

# **CRE Loan Workouts – Best Practices**

**PRESENTED BY:**

**WILLIAM “TED” ANGLYN, MAI, CCIM**



# For Information Purposes Only

While a great deal of care has been taken to provide accurate and current information, neither The Appraisal Institute nor Ted Anglyn assume responsibility for the accuracy of the data contained herein.

Further, the general principles and conclusions presented in this text are subject to local, state, and federal laws and regulations, court cases, and any revisions of the same.

This publication is offered for educational purposes with the understanding that The Appraisal Institute and Ted Anglyn are not engaged in rendering legal, accounting, or any other professional service.



# Acknowledgements

William “Ted” Anglyn, MAI, CCIM

Anglyn Property Advisors, LLC

PO Box 71144

Marietta, GA 30007

[Tanglyn@anglynproperty.com](mailto:Tanglyn@anglynproperty.com)



# Supplemental Information

- <http://www.fdic.gov/news/news/press/2009/pro9194.html>
- [www.fasb.org](http://www.fasb.org)
- Accounting Standards Codification (ASC)
- Accounting Standards Updates
- [www.mossadams.com](http://www.mossadams.com)



# Policy Statement

## **Prudent Commercial Real Estate Loan Workouts**

1. Effective October 30, 2009.
2. 33 Page Document.
3. 17 Scenarios of Attachment 1.
4. Replaces November 7, 1991 “Interagency Policy Statement on the Review and Classification of Commercial Real Estate Loans”, as well as two other subsequent guidelines.

# Authoritative Accounting Guidance Review (Page 30)

1. FASB ASC 310-10-35-2 through 30 – **former** reference FASB 114, Accounting by Creditors for Impairment of a Loan.
2. FASB ASC 820, Fair Value Measurements and Disclosures – **former** reference FASB 157, Fair Value Measurements.

NOTE: THREE ACCOUNTING STANDARDS  
UPDATES HAVE BEEN ISSUED ON FAIR  
VALUE MEASUREMENT IN PAST 12 MONTHS



# Key Terms/Concepts

- Five Loan Classifications
- KEY STARTING POINT
- Trouble Debt Restructure
- ALLL – Allowance for loan and lease losses
- Fair Value Measurement
- A/B Note Structure
- Unobservable Events



# LOAN CLASSIFICATIONS

- 1. Pass
  - 2. Special Mention
  - 3. Substandard
  - 4. Doubtful
  - 5. Loss
- 
- NOTE: DEPICTED ON ATTACHMENT 4 – Page 33 of Policy Statement.



## KEY STARTING POINT

- ARE YOU BETTER OFF WORKING OUT THE LOAN OR FORECLOSING – Is Liquidation Value less than Market Value?
- Regulators recognize: Prudent loan workout agreements are generally in the best interest of both the Institution and the Borrower.



# Troubled Debt Restructure (TDR)

- If Market Value is less than loan balance, prepare Fair Value for loss determination.

## Key Points:

1. Fair Value and Liquidation Value are needed to do the ALLL and loan classification.
2. Fair Value determines the substandard and doubtful, while market value and liquidation determine the loss amount.



# FAIR VALUE MEASUREMENT

## NORMAL MARKET CONDITIONS

- DOES FAIR VALUE EQUAL MARKET VALUE?
- GAAP indicates Fair Value should be same as Market Value under normal market conditions. But, what about sales/disposition costs?



# FAIR VALUE MEASUREMENT

Prepared to structure an “A/B” Note loan. The “A” note would be based on the as is market value. The “B” note would be the hopeful portion and represent the difference between the loan balance and the “A” note.

- FAIR VALUE would establish (potentially) the amount to be classified as substandard versus a total loss within the A/B Note structure.



# FAIR VALUE MEASUREMENT

## NON-FUNCTIONAL (DYSFUNCTIONAL) MARKET CONDITIONS

- FAIR VALUE IS MORE FLEXIBLE THAN MARKET VALUE
  1. Fair Value does not punish for “Unobservable Events” – an example of an unobservable event in a non-functional market would be developer’s profit.
  2. The discount rate would not be market based but rather the Institution’s cost of capital.



# CONCLUDING COMMENTS

1. New Commercial Real Estate Loan Workout procedures are generally advantageous.
2. Appraisers are needed to provide guidance on as is market value and should familiarize themselves with Fair Value.
3. Substantial confusion prevails relative to Fair Value measurements.
4. Limited clarity is provided on establishment of “unobservable” and the use of the associated discount rate for Fair Value.