

Loan Defaults

Friendly foreclosures gain popularity when all else fails

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By: Polyana da Costa

More than two years into the real estate crisis, many developers and property owners in South Florida are learning the hard way that there are times when you just need to let go — and now is one of those times.

With no recovery in sight, borrowers with multimillion-dollar loans in default are becoming more open to so-called friendly foreclosures, rather than fighting a costly — and usually unsuccessful — court battle.

The nation's largest condo development company, the Related Group, recently gave up ownership of a high-profile West Palm Beach residential building to rid itself of a \$119 million construction loan by a lending syndicate led by the Bank of Nova Scotia. The developer announced the friendly foreclosure soon after a foreclosure lawsuit was filed in Palm Beach Circuit Court but said it had been negotiating with the lender since January.

Representatives of America's largest pension fund, the California Public Employees' Retirement System (CalPERS), and partner Miller Advisory Group also told the Daily Business Review they were going to let a \$138 million foreclosure lawsuit against their Downtown at the Gardens mall in Palm Beach Gardens be a friendly one.



Thomas Lehman

The mall owners already have filed a document in court agreeing to the final summary judgment and said they have transferred their ownership interest to the lender, which is proceeding with the foreclosure to protect itself from other parties that may claim an interest in the property. By going through the foreclosure process, the senior lender typically can wipe out all other smaller claims against a property, including mezzanine loans and mechanics liens.

Attorney Dan Kaskel of Sachs Sax Caplan, who assisted the financially distressed EB developers in several friendly foreclosures when he was counsel for the company, said he is working on about eight friendly foreclosures involving residential and office developers, warehouse owners and other commercial projects, as well as homeowners.

Click play to listen to Dan Kaskel



"The borrowers that maybe 18 or 24 months ago were more resistant and had their feet on the ground are tired today," Kaskel said. "Their resources are running very thin, and they are realizing that all they were doing was buying time. So I'm seeing a lot more cooperation from borrowers now."

Developers who have been stuck with unsold residential units and other properties for more than a year are seeing their debt

continue to grow as interest and fees add up, and realize they are not dealing well with a short-term crisis, he said.

"They were talking about six or eight more months of problems. Now, they have run out of resources to put out good defenses," he added.

Gary Dunkel, a Greenberg Traurig attorney representing BH AABE DATG LLC, the lender on the Downtown at the Gardens, said he also has seen a shift in borrowers' perspective resulting in more friendly foreclosures in recent months, he said.

"Certain borrowers had hoped things were not going to turn as bad, but some borrowers aren't as optimistic anymore."

JUST HOW FRIENDLY?

Although it's called a friendly foreclosure, the process isn't always that amicable, since borrowers and lenders face big losses. The procedure is basically a settlement that can save both parties from mounting legal fees.

Attorney Thomas Lehman of Tew Cardenas, who is negotiating several friendly foreclosures, said they can be defined as ones in which borrowers don't wage a court fight to stop the lender from obtaining a judgment against the borrower. But the "real friendly foreclosure" releases the borrowers from personal guarantees, he said.

Most development loans are secured by collateral and personal guarantees beyond the property in foreclosure. After the foreclosure, if the appraised value is less than the loan balance, the lender can pursue those guarantees or guarantors for the difference.

"I think the way the market is now, most people are agreeing to go ahead and not fight the foreclosure judgment, but that is just the first step," Lehman said. "Then, the question is if the second step is going to be friendly."

In many cases during the foreclosure negotiation, the borrower is asked to pay the lender a certain amount of money as

part of the agreement to be released from a future deficiency judgment.

In both Related's CityPlace South Tower foreclosure and the Downtown at the Gardens case, the owners said after the friendly foreclosure agreement the debt will be satisfied in full.

BETWEEN FRIENDS:

A sampling of recent, prominent friendly foreclosures in South Florida

- CityPlace South Tower by Related: \$134.7 million construction loan on 420 units. With the sale of 39 units (381 remain unsold), the builder generated about \$25 million, but the debt was \$119.1 million, including mounting interest, when a foreclosure suit was filed this month.
- Downtown at the Gardens: Original loan was \$140 million. Lender BH AABE, which bought the mortgage note from TIAA-CREF, claimed it was owed about \$138 million when it filed a foreclosure suit this month. The mall owners have transferred ownership interest to the lender.
- Renzi Development's West Palm Beach and Miami Beach sites: Broadway Bank was owed \$18.2 million for a Miami Beach parcel at Collins Avenue and 67th Street, and took a deed in lieu of foreclosure last year for \$15 million. The lender also took a deed in lieu of foreclosure for \$10 million on a parcel in downtown West Palm Beach to cover a \$15 million loan.
- EB Developers projects: EB negotiated several friendly foreclosure deals with its creditors, including one involving a \$29 million loan with AmTrust Bank, which took over 42 acres in Palm Beach Gardens. EB also was able to get Lehman Brothers, which financed a number of its projects in Florida, to release a portion of the personal guarantees through friendly foreclosures, according to former counsel Dan Kaskel.
- Boca Developers: Gave back the Oaks I at Biscayne Landing, The Marina Grande at Riviera Beach and the Peninsula II in Aventura to mezzanine lender Cerberus Capital Management after it defaulted on a \$200 million-plus loan. Cerberus recently gave back Oaks I to the senior lender iStar.

The safest and simplest way to avoid a deficiency judgment is through a deed in lieu of foreclosure, in which the owner transfers title of the property to the lender without a foreclosure lawsuit having to be filed.

But in most cases, lenders want to play it safe and foreclose to eliminate any rights that other creditors may have. In other cases, the documentary stamps fees on the transfer (considered a sale even if it's a deed in lieu of foreclosure) are much costlier than a foreclosure legal process, depending on the magnitude of the project.

Attorney Shari Olefson, of the Fort Lauderdale law firm Fowler White Boggs, is representing the lender on a "huge" resort project in Central Florida in which the documentary stamps would be in the \$1 million range if the developer were to agree

to a deed in lieu of foreclosure. Olefson declined to name the project and the parties involved, but said the developer recently became open to a friendly foreclosure.

"The biggest issue with most developers is getting them emotionally OK with it," she said. "Everyone seems to think they need a little bit more time [to sell, refinance or bring an investor into the project] ... but we won't even start talking about settlement unless I know the borrower has accepted the fact that he is going to allow us to take title to the property," she said.

Olefson represented Renzi Development last year when it gave up the deeds on two projects in lieu of foreclosure. On one property, Renzi owed about \$15 million to Broadway Bank for a mortgage on a West Palm Beach development site. Renzi transferred the property in a deed in lieu of foreclosure to the lender for \$10 million, according to county records.

"They saved so much money by doing that," she said. "They had a matured loan in default, and they did the right thing. And if they wanted to go back to that bank in the future, they would have a good relationship with it. They were really one of the first to go for [friendly foreclosures] when many were resisting it."

The 'DELUSIONAL phase'

Cherish Thompson, the attorney who filed the foreclosure lawsuit against CityPlace South Tower on behalf of a lending syndicate, said while 10 percent of her cases are friendly foreclosures, she thinks there still is a long way to go for some developers to let go of their projects.

"A lot of developers are still in the delusional phase," she said. "Every time I go to a settlement, I tell them, 'You have no defense here. You don't have the ability to pay.'"

But Olefson, who represents lenders and developers, says developers and owners slowly are realizing that a settlement would be the best option, she said.

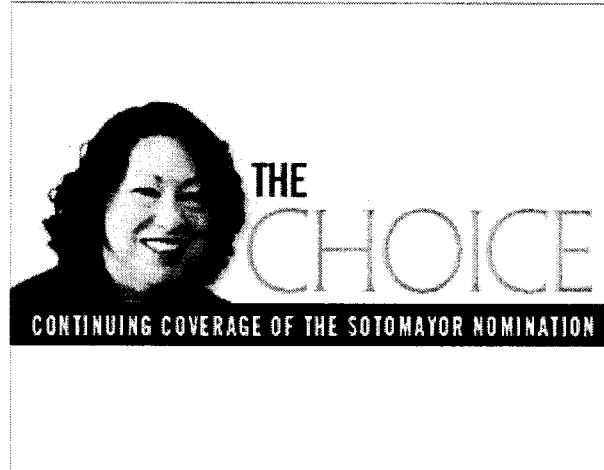
"When I'm on the flip side representing developers, I tell them the same thing," she said. "At the end of the day, the enemy is not the lender or the developer. The enemy is the economy. We are all at war, and when you have to fight a war on five different fronts, a friendly foreclosure is the best option for both."

In most cases, the biggest obstacle to friendly foreclosures are disagreements between partners and investors in the project.

"A lot of these deals have so many parties involved, and they are always fighting each other," she said.

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