



Apartment Finance Today – July/August 2005

Mortgage Lending: Insurance Companies

Life companies start targeting TICs

A few insurers are exploiting the greater flexibility they have compared to conduits in order to “customize” deals for fractionalized ownerships.

By: Brad Berton

If you're investing in tenant-in-common ownership structures (TICs), financing can be hard to find. But change is coming.

Now at least three life companies are responding to a promising – and growing – apartment lending niche where they're not yet facing much competition from Fannie Mae and Freddie Mac: TICs. Like regular Sec. 1031 exchanges, TICs allow the deferment of capital gains. Many investors use this vehicle to sell real estate and exchange equity for interests in larger, professionally managed properties.

The government-sponsored enterprises (GSEs) are still quite reluctant to lend against properties owned by TIC-related borrowing entities, according to experts. While that will almost certainly change in coming years, the reluctance reflects continued discomfort with ownerships comprised of fractionalized interests split among handfuls or even dozens of individuals, noted Eric Tupler, an active TIC mortgage banker who manages L.J. Melody & Co.'s Denver office.

TIC loans becoming more common

“It hasn't happened yet, but I think lending to TICs will become mainstream at some point” as evolving borrowing structures satisfy lender concerns, Tupler said.

Meanwhile conduit lenders are accommodating the growing number of TIC borrowers with standardized loans, which are sold efficiently to investors through commercial mortgage-backed securities.

Insurers such as MetLife, John Hancock Life and Allianz Life are also responding by targeting a bigger share of the TIC lending business. According to dealmakers, the life companies as portfolio lenders tend to compete by exploiting flexibility that conduits can't replicate.

While they can't really offer significantly more attractive rates and terms than conduits for TIC acquisition financing, life companies generally have more flexibility to “customize” transactions, noted Frank Satterfield, founder of Harbor Capital Group in Houston. “The

bottom line is they're better able to offer an 'out-of-the-pocket' structure," he continued, adding that insurers tend to focus on larger, higher-quality assets regardless of ownership category.

Loans before stabilization

One area where such flexibility can be especially meaningful to sponsors that organize TIC investments is in financing purchases of new communities before they're stabilized. Life companies in many cases are more willing than conduits to fund an acquisition based on projected revenues rather than current collections, Satterfield and Tupler agreed.

In a recent transaction that Satterfield helped arrange, MetLife provided \$29.2 million to a TIC that was formed by sponsor International Realty, Inc., to acquire the 340-unit Heights at Peachtree Creek in Atlanta. MetLife offered a short-term floating-rate first mortgage equating to 65% of the purchase price, and also issued a forward commitment to take out that loan with a fixed mortgage at a 75% loan-to-value ratio upon stabilization.

MetLife has also provided first-priority and short-term mezzanine financing, or worked with third-party mezz lenders to provide it, for TIC-related borrowers in such situations, said Satterfield. That has included single properties and even portfolios of communities acquired before stabilization, continued Satterfield, whose company has arranged some \$600 million in TIC finance transactions (with life companies funding about a third of them, and conduit lenders most of the balance).

Life company flexibility can also help sponsors close on stabilized communities amid heavy bidding before a final TIC team is in place. MetLife funded a Creekstone Cos. affiliate's acquisition of an infill community near downtown Austin with a short-term floating-rate first at 75% of the purchase price, with RAIT Investment Trust providing a temporary mezz slice equating to another 15% of capitalization.

That helped Creekstone retain the option of converting the stabilized property into condominiums if that proved to be the best strategy, or alternatively flipping ownership to a Creekstone-sponsored TIC with MetLife taking out both short-term facilities with a fixed-rate permanent mortgage.

Tighter spreads on short loans

On five-year deals, life companies can even occasionally offer tighter rate spreads than conduits, which are hard to beat on seven- or 10-year transactions, said Amos Smith, senior vice president with Johnson Capital in Irvine, Calif. That can be a meaningful factor for TICs that don't want to be locked into longer terms, he added.

They also tend to be more flexible and personal than conduit programs with respect to ongoing loan-servicing matters, such as when a TIC-related borrower wants to amend loan documents or terms, said Larry Stephenson, senior managing director with NorthMarq Capital in Bloomington, Minn.

Life companies also appear to be getting more and more creative with the interest-rate structures they'll offer TIC borrowers, including convertible floating-to-fixed and fixed-to-

floating options, added Melody's Tupler. And while prepayment provisions are in flux at conduits because of competitive pressures (and aren't especially meaningful to TICs in any case), insurers have greater flexibility to accommodate borrower wishes, he added.

Life insurers also have more flexibility to waive capital-reserve requirements or tax and insurance escrowing provisions, added Satterfield. But he also noted that those aren't particularly significant issues for TIC sponsors, which tend to encourage generous reserves and escrows to minimize capital calls.

MetLife has edge

Satterfield said that MetLife has taken the lead to some degree as life companies dip into the TIC lending pool. Having deliberately sought to understand TIC business models and financial needs, MetLife loan-review committee members are now able to assess a transaction quickly when a finance opportunity arises, he added.

Meanwhile, John Hancock has also actively been funding TIC multifamily acquisitions, as has Allianz. Allianz just financed portions of Creekstone affiliate acquisitions exceeding \$60 million: the 284-unit Reserve at Walnut Creek in Austin, Texas, and the 356-unit Alexan Castle Pines in Castle Rock, Colo.

But as additional insurers and the GSEs get more comfortable lending to fractionalized ownerships, the rates and terms they'll offer are expected to emphasize the sponsorship's stake and experience perhaps even more than the number and/or sophistication of the TIC investors, experts surmise.

"The sponsor's reputation and experience go a long way toward determining a life company's interest in financing an acquisition," Stephenson said. If a credible, well-capitalized sponsor has a 10% stake in a TIC-owned property, that deal might even attract Fannie or Freddie today, Smith thinks.