



## TIC Industry Slows, Focuses On Quality

By Jessica Lillian

Although still considered a growing, active and important market on its own, the tenant-in-common (TIC) industry is currently facing the same hurdles placed in front of most participants these days in the larger world of 1031 exchanges and in commercial real estate investment as a whole.

"It's all real estate, and the credit crunch or lack of liquidity has tremendously inhibited sellers of properties from being able to transact, as well as purchasers of properties from being able to transact," explains Duke Runnels, president and CEO of FORT Properties, a real estate investment company and sponsor of TIC offerings. "It's put a damper on things, and that's an understatement."

Commercial mortgage deal volume, of course, heavily factors into the production of accurate valuations, acquisitions of properties to make available to investors, and successful TIC transactions. "It's hard to ascertain what the true value of real estate is today when it's hard to obtain financing on that real estate," he points out.

Furthermore, because a great deal of TIC investment is made by retirement income-minded seniors and others unlikely to seek value-add opportunities or other speculative prospects, the industry was already characterized by more of an emphasis on property quality, stability and certainty than in many other areas of commercial real estate investment.

The threat of property-level events such as lease renewals and tenant improvements, for example, may trigger caution flags, whereas long-term credit leases that allow minimal market exposure are particularly attractive to these investors.

Among the major asset types, stabilized office properties, as well as industrial and warehouse properties, are popular among TIC investors at the moment, according to Runnels, while retail and hospitality have all but entirely fallen out of favor. Although his firm does not currently deal with multifamily, he observes a "fair amount" of TIC activity in the sector.

Overall, he says, the TIC industry remains active in "solid markets where job growth is still evident and the properties are solid and conservatively underwritten with stable cashflow in place." Although tertiary markets are largely considered too risky, both primary and secondary markets present viable TIC opportunities.

The secondary TIC market itself, meanwhile, has yet to reach a significant size. "There has not been a tremendous need to develop that market, as investors tend to not want to exit the program," notes Runnels.

In addition, a general lack of standardization in the TIC industry means that individual sponsors' offerings tend to contain differing components - further inhibiting the development of a cohesive secondary market.

With many life companies and other portfolio lenders now stepping up their activities in providing property financing as borrowers await the return of conduit lenders, another notable TIC trend of late has been a growing interest in Delaware Statutory Trusts (DSTs).

"A lender -specifically a life company lender -does not view favorably having TICs on title," Runnels explains. "Doing a DST is a specific way of investing that avoids that [problem] and still qualifies for the 1031."

Also on the TIC regulatory side, guidelines regarding whether products involved in TIC transactions are considered securities or real estate are now under development from the National Association of Securities Dealers and U.S. Securities and Exchange Commission. Runnels says these groundbreaking new rules would essentially require the products to be sold as securities but would still allow participation from the real estate community through referral fees or another means.

Finally - and possibly most importantly - as during any particular market era, adjusting appropriately to market conditions is key for effective TIC participation, stresses Runnels.

"If you're involved in the tenant-in-common industry - or any place in real estate - your mission is to acknowledge what the landscape is and play within the guidelines of that landscape," he states.

Right now, those guidelines reflect the same principles and refrains as in the rest of commercial real estate, including flight to quality, stringent underwriting, raised debt coverage ratios and insistence upon in-place cashflow measurements rather than projections.

In particular, "There are a lot of properties acquired in the last couple of years that were acquired off of projections rather than income in place," Runnels remarks.

Despite all the new challenges, for commercial mortgage brokers and bankers specifically, he believes today's TIC climate offers "probably a greater opportunity than ever before" for providing counseling and advising services, as well as fostering the types of close relationships that are increasingly important for all parties' success.