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Let the Bidding Begin

As commercial property loans come up for refinancing, industry experts predict that auction activity will grow.

By Mariwyn Evans | October 2009

As short-term commercial property loans come up for refinancing, experts predict that auction activity will grow.

As foreclosures swell and the credit crunch continues, auctions are returning to the forefront of commercial real estate. Even notable buildings such as Boston's John Hancock tower have gone the auction route, giving heightened visibility to a selling method that's been more commonly associated with residential real estate in recent years.

"Auctions will help put distressed properties back into the market faster and get things back to normal, just as they did in the Resolution Trust Corp. era that followed the savings-and-loan crisis," says David Gilmore, managing director of Sperry Van Ness Accelerated Marketing, an Atlanta-based venture that specializes in asset disposition through auctions.

Approximately \$15.5 billion in commercial real estate was auctioned in 2008 and that figure is on the rise, according to Chris Longly, deputy executive director of the National Auctioneers Association in Overland Park, Kan.

Longly and other industry experts, including Rhett Winchell, president of the auction division for Kennedy Wilson Inc. in Los Angeles, expect to see a surge in commercial auctions over the next 12 months as more commercial property loans come up for refinancing. Commercial loans are mostly short term, and without ready financing even the most experienced commercial players can get into trouble.

The Right Method for the Right Time

The growing appeal of commercial auctions has much to do with their promise of a fast turnaround time. Rather than wait months or longer for an offer to roll in, the seller can set a specific date of sale.

"That's very valuable at a time when there's no sense of urgency and buyers continue to sit on the sidelines," says Max Spann Jr., an auctioneer and commercial broker with Max Spann Real Estate in Clinton, N.J.

Most commercial auctions are held within four to 10 weeks after marketing begins. Sales often close in 30 days, though many sellers are extending that term to 45 or even 60 days to accommodate the tight financing climate, says Barbara Bonnette of Bonnette Auctions/United Country in Alexandria, La.

In markets where there are few sales—and hence, few comps—it's difficult to set a price for a listed property. "The only strategy that a conventional broker has in a down market is to reduce the price and

try to find a value," says Alan Kravets, president of national auction firm Sheldon Good & Co., based in Chicago. "A properly run auction, on the other hand, gets the property in front of buyers and lets the buyer, not the seller, set the price."

An auction also "validates the selling price," Spann says. "There's nothing like a seeing a crowd of people bid on a property to overcome your fear that you're paying too much."

Another big perk of the auction process is that the seller can dictate conditions of the sale up front, says Michael A. Fine, CCIM, executive vice president and partner with Sheldon Good. "With a conventional sale, you have to negotiate terms and price simultaneously, which can take months. With an auction, the seller controls the terms and conditions, and the bidding process determines the price based on those terms."

But that doesn't mean auctions are completely immune to the problems plaguing conventional property sales. "We're finding that some sellers can't afford an absolute auction (see "Not All Auctions Are the Same," page 18) because they owe more than the property is worth. Others set reserves too high. There's still a gap between the bid and ask," says John Seckerson, CCIM, of Colliers International in Portland.

#### Web Changes the Game

The Internet has made the auction process a lot easier today than it was during the downturn of the 1990s, especially on the marketing front, some practitioners say. "We promote our auctions on more than 700 Web sites and send a mass e-mail to our databases of prospects," says Bonnette, a 22-year auction veteran.

She also uses more traditional methods such as newspaper ads, brochure mailings, and phone calls. Because of the short marketing time, "it's a full court press. You have to market very aggressively to make the auction successful," she says.

Online bidding, both in real time and through a timed auction (think eBay), can also greatly expand the swath of potential buyers for certain properties. But auctioneers have varying opinions on the value and appropriate application of the technique.

One proponent is Carl Montgomery at Comas Montgomery in Murfreesboro, Tenn. "Online auctions are extremely convenient for buyers, and allow us to expand a property's exposure to out-of-state buyers," says Montgomery, who is one of the 37 members of MarketNet Alliance, a group of auctioneers who share an online bidding platform.

Bonnette adds that real-time online auctions tend to drive up the selling price, "although I haven't found that many properties are being bought by the online bidders."

A new variation on the online auction model comes from AuctionPoint, a company based in Marina Del Ray, Calif., that created an auction tool specifically for commercial properties. The company sets up

individual property auction Web sites and provides the platform for the online auction. Brokers handle their own marketing.

Still, not everyone is convinced that the Web is the best forum for auctions. "Online-only auctions don't work as well for commercial property and don't even maximize prices in most residential sales," Kravets says. "They don't capture the electricity of a live auction." Video simulcasts can help capture some of that excitement, he notes.

### Brokers Play a Bigger Role

Another big change from the auctions of two decades ago is the growing sense of cooperation between commercial brokers and auctioneers. "In the past, there was a fear of competition between brokers and auctioneers, but now companies are recognizing that by partnering, they both have a great opportunity to make a living in a challenging market," Longly says.

Colliers International is one company that's acknowledging the growing demand for auctions by forming an alliance with the three-year-old auction arm of United Country Real Estate, based in Kansas City, Mo. "Commercial brokers bring an invaluable knowledge of their markets and buyers that's critical to a successful auction," says Mike Jones, president of United Country Auction Services.

At United Country, the auction option is often built into the overall commercial sales framework. "Listings are marketed conventionally for perhaps 120 days, and if there are no offers we take them to auction," Bonnette says.

Another major commercial player, NAI Global, has had an alliance since 2001 with Higginbotham Auctioneers International Ltd. of Lakeland, Fla. If a property is being auctioned, the local broker "assumes the role of showing the property. Local brokers are also bringing buyers to the auction," says Higginbotham General Manager John Haney.

Smaller brokers can partner with local or national auction companies to show properties or gather property information for the offering package, Spann notes.

Often, commercial brokers are reluctant to work with an auctioneer because they aren't educated about the auction process or how the compensation works, Bonnette says. "Once they realize that they'll get a commission split when they bring a listing or register a buyer for the auction, they become more receptive."

Brokers who aren't affiliated with an auction company can always earn referrals fees for suggesting an auction as an alternative when a property is not selling, Fine adds.

Brokers tend to look more favorably on auctions when they learn how fast that payday comes, says Bill Sheridan, president of Sheridan Realty & Auction in Mason, Mich., and 2009 chairman of the NATIONAL ASSOCIATION OF REALTORS® Auction Forum. Auctions also provide a way for a broker to earn commission even after a listing has expired, he adds.

## What the Future Holds

If you're interested in teaming up with an auctioneer, or even becoming one, you're probably wondering how demand for auctions will change after commercial markets have stabilized.

"Auctions have value in both good markets and slow ones," says Fine, who helped develop the NAR course "Introduction to Real Estate Auction," which can be taken online or in select locations (go to [www.coursecalendar.com](http://www.coursecalendar.com) for more information).

There will always be owners who need to sell quickly because of divorce, personal financial problems, or a new business strategy, he says. Similarly, corporations and retailers will always find auctions a convenient way to sell off surplus properties and retail outparcels.

Today's sellers, in general, are more interested in getting transactions closed fast—regardless of market conditions, Jones says. "The patience level in the market is not what it once was," he says.

Thanks to eBay, there's also a wider familiarity with the auction process, Gilmore says. "Buyers and commercial brokers are more educated about auctions, so there's less of a negative image," Winchell says.

The fact that the real estate market is becoming more global also will boost demand. Auctions are much more common in New Zealand, Australia, and South Africa than in the United States, so buyers and sellers who've worked in those areas will be more receptive, Sheridan says.

Looking ahead to when the commercial market has picked up steam and prices are appreciating again, auctions will be just as valuable for sellers as they are today, Fine says. That's because appraisals and comps may lag market price in a rising market. But an auction will capture the immediate value, he explains.

Ultimately, says Stephen Karbelk, president of National Commercial Auctioneers in Tulsa, Okla., there's a place for both auctions and conventional brokerage in every market—the choice depends on the client's circumstances. "We're here to solve the client's problems and get the property sold," he says.

## Is It Suitable for Auction?

Although any property could be auctioned, not every property is positioned to net the maximum return. Here are the key ingredients that experienced auctioneers say make a property best suited for this selling method:

- A realistic seller who understands current market pricing and has a sense of urgency.
- A seller with equity who can provide financing to buyers or make up any gaps between the mortgage owed and the sale price.
- A qualified buyer who's able to bring cash or secure financing rapidly.
- A well-conceived offering memorandum that resolves any issues with the property before the sale.

- A property that's generating cash flow.

#### Not All Auctions Are the Same

There are many different types of auctions. Know the terms so that you can help determine which method would work best for your client.

- Absolute auction. The property is sold to the highest bidder with no limiting conditions or amount
- Auction with a published minimum bid or reserve price. The minimum bid sets a floor for bidding, but the seller still reserves the right to accept or decline the bid at any time before the completion of the auction. These days, many auctioneers encourage sellers to choose a low minimum—50 percent to 60 percent of the last asking price—to demonstrate to buyers that the property will be sold.
- Unpublished reserve auction. The seller reserves the right to establish a reserve price, to accept or decline any and all bids, or to withdraw the property at any time prior to the auctioneer announcing the completion of the sale. Many auctioneers encourage sellers not to publish the reserve so that the seller has the option of taking a bid that is below the reserve.
- Sealed-bid auction. Confidential bids are submitted, to be opened at a predetermined place and time. It's not a true auction in that it does not allow for reaction from the competitive marketplace. Sealed bids allow the seller to choose a buyer on criteria other than price, such as ability to obtain financing.

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