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We Can't Start 'Til We Finish

By **Billy Procida***

When I sat down to write this article, I reviewed what I'd written over the last year, looking for something that has changed in the market. Unfortunately, I could not find much. What I did find, however, was a common issue: there are thousands of commercial real estate developments out there that are unfinished. These projects are mid-construction, the developer has depleted all available funds and the banks' current balance is worth less than par.

Getting these projects going again is critical to the long-term health of the commercial real estate market. The sooner that any half-built projects are finished, the faster the market can absorb them. And these half-built projects need to get off the ground so that the backlog of shovel-ready projects can begin.

To start this process, banks will need to invest additional dollars to protect their collateral from deteriorating. Any money banks invest would be money well spent, if handled properly. It can only enhance the value of the project as well as the bank's investment. Smarter banks will go as far as to see the projects through to completion, obtaining the certificate of occupancy.

One critical part of this whole process is for banks to get their paperwork in order. Many bank loan files tend to lack required interim information such as shop drawings, weld tests, concrete tests and surveys. All of these are needed to finish projects and get certificate of occupancy approval. In addition, copies and assignments of all the professional and construction contracts, including warranties and guarantees, are probably missing from the loan file as well.

It may be hard, however, to reconcile what the borrower and lender each want. For example, the borrower may want to be removed from the guarantee and the lender may want his money back. But because the borrower and the banker who used to be golf buddies are now enemies, the solution may seem obvious

and yet the parties are unwilling to see the big picture. Instead, lawyers for each party go back and forth, legal fees build and the project remains semi-complete.

This can have an extremely negative impact on the projects. Projects that are not weatherized prior to the onset of another cold winter will hyper-deteriorate. The value of the project depreciates as relationships worsen and litigation continues.

Sure, if you are the lender, you can foreclose, throw the developer out and proceed on your own. But it is far more efficient and cost-effective to get the borrower into a forbearance with a deed in lieu of foreclosure—I suggest held in escrow, so as not to convey title and the liability that goes with it—then trade for all the significant bits of information and documentation necessary to complete the project. But if the borrower cooperates, you can agree to forgive all or part of their guarantee. It's probably worthless anyway.

Solutions to these problems are simple if the parties agree to cooperate with each other. This will also allow everyone to avoid un-recoupable legal fees and save time and money instead of recreating the wheel and repairing the damage of a semi-built project. A finished project creates opportunities for investors to bid on the note or the fee interest without assuming reserves for unknown structural defects and other variable conditions.

Re-starting these projects is a step that needs to be taken to get the commercial real estate market going again. The question is IF and WHEN it will happen.

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