"In dealing with 'work-out' situations for financial institutions, the primary goal of the real estate consultant is to help preserve asset value and to disentangle the institutions from operational problems for which they are ill-equipped", commented Daniel Rose, partner of Rose Associates, one of the nation's leading builder-owner-management organizations.

"The competent real estate 'doctor' can provide the expertise which will permit the institution to return to the role of passive lender, and to leave planning, construction and management headaches to experts in those fields," Rose feels.

Just as medical men have areas of specialization, so do real estate "doctors" ; some specialize in consultation, analysis and advice; some, in the reorganization of sick companies and in the disposition of large-scale problem properties; others, such as Rose Associates, specialize in completing the construction and in renting and management of stalled projects, in addition to general consultation.

The first step to be taken with a problem property is a thorough analysis of the job and a review of all feasible alternatives.

"The lender has several options available when faced with a defaulted loan," explained Mr. Rose

He can: 1) re-negotiate the debt agreement with the existing developer; 2) start foreclosure proceedings; or 3) attempt to acquire the deed in lieu of foreclosure.

If the property is acquired, the lender can: 1) attempt to dispose of it "as is"; 2) provide necessary fresh financing to permit a new developer to acquire and complete; or 3) have the institution undertake completion of the project for its own account.

"Each of these alternatives has pros and cons which must be considered in the light of the particular circumstances," Rose observed. "Generally, foreclosure is costly and time-consuming; and if an owner resorts to bankruptcy protection under Chapter 10, 11 or 12, the lender may end up waiting indefinitely to obtain possession."

Taking the deed in lieu of foreclosure usually entails paying off the foreclosed owner for his "nuisance value" and also relinquishing any outstanding claims against him.

In either case, the lender is then left with property he is not prepared to handle.

"Real estate specialists must first help a lender to distinguish between a permanently sick situation and one with sound underlying values which were clouded by temporarily adverse conditions or by under-financing" In some cases, notes Rose, "where the total value on completion will actually be less than the cost to complete, the use of bulldozers might be advised".

Problem loans generally fall into several broad categories:

Case One: <u>Underdeveloped Land</u>

Underdeveloped land problems involve situations in which large parcels have been acquired that still need sewage, utility lines, roads, etc. installed to make the land ideally marketable. The real estate "doctor" evaluates the project to determine whether the project justifies the additional investment. Such a situation now exists in the Orlando, Florida area where the institution was advised to put the property on the market "as is", with favorable financing for a sound prospective purchaser. Prospects for recapture of loan principal are still undetermined.

Case Two: <u>Partially Developed Property</u>

In some cases the infra-structure may be in place and some portion of a planned community may be completed. However, money may have run out and the project may require additional funds to complete the "amenity package".

In one such case, with legitimate, but unforeseen cost overruns; but with good prospects, the lender was advised to re-cast the loan to capitalize interest for a period, and to advance to the original developer funds necessary for completion. In another case, where fraud or gross incompetence was indicated, a new developer was suggested for completion.

In the first instance, the lender now has participation prospects that may well return not only the original loan and interest, but a share of indicated profits as well.

In the second instance, the lender will be lucky if he can recapture the bulk of his loan.

Uncompleted high-rise construction is another problem in this category, and because of the large sums involved, great care is required in the analysis of such a project.

In some cases, the job should be scaled down in size or otherwise redesigned; in others, converted from rental to co-op/condominium or the reverse, depending upon local marketing conditions; in some cases, common sense dictates ploughing ahead and finishing what was planned originally. Sometimes, a sale of tax losses can provide crucial additional "front-end" capital.

In all such situations, however, indicated action should not be delayed unnecessarily, as all concerned lose by shutting down a job for an extended period. Interest is running, taxes are accumulating, and usually the physical construction deteriorates in the interim.

The worst of such situations seem to be "consortium" loans, where several institutions are involved in one large loan and are unable to agree on remedial steps.

Case Three: Completed Projects Unable to Pay Debt Service

This situation may have endless variations. Mr. Rose cites a shopping center where the major tenant went bankrupt, leaving the bank with a large shopping mall and no lead tenant.

Rose Associates was called in to find a lead tenant,to manage the project and to dispose of it.

In another situation, an electrically heated building originally built as a condominium ran into substantial cost over-runs. The original loan was sold to a second institution who called in Rose Associates to manage the building.

The proposed Rose program involves converting the heating system to oil, modifying layouts and adding amenities which will help make the building marketable. In addition, the condominium is being converted into rental units.

Rose has bought the mortgage and will keep the project in their own portfolio.

In the above instances, services were performed for institutions which they would have been hard-pressed to perform for themselves.

These generally break down as follows:

1) Real Estate Tax Appeals and Abatements:

On acquisition of property, lending institutions usually pay their real estate tax arrears as billed. The real estate specialist, on the other hand, as a matter of routine checks to see if any previous tax payments of "open" protested years may possibly be applied to current bills in settlement.

2) <u>Zoning, Land Use, Environmental Problems and other Government Negotiations</u>:

Public officials tend to look on financial institutions as "bottomless pits" and to deal with them accordingly. The competent private developer can generally act much more effectively on a given project than can an institution.

3) <u>Packaging and Sale of Tax Losses</u>:

This is an area that often calls for technical ingenuity and sophisticated "horse-trading".

4) <u>Marketing, Renting and Selling:</u>

These require specialized skills, not only in implementation, but in programing and supervision as well.

5) <u>Operational Trouble-Shooting:</u>

The need for operational expertise here is self-evident.

In one foreclosed rent-controlled building in New York, Rose Associates, on behalf of an out-of-state bank, is in the process of re-casting real estate taxes, operating expenses, and rental income through a capital improvement program, tax appeal and "hardship" application that may well create a substantial "bottom line" where none existed before.

It seems clear that knowing what to do with a "bottom line" is one thing; creating it is another. It is the function of the lending institution to deal with the first, and for the real estate specialist to deal with the other.