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Kevin Jursinski: Commercial real estate foreclosures next big crisis — here are suggested solutions

Kevin Jursinski - Guest Opinion

Like a punch drunk fighter with a big heart grappling to get up off the canvas after a one-two punch of devastating residential foreclosures and skyrocketing unemployment rates, our economy is staggering to its feet.

Unfortunately, we may be facing a knockout punch due to a potential crisis in commercial real estate. Proactive ways exist to avert the next blow, but it will take intelligence and bold planning.

Here are some causes for concern:

1. Commercial vacancy rates have risen sharply in the last several years, reflective of the downturn in the economy.
2. As vacancies increase, values of commercial properties drop.
3. As vacancies increase, commercial property owners struggle to service mortgage debt, creating default scenarios.
4. When defaults occur in commercial loans, foreclosures result and values drop further.
5. Between 2009 and 2011, over $814 Billion in commercial real estate loans will mature nationally.
6. Because of the tight credit market a significant number of commercial loans that originated between 2004 and 2008 will be precluded from refinance opportunities.
7. Even solvent borrowers are being denied extensions of their loans due to current low appraisals on commercial property.
8. Deutsche Bank issued a report indicating that 80 percent of the commercial loans made in 2007, financed by mortgage-backed securities, are due to mature but will not qualify for long term financing. If they are not extended, they will go into default.

This is a crisis that will be upon us very soon. Our banking institutions and our government cannot react as inefficiently as they have in addressing residential foreclosures.

Here are my suggestions:

• Tax Subsidies For Private Investors vs. Bank Bailouts. Encourage the purchase of commercial mortgage paper and properties by offering tax subsidies.
Private investors who take over troubled properties or nonperforming loans will want a discount for the risk they assume. This causes write-downs by lenders who will seek additional governmental bailouts or face FDIC takeover. A better solution is to provide tax subsidies for these investors to increase return on investment, enhance the asset value and reduce loan loss.

• Smart Business Model Using Government Guarantees. Rather than bailout lenders from toxic commercial loans the government should conduct itself as a sound business manager for its shareholders — the U.S. taxpayers —by:

A. Identifying non-toxic commercial assets.
They should provide a federal guarantee only for a portion of the loan based upon an economic analysis of anticipated revenues. This calculated guarantee would encourage lending by banks to refinance or modify performing but struggling loans.

B. Identifying toxic debts held by lenders.
Let the market dictate the disposal of these toxic debts by offering tax subsidies to investors to encourage the purchase and enhance the value of the troubled asset and reduce the loan loss.

C. Using government guarantees.
This incentivizes banks to modify existing loans, but provides for a recapture value so taxpayers share in profits when the loan performs.

• 21st Century Mediation Model. More efficient ways exist to address commercial loan defaults than the antiquated foreclosure process currently in use. Lending institutions need to embrace proactive mediation, proven to effectively resolve issues in litigation cases with a success rate of over 80 percent.

Lenders need to staff loss mitigation departments with solution minded individuals tasked to structure creative loan workouts that include government guarantees and tax subsidies. Foreclosure should be a last resort.

The next real estate crisis will soon be upon us. We need leaders who can assess the risk and implement a sound business approach to resolve the problem while exercising their fiduciary duties as stewards of the taxpayer’s money.
