

2024 Financial Management Conference

Workouts - Lender/Investor, We Have a Problem: How to Engage Key Stakeholders

John Fowler

Michael Pitchford

Dana Moore, Principal, Compass

Moderator: Mark Deitcher, Chief Financial Officer, Mission First Housing Group

Sept. 05, 2024

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Continuing Professional Education (CPEs) Requirements for CPAs

- Please find the **SESSION HOST** to **SIGN IN** at the beginning and **SIGN OUT** at the end of every session using the **QR code**. We use that attendance log to verify your participation for CPE credits.
- Please **submit all conference evaluations**. Evaluation links are emailed to registrants daily. Please see the session host (the person monitoring the sign-in process) if you prefer a paper evaluation.
- For more information on CPE credits, contact Lindsay Wells at consult.lwells@gmail.com.

Polling Question #1

Are you currently engaged in or thinking about beginning a workout with your lender and/or investor:

- Yes or No (show of hands)

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Workouts: How to Engage Internal Stakeholders

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What is the Role of the CFO?

1. Almost all problems manifest themselves through CashFlow
2. See your role as critical to identify and working through agency change
3. Find your voice and speak up when you see a problem

How do we know if have a problem ?

- It's the cashflow stupid...or lack of !!
- What are the warning signs – there are a lot !
- Why don't agencies act sooner to turn things around ?

How do I get the organization to understand and address the needed change?

- Talk candidly with the Executive Director
- Make sure Board reports reflect clearly the problem
- Insist on discussing this at the Board level and not get lost in Board Agenda
- Work collaboratively toward solutions and next steps
- Ensure Board approves your efforts and steps and their informed and ready to approval transactions as needed
- Talk candidly with the staff

When do I need an outside consultant ?

- Talk candidly with the Executive Director Is the problem beyond anyone's in-house expertise and experience ?
- Do you need an outside consultant to confirm there is a problem and what it truly is ?
- Does the Board or Stakeholders require outside expertise and credibility to work with you and to solve things quickly ?

Case study

- Retiring long-term Executive Director
- Lack of Board Reporting, Board turnover
- Had all the warning signs, didn't want to believe it was that bad
- Finally reached out for help

Recap

1. Organizational Challenges all manifest themselves in CashFlow but its much more complicated arriving at the source(s) of the problem
2. Understand your role as the CFO in identifying, and managing a turnaround/workout
3. Know the warning signs
4. When an agency is experiencing trouble its never one thing and doesn't go away by waiting it out.
5. Make a plan ,with specific steps and timeframes, track and adjust as necessary.
6. Consider hiring a professional to assess the problem(s), prioritize the approach, assess staff's abilities, and interface with financial partners.
7. Great communications at all levels is critical in getting the organization to come together all working toward the same goals.

Polling Question #2

If you are engaged in a workout have you retained consulting support?

- *Yes or No (show of hands)*

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Workouts – You and Your Lender

Michael Pitchford

Sept. 05, 2024

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“you and your lender”

- Bank risk ratings
- Bank workout conversations
- Some inside hints on workouts

Polling Question #3

Have you ever asked your lender what your loan is risk rated?

- *Yes or No (show of hands)*

Bank risk ratings

- Banks risk rate their loans
- Some banks use different number scales but it is essentially like this:

Bank risk ratings

- Banks risk rate their loans
- Some banks use different number scales but it is essentially like this:

Risk Rated 1 – 5:

- Well secured or guaranteed
- Virtually no credit risk/Maybe a government borrower
- Maybe full cash security
- Overly capitalized and very low LTV

Risk Rated 6 or “pass”:

- Well secured, very low risk of any loss
- Strong well-margined collateral
- Excellent financial history and market trends
- Strong management
- Stable/strong industry

Risk Rated 7 “Other Assets Especially Mentioned, OAEM”:

- Maybe ok security margin/LTV
- Maybe ok debt service capacity
- Maybe good management
- Maybe steady financial trends
- Moderate capital level
- Something is not quite right, however

Risk Rated 8:

- Deteriorating collateral value, market, something
- Maybe covenant breaches
- Potential debt service shortfalls
- Significant adverse developments
- Modest chance of a credit loss

Risk rated 9 “doubtful”

- Need for immediate action indicated
- Security shortfall/capital crisis
- Cessation of operations
- Adverse management change
- Delinquent on interest and principle
- Multiple monetary and non-monetary covenant defaults

Risk Rated 10 “loss”

- Receivership or bankruptcy
- Definite loss evident
- Disappearing assets/security
- Fraud

Talking to your lender

- Honest sharing of the situation
- Sharing a workout plan
- Making a specific forbearance request

Things to know about your lender

- Their profitability model, capital charge
- Loan loss reserves, ramp up with risk ratings
- They can often make more money fixing a loan than making a new one!
- Is it you or everybody? It makes a difference...

Polling Question #4

Which factor would create the worst Lender risk ratings?

- *Security shortfall*
- *Covenant breach for failure to provide audit*
- *Uncertainty around repayment*
- *Bankruptcy or Receivership*

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Workouts: A Case Study

Dana Moore, Compass Advisors

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Tools at your disposal

I/O (interest only) vs. P&I (principal and interest)

- Temporary cash flow relief needed

Interest rate reduction

- Temporary cash flow relief needed

Covenant modifications

- Temporary or permanent relief needed

Performance hurdles

- Temporary relief needed - project performance will be caught up in time

Cash flow sweeps

- A tool to get improve Lender's position, give control, and potentially hyperamortize loan, resulting in improved LTV

Tools continued

Forbearance - time

Standstills and negotiation letters

Troubled Debt Restructures – over leverage with some upside

Deeds in Lieu

Sale of collateral

Foreclosure

Bankruptcy

Case Study #1

Situation

- Borrower with single asset nonrecourse agency loan
- Workout Goals: temporary relief
- Other Goals:
 - Limit cash outlays from sponsor
 - Maintain ownership of property

Resolution

- Steps taken
 - Prenegotiation Letter
 - Forbearance
- Plan elements – milestones and performance hurdles/time and contract relief
- Resolution/Tools used – Forbearance, interest added to note balance

Case Study #2

Situation

- Borrower with single asset nonrecourse agency loan
- Workout Goals: revised debt structure/TDR (A/B note structure with cash flow sweep)
- Other Goals:
 - Limit cash outlays from sponsor
 - Maintain ownership of property

Resolution

- Steps taken
 - Prenegotiation Letter
 - Restructure presented and denied
 - BK
- Plan elements – revised terms proposed which were rejected
- Resolution/Tools – Bankruptcy/court cramdown/improved deal terms

Case Study #3

Situation

- Borrower with large land positions, limited liquidity and limited cash flow impacted by declining market values. Significantly overleveraged.
- Workout Goals: deleverage organization, preserve cash, avoiding bankruptcy
- Other Goals:
 - preserve housing/affordability restrictions
 - preserve jobs

Resolution

- Steps taken
 - All debt service payments stopped
 - BK analysis presented with full financial disclosure
 - Multiple lenders – commercial banks, local banks, CDFIs, state and federal
- Plan elements – equal treatment like creditors (13)
- Resolution/Tools used - Deed in lieu, Charge-offs, Discounted note sales, restructures with changed business terms
- Avoided bankruptcy

Case Study #4

Situation

- Borrower with \$30MM debt overhang corporate
- Workout Goals: deleverage organization and avoid bankruptcy
- Other Goals:
 - Preserve housing
 - Preserve jobs

Resolution

- Steps taken
 - Identify “knight” to save organization
 - Cleanse organization through merger
- Plan elements – all creditors treated equally, bk analysis developed, \$0.10/\$1.00 recovery for unsecured creditors
- Resolution/Tools – Merger, debt write-offs, asset sales, modifications

Case Study #5

Situation

- Borrower with nonperforming portfolio of real estate assets (15 assets)
- Workout Goals: deleverage
- Other Goals:
 - Limit cash outlays from sponsor

Resolution

- Steps taken
 - Education
 - Restructure not an option
 - Permission to sell
- Plan elements – appraisal/bov/gtys
- Resolution/Tools – Sales/5Q “free ride” plan

Concluding Thoughts

- Success driven by achieving win-win where possible
- Have clear and realistic goals, with an understanding and acceptance of implications of workout

Evaluation Reminder

- Please submit all conference evaluations. Use the electronic evaluation link in your email.
- Contact consult.lwells@gmail.com if you do not receive the link.

CONTACT INFORMATION

Mark Deitcher

mdeitcher@missionfirsthousing.org

Dana Moore

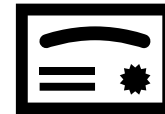
mdanamore@gmail.com

Michael Pitchford

John.michael.pitchford@gmail.com

John Fowler

johnslocpa@sbcglobal.net



Lindsay Wells

(CPE credit contact)

consult.lwells@gmail.com

