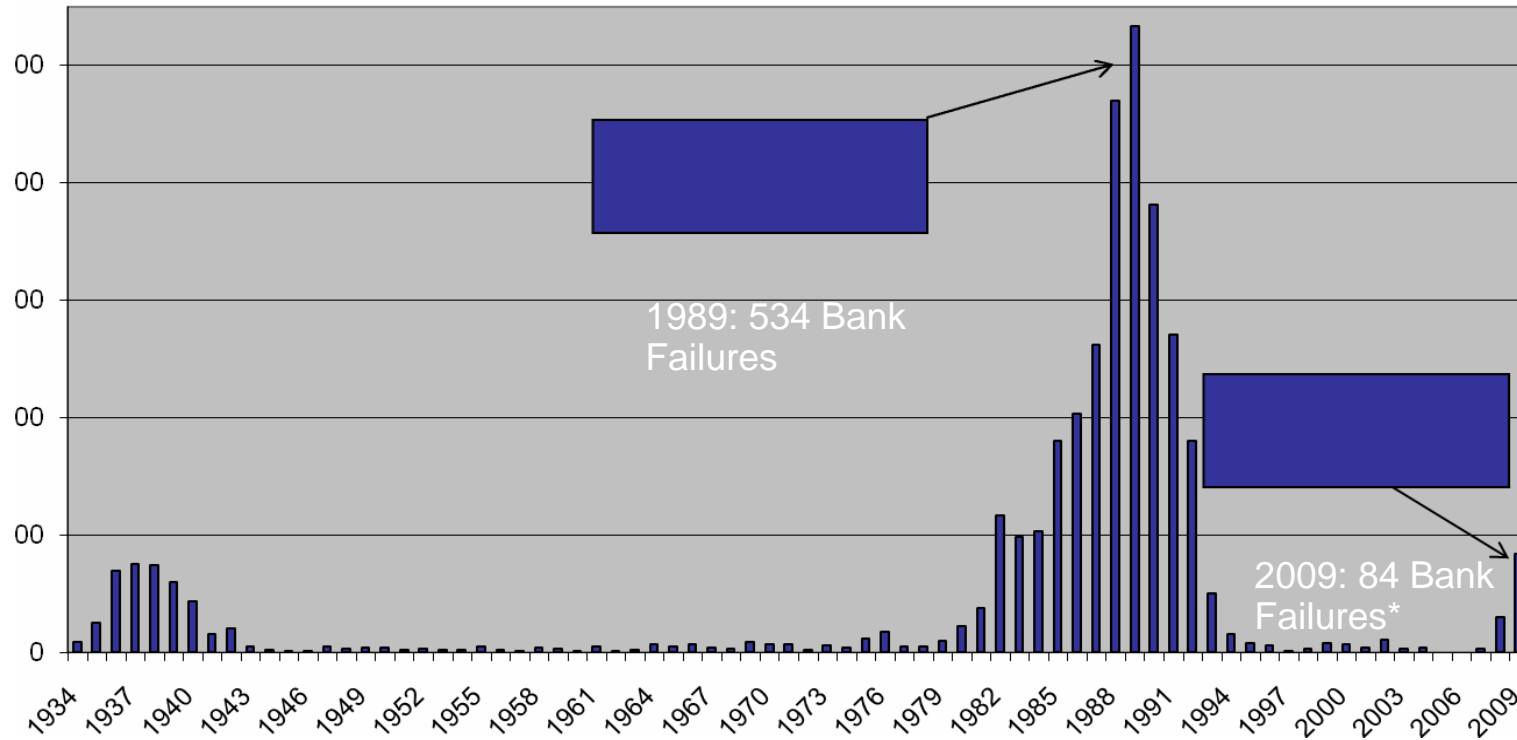


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How Today Differs from the 80's

Bank Failures & FDIC Assisted Transactions



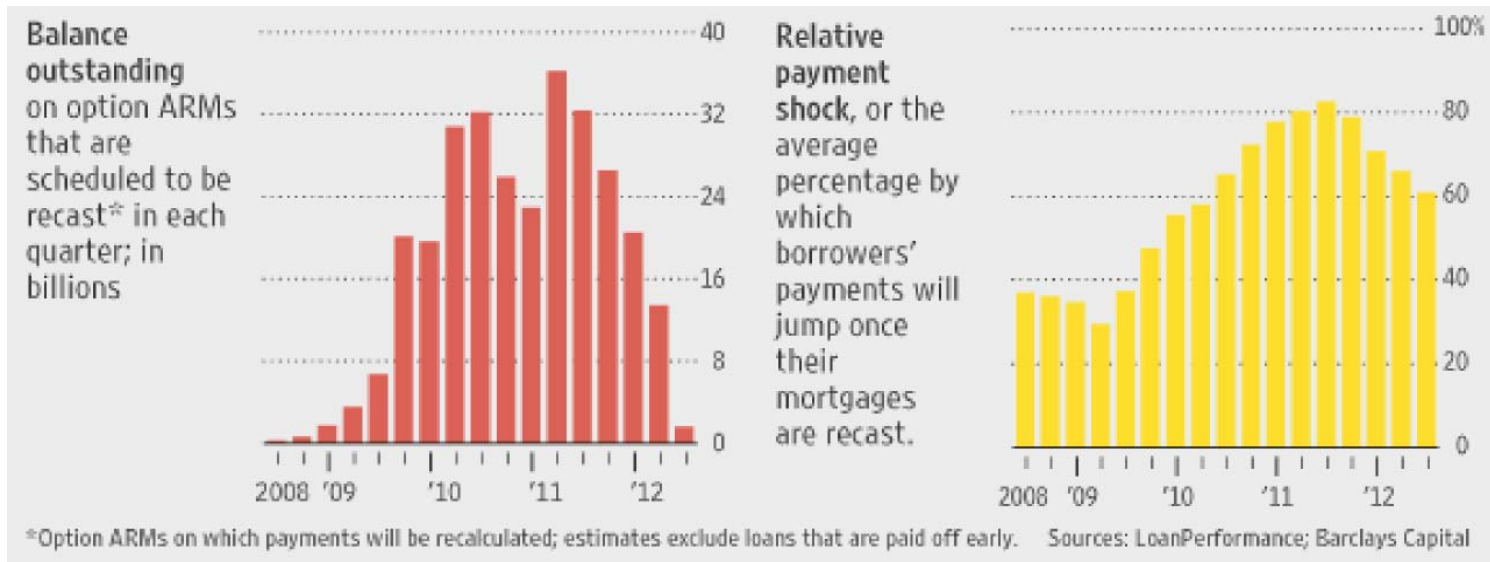
2008 Amegy Bank N.A. Member FDIC.

*As of 9/1/09

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What will be the Impact of Option ARMs?



Source: *Wall Street Journal*

2008 Amegy Bank N.A. Member FDIC.

California Real Estate Receiverships

New Clients During the Credit Crisis

- **Receivers** – They are the initial point-of-contact for *interim work* for many of the defaulting assets.
- **In Place** – When in place and employed by a receiver, many if not most new owners (lender or note buyers that foreclose on the note) will retain 3rd party consultants through disposition.
- **New Owner** – They’ve written down the asset and are (often) “motivated” to sell (bank or 3rd party).
- *Introduce receivers to your lender contacts* (receivers will likely contact you for any brokerage work sourced from that lender in the future)
- Email “basics” of troubled assets (*BEFORE N.O.D.*) to receivers; you will be their 1st Point-Of-Contact for leasing / sales of that property.



Closing Thoughts...

It's ideal if you are:

- the 1st born,
- 2nd wife,
- 3rd broker and
- “past” president!



Closing Thoughts... II

“It is better to be silent and thought a fool, than to speak and to remove all doubt”

Mark Twain



Thanks!

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