

What Will Those Financiers Think of Next?

Desperate times may require desperate measures, but they also engender new and imaginative products and methods. With conventional financing woefully unavailable for real estate development, two new "out of the box" financing tools are creeping into discussions across the country. We offer this discussion not as an endorsement or evaluation of these products, but rather to take note of two interesting blips on the radar screen.

A company known as Freehold Capital Partners has applied for a business-method patent for a system of Reconveyance Fee Instruments they have developed. The instruments are obligations or covenants recorded against a property which require the payment of a reconveyance fee to the originator any time the property is sold. As advertised, the Reconveyance Fee Instrument calls for the payment of 1% of the gross sales price each time a piece of real estate is conveyed. This mechanism is akin to Wisconsin's transfer fee, except that it is paid to the originator of the instrument, rather than the state. Under the system licensed by Freehold, the obligation exists for a period of 99 years and affects transactions well beyond the initial sale from the licensee to their buyer.

This mechanism is described as a means by which the initial cost of development can be transferred to future purchasers and owners of a property. Instead of the first buyer of a development property paying all of their development costs in the form of the purchase price, some of the project costs can be carried through the developer's anticipated future stream of income from reconveyance fees. Thus, a developer could lower the sale price of a property as the reconveyance fees may compensate for this discount.

The Reconveyance Fee Instruments may also be used as a funding source for the developer. The contract right to this future stream of income could be monetized by selling the right to collect fees paid under the instruments. Third parties would presumably pay a discounted lump sum in exchange for an indefinite future stream of payments. Freehold anticipates serving as an aggregator of the Reconveyance Fee Instruments. They note that when a sufficient quantity of instruments are aggregated into a single pool, realistic income projections can be made, making the purchase of these rights more feasible.

Another unique product hitting the streets is financing through life settlements. Firms offering life settlements pay persons insured under life insurance policies

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for the right to collect as beneficiary under the policy. The insured "cashes out" their interest in their life insurance policy in return for an immediate cash payment. The life settlement firm then stands as the beneficiary under the policy and collects the policy benefit upon the death of the insured.

This funding mechanism has now been coupled to distressed real estate. Life settlement aggregators use their fund pool to acquire distressed real estate. In a life settlement transaction, the seller of the property (presumably banks and other lenders from REO portfolios or developers with distressed inventory) conveys the distressed real estate at an agreed purchase price to the life settlement aggregator. Then, the seller immediately reinvests its sale proceeds in the life settlement fund. The life settlement fund pays a coupon rate back to the investor, funded through the proceeds of the aggregated life insurance policies. The seller has essentially divested a troubled asset and replaced it with a product delivering a prescribed return.

Practically speaking, the future proceeds of life insurance policies are securitized and used as a substitute for distressed real estate assets. Few readers can avoid raising an eyebrow in response to this plan and the use of this mechanism by financial institutions is currently subject to review by various regulators.

These products are presented in the context of trend spotting and making you aware of new and unusual products in the world of finance. These products and similar mechanisms should not be considered without thoughtful review by you and your counsel. (Remember that Freehold Capital Partners asserts intellectual property protections over the reconveyance fee scheme.)

[Reinhart's Real Estate team](#) stands ready to assist you with any question concerning real estate finance and the imaginative products appearing on the market.

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