When Restructuring Financially Distressed CCRCs, Go With Creativity—Not Bankruptcy

Posted By eecker On July 24, 2012 @ 5:07 pm In Senior Housing | No Comments

Multiple headlines in the not-too-distant past have trumpeted the struggles of some non-profit continuing care retirement communities (CCRCs) that are attributable—at least in part—to their financing structures, and there are bound to be more coming down the pike, those in the market say.

But while bankruptcy has traditionally been the main option for these distressed communities, as evidenced by the epic default and eventual bankruptcy sale [1] of Chicago's Clare at Water Tower, the traditional workout needs to make way for more outside-the-box solutions.

That, or stay away from bankruptcy in the first place, said David Reis, CEO of Senior Care Development LLC, during a Distressed Healthcare Assets webcast hosted in July by law firm McDermott Will & Emery LLP.

"We're trying to solve issues before bankruptcy to keep the value there longer," says Reis, whose Chicago Senior Care company purchased the Clare out of bankruptcy in 2011. "I have a feeling with the amount of activity in the next year or two, people will get more creative and not just reach for the bankruptcy tag. They'll go to the marketplace and try to solve the problems to keep the community."

Bankruptcy typically leads to a purchase at 70% to 80% of the community's value, whereas distressed properties that don't go into bankruptcy should still be able to get about 90% of the fair market value, Reis says.

But preventing bankruptcy can be less clear-cut than a simple solution. Depending on how long the community has been in business, the timing of the distress can cause hurdles that are difficult to overcome.

"CCRC projects are difficult to restructure," says Nathan Coco, partner with McDermott Will & Emery. "This is particularly true where a project becomes distressed during the fill-up phase. Entrance fees are the lifeblood, so if units are selling, it likely doesn't need a workout. If they're not selling, a workout may not make a bit of difference. Covenant relief might buy time… but bankruptcy may be the only hope."

Bankruptcy, however, should be avoided at all costs, he says. It is expensive and can be extremely difficult to find lenders to work with in a property that is distressed.

Additionally, the residents must be considered, as well as the headline risk that a bankruptcy presents.

“In almost all cases, the residents’ contracts are assumed and assigned to a buyer,” Coco says. “This can lead to displaced resident and headline risk. One thing we are likely to see is more creativity in terms of how resident contracts are handled.”

What that creativity may entail is still an unknown, but greater flexibility on the part of banks might be one change to look for. A line of credit option, for example, may be more likely to happen today than in recent memory.

“Over time, we’re seeing banks being willing at least to consider that, or make modest adjustments to debt,” says David Fields, director of RBC Capital Markets. “There’s a lot of pressure for banks to look for resolution now with some seeing more willingness to compromise.”

Written by Elizabeth Ecker [2]

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[1] epic default and eventual bankruptcy sale: **http://seniorhousingnews.com/2012/04/13/chicago-senior-care-acquires-the-clare-at-bankruptcy-auction-for-53-million/**
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Chicago Senior Care Acquires the Clare for $53 Million at Bankruptcy Auction

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Chicago Senior Care, LLC, a partnership between Senior Care Development, LLC, Fundamental Advisors LP, and Life Care Companies LLC, placed the winning bid on the bankrupt Clare at Water Tower, a luxury senior high rise located in Chicago's Gold Coast.

The acquisition was led by stalking horse bidder Senior Care Development, out of Harrison, N.Y., which ended up paying $53.5 million in cash along with agreeing to assume liabilities that include approximately $57 million in existing resident contracts.

"By being the winning bidder, we ended up with a beautiful CCRC which is really highly unique and probably the best-located, most magnificent community in any urban setting that I know of in the country," says David Reis, CEO of Senior Care Development, who has extensive prior experience in CCRC turnaround opportunities. "The Clare is going to be the jewel in our crown."

Although the partnership venture will end up paying much more than its original bid [1] of $29.5 million plus the assumption of liabilities, Reis says that was to be expected, as the Clare's prior financial issues, including resident agreements and its ground lease with Loyola University, had to be resolved leading up to the bankruptcy auction.

As the stalking horse bidder, Senior Care Development worked with the Clare's not-for-profit sponsor the Franciscan Sisters of Chicago and Houlihan Lokey, whose Healthcare Group was hired to restructure the luxury community, and was able to solve many of its problems, which Reis says "allowed the debtor to maximize value at an auction setting."

By taking on the resident contract liability, all of the Clare's current residents are guaranteed a 100% refund on any money due to them upon leaving, Reis says, adding that through the bankruptcy and restructuring process, none of the residents have lost a dollar.

Reis says his company helped write an addendum to the resident agreement which all existing residents will sign, reaffirming their refunds and allowing the new ownership to offer a different contract to prospective residents that is "more in line with normal industry standard" after a previous agreement [2] (which delayed refunds until other unoccupied units were sold) that Reis calls "off-mark."

The new policy will refund a resident's entrance fee when that particular unit has been resold, and Reis says he's confident in the Chicago Senior Care partnership's ability to put the community on the right track.

The new owner also plans to offer a variety of refund structures. The current plan is predominantly a 90% refund structure, says Reis, but new options will include a 50% refund-of-capital plan and a 0% refund plan. "By doing so, we'll be able to push down the average entrance fee to a level that we think will be highly attractive," he says.

"The problems the Clare had are all solvable," Reis told SHN. The plan is to lower apartment prices to a "market-correct" level with price points a minimum of 20% less expensive than what they're at right now, while maintaining current standards. "It will still be luxury, 100%," he says. "That's the market we're serving, and that we expect to continue to serve."

The high-rise's issues have been financial in nature, not operational, and Reis says the goal is to attract prospects at a lower price point who are looking for a high-end style of living; he hopes a lower price point will give the Clare a competitive edge over nearby The Admiral at the Lake.

Buying the Clare at such a discounted price—its development cost sponsor Franciscan Sisters $272 million—allows Chicago Senior Care to "pass the discount on" to residents, says Reis.

At time of sale, the community's skilled nursing, assisted living, and memory care units were "doing well," according to Reis, likely because there's "not a whole lot" offering similar services in downtown Chicago. But the independent living is only about 35% occupied, and that's where the new venture is hoping to attract new business.

For now, Chicago Senior Care is focusing on transitioning ownership and management of the building, and will take possession in about 60 to 90 days, pending normal regulatory requirements.

"We look forward to working with the Franciscans as we transition from their ownership to ours; they've been nothing but professional through this whole process, and we expect smooth sailing," Reis says.

Written by Alyssa Gerace [3]

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[1] original bid: **http://seniorhousingnews.com/2012/03/14/senior-care-development-bids-over-86-million-for-bankrupt-clare-at-water-tower/**
[2] previous agreement: **http://seniorhousingnews.com/2012/03/25/on-the-record-david-reis-ceo-of-senior-care-development/**
[3] Alyssa Gerace: **mailto:agerace@seniorhousingnews.com**

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On the Record: David Reis, CEO of Senior Care Development

Posted By Alyssa Gerace On March 25, 2012 @ 8:57 am In CCRCs,On the Record,Senior Housing,Senior Living | Comments Disabled

After seeing that Senior Care Development, LLC had placed a stalking-horse bid [1] on the bankrupt Clare at Water Tower, in Chicago's Gold Coast, Senior Housing News tracked down its chief executive officer David Reis for an exclusive interview. Reis has extensive experience in senior living development, and specializes in ground-up development of large-scale continuing care retirement communities (CCRCs) and acquiring troubled ones and turning them around.

Although Reis couldn't share too much additional information about his company's dealings with the Clare and its sponsor, the Franciscan Sisters of Chicago Service Corp., due to confidentiality agreements, he did tell us his plans to change the luxury high-rise's entrance fee refund structure if his bid is accepted; what makes him so favorable toward the CCRC model of senior living; and why the current model of nonprofit financing will "go the way of the dodo bird."

Senior Housing News: What made you interested in the Clare, and if your bid is successful, will you continue to have a relationship with the Clare's sponsors [the Franciscan Sisters]?

David Reis: Since our purchase of Monarch Landing and Sedgebrook [two senior living communities originally developed by Erickson Living, which Senior Care Development purchased after Erickson's bankruptcy filing], we've done a lot more research into the Chicago marketplace, and we really feel that the Clare is highly unique. It's one of only a few high-rise CCRCs in the entire country, and it really has a spectacular location—a block away from Michigan Avenue, in what we consider a very vibrant section of downtown, that we feel has a lot of appeal for seniors.

Our bid does not contain any future relationship with the Franciscan Sisters. We are planning on bringing in [operator] Life Care Services as our management company. We've done business with them for more than 20 years, and they manage all of our facilities.

SHN: Do you feel that other urban cities can sustain a CCRC such as the Clare?

DR: One hundred percent, yes. The problem is the cost of land, and the cost of building infrastructure is really cost-prohibitive.

If you went to New York City and wanted to duplicate a high-rise CCRC there, and you costed out the land, construction, etc., you would find that the cost you would have to charge a resident is way far in excess of what their competing options are. Therefore, when you finish that analysis, you'd say, 'Wait a second, I can't afford to sell these for a price these prospects can afford to pay.'

That's why you don't see more CCRCs in cities. Between the arts, and access to great hospitals that are in the city, all the vibrant parts, what I consider the fabric of a city life—it's really great for the residents to have access to. But because of that cost analysis, I can only think of one other CCRC in a city in Washington State. I don't really know of any other city that supports a large CCRC, and in a way, that's what makes the Clare a very attractive asset to purchase.

SHN: Your company ended up buying two former Erickson Living properties in the Chicago area after Erickson's bankruptcy filing. What opportunity does your company see in the distressed market?

DR: [Senior Care Development] bought them out of bankruptcy for cash, and they're highly stable communities—debt-free. What we find is that the communities that we organize appropriately do extremely well. Really, if there are 1,900 CCRCs around the country, and less than 3% of them find themselves in any financial distress– It really is less than any other type of real estate sector, like condos. As a real estate group, a less-than 3% default rate is extremely low.

Senior Care Development specializes in either building large-scale CCRCs from the ground up, or buying distressed communities. [Sometimes] we buy them through bankruptcy court; some projects we're looking to team up with the nonprofit who owns them and keep them in place, help them reorganize their finances through or out of bankruptcy court.

We're probably tracking a couple dozen communities in various stages of covenant violations or distress of some sort. I would say that almost all of them are nonprofits.

SHN: What might nonprofit status have to do with bankruptcy filings by CCRC sponsors?

DR: If you look at the history of CCRCs in the U.S., maybe 80% of them are nonprofits. A very high percentage of the nonprofit market traditionally had a refund plan that stated that when a resident left a community, they or their estate would get back whatever percentage they had paid—typically a 90% refund plan—when their unit resold. Saying you only get repaid when your unit resells shifts risk to residents.

Most people who move into CCRCs really have no issues and have good lives and are in a community that's financially viable. People have to start looking at the finances of the sponsors, irrespective of if they're for-profit or nonprofit. Looking across the U.S., the vast majority of CCRCs that are having financial stress, are all owned by nonprofits.

Nonprofits can use nontaxable status to go raise 100% of their financing in the bond market. Traditionally, many organizations hardly put a dime of their own money into the project, and many hadn't been in the business, had no experience, and offered no skin in the game.

The model of a nonprofit getting 100% financing is going the way of the dodo bird. That's history. Because no one else in this business gets to put no cash in the game, and doesn't have to have any experience to go out there and operate. Moving forward, a lot of people who buy tax-exempt bonds, who would buy these– they're gonna find that they're not gonna want to buy these types of bonds from nonprofit, inexperienced sponsors.

SHN: How does aging in place affect senior living communities' business models?

DR: Everyone would like to have seniors moving at a younger age. That's the Holy Grail that one searches for. I can tell you in 25 years of doing this, for brand-new senior living communities that have just opened their doors, typically the average age of a resident moving in is 78. For a stable community, that age is about 81.

Interestingly enough, those numbers haven't changed in the last decade as far as I know. When you look at these move-in rates, these numbers are uncannily accurate. That said, average life expectancy of a move-in into a stable community is somewhere between seven and 10 years.

I'm a big believer in the full continuum of care, having independent living, assisted living, and skilled nursing al on one campus. I'm really a believer

that elderly people don’t want to leave their house and have to worry about moving more than once.

Say for example a couple moves into an independent living community, and then maybe one of them needs skilled nursing. I don’t think it’s right to disrupt that and have a double move. They’re better off going to a community that has all the levels of care at that community. I’ve shied away from assisted or independent living communities.

SHN: Out of the assisted living, memory care, and CCRC sectors, which do you think will see the most success, and why?

DR: I’m a fan of CCRCs because if you build a typical 250-unit independent living CCRC, your turnover, on a community that’s already aged in place and is stable– by the time it’s been open a decade or so, it’s only turning over maybe 8% of its community a year. For a stable community with 250 units, that’s only about 20 units a year that need to be sold; it’s less than two a month, and that’s very doable.

For assisted living communities, though—if you have a 90-unit assisted living community, it’s a third the size of a CCRC, but about 40% of its units are turning over each year, for about 36 units—50% more than a CCRC. That’s three units a month, for a building that’s a third the size of a CCRC.

On top of that, assisted living communities really have no barriers to entry for building. Anyone with a four-acre site can build an assisted living community, and the licensing is no big deal. It’s not like with a CCRC, which needs a certificate of need with the nursing home, and has more barriers to entry.

CCRCs won’t necessarily be the highest growth, but they will be the most stable. The barriers are so high that by definition, that keeps growth down. As a developer/investor, I like that.

I’ve never been a fan of assisted living because there are no barriers to entry, and there’s huge turnover, and that’s been born out in the statistics right now of occupancy, where most CCRCs across the country that are well-managed are running at 91, 92% occupancy or better, while assisted living is running about 86%.

The CCRC model offers the most bang for the buck. It’s a stable platform, it’s highly successful, and it will continue to be a success.

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[1] stalking-horse bid:
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