



S.E.C. Real Estate Observer

AN E-PUBLICATION OF THE SOCIETY OF EXCHANGE COUNSELORS

Service. Experience. Counsel.



Inside This Issue

Welcome to the winter 2011 issue of the S.E.C. Observer. In this issue, Chris Dischinger, S.E.C., presents his final article as the 2011 President of S.E.C., and does an excellent job of defining the “history and importance of equity marketing.”

Jim Brondino, S.E.C., CCIM, completes his series on moderators as “value creators” in part two; and Ernie Eden reveals his “top ten multifamily performance tips from 2011.” Hunter Quistgard, S.E.C., explains how “perception drives all transactions,” and Steve England, S.E.C., ALC, provides formulas and strategies for “finding transactions in ‘dead’ listings.”

The S.E.C. Education Foundation presents “S.E.C. Takes it on the Road,” short pieces about our moderators as they travel the country running marketing sessions. In the Spotlight, guest author Jeffrey S. Weil, MCR.h, CCIM, SIOR, Senior Vice President of Colliers International, shares his “corporate office perspectives” in Office Times.com.

In the History Files, Richard Reno, S.E.C., advises brokers to “ask these questions first” before taking on a client; and Cliff Weaver, S.E.C., CCIM, imparts “personal money management” tips.

Anthony J. Bruozas of Childress Duffy Ltd., a national sponsor for the Society, provides valuable advice to the mortgagee when “providing financing for the sale of equipment, to confirm that their interest is correctly defined in the insurance policy.”

Enjoy this issue, and, as always, we welcome your comments, suggestions, and submission of articles to be considered for publication. Please contact the S.E.C. office via email sec@secounselors.com.

Jackie Hellingson
S.E.C. Observer Editor

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“Equity Marketing”

Chris Dischinger, S.E.C.
2011 President

It is probably fair to say that the first human commerce involved two primitive human beings arranging to trade one vital necessity for another (food for clothing, perhaps?). These early humans had no concept about currencies, banks, a federal reserve, or the idea of fiat money. Had the original cave man asked his neighbor to accept a piece of paper for that night's dinner and all the paper said was that the receiving party would receive some value in the future, the neighbor would have probably considered clubbing this charlatan to death.

Today we see that many people are again questioning the value of paper currency and what true value it will have in the future. We have recently seen a huge run up in the value of gold and silver precisely because many people fear what the true value of a dollar bill might be in the future. The other interesting occurrence today is the historic rate of return on the greenback. Today we are experiencing a rate of return on a 10-year treasury bill at slightly north of 2%. This rate of return of a long term instrument is not even equal to the rate of inflation. This means that an investor in the 10-year treasury is *expecting* to lose money on this investment, and they simply hope to preserve most of their capital.

Despite all the gloom and doom that has been associated with real estate the last four years, good investment real estate (read: *NOT* speculative vacation condos) continues to provide an excellent return (6-10% cap rates), a good hedge against inflation, strong tax advantages, possible appreciation and a tangible asset. (Once all these benefits are factored in most investors are looking at real returns on equity in the teens.) Real estate most certainly can go down in value, however much like gold or silver it has a value beyond a promise to pay. Real estate provides for basic human needs such as shelter, a place for commerce or land to grow food. Real estate is also limited in supply. The government cannot decide tomorrow to turn on the printing press and increase the supply of real estate in the United States by 10%.

OK, so these are some basic tenets on the value of real estate that have been around for centuries—what is the point, you ask? The point is that in an environment where cash may actually have less value than real estate, we should begin seeing more direct exchanges of real estate. I can certainly see a time when an owner of real estate may not be willing to do an exchange that does not result in ending up with the replacement real estate at closing (who would want to give up an 8% return for a 2% return?).

The Society of Exchange Counselors is a group of real estate professionals whose members are well versed in the ability to take a client from one real estate investment to another without the risk of getting stuck with cash.

Equity marketing is a process that we embrace that allows the client to either trade equity for equity or, at the very least, brings together several parties to a transaction at one time, thus reducing the chance our clients will get stuck with cash and possibly a onerous tax bill. The Society of Exchange Counselors meets six times a year in a forum that promotes transactions such as these and we pledge to provide service, counsel and experience in all that we do. Equity marketing and creative techniques also allow the client some control over financing by allowing two parties to trade equity for equity, structure tax deferred transactions, and limit the risks of finding suitable replacement properties.

Let's look at an example of how this might work with two parties with different goals:

Party A is a young aggressive real estate investor who acquired a vacant property, found a NNN tenant, built out the property and signed a long-term lease. The property is valued a 7% cap and has a 10-year lease.

Property value	\$1,000,000
Property loan	\$ 400,000
Equity	\$ 600,000

Party B is an older operator of apartments who no longer wants to hassle with the day-to-day operations. The property is also valued at a 7% cap.

Property value	\$2,000,000
Property loan	\$1,000,000
Equity	\$1,000,000

They arrange an exchange where Party A can take created equity and leverage into a more valuable property, can increase their depreciation, has the opportunity to raise rents with inflation, and take on a property that is easier to finance in today's market. Party B reduces management (NNN) and fluctuating rent, can either take some cash or diversify into another asset, could reduce debt, and pays only a portion of the taxes on their gain. Both parties achieve their respective goals and by closing simultaneously, reduce the reinvestment risk. In this case Party B could insist that Party A allows them to carryback a second mortgage which would qualify for installment sales treatment, thereby eliminating any taxes at closing.

If you stop and let your mind wander for a minute you can understand the infinite possibilities of how such transactions can be structured. It's these benefits that the buyers and sellers of real estate are truly seeking, not the dollar bills that normally accompany real estate transactions.

“Value Creators – Part 2”

Jim D. Brondino, S.E.C.

In the last article I spoke about the duties of the Moderator, what price is and how it is established, client participation, and TAKERS. Now, how does the Moderator fit into this equation? Moderators must be cognizant that value equates to the sum of the benefits as may be identified and/or interpreted by each individual. The Moderator’s task is twofold. First, the Moderator must extract from the Presenter and deliver to the participants (through well crafted questions) as many facts, feature, amenities, specifically stated opportunities, and/or potentials for profit that are present in the subject property. And, secondly, through this same questioning procedure and reveal through the Presenter, the client’s capabilities, talents, expertise, property ownership experience, skill and other assets they are willing and/or capable of contributing to the transaction, including what the client is prepared to do to forward a transaction. The list again is:

1. Discount and buyback
2. Lease back
3. Lend back
4. Joint venture forfeiting cash flow
5. Partition the cash flow and provide a high rate of return
6. Joint venture providing a safety first position
7. Take a low interest carry back note
8. Make a geographical move (relocate)
9. Take on a negative cash flow
10. Use financial strength
11. Accept personal property
12. Move the debt
13. Provide management
14. Take property in any location
15. Remain responsible for the existing debt
16. Remain responsible for the payments
17. Obtain the entitlements to the property
18. Mitigate wetlands or other environmental restraints on the property
19. Pay all closing costs
20. Add cash (amount)
21. Other!

It is the Moderator’s responsibility to flush out, in a concise manner, all the significant information from the Presenter needed by those assembled to cause action, whether it be verbal or written. This process enables the participants to tally the benefits appropriate to their situation or circumstances.

Moderators must remain focused and objective. Although on rare occasions it does become necessary to elucidate a possible benefit, this circumstance arises only when the information from the Presenter remains confusing or unclear. Moderators should have confidence that the participants listening to a well-designed presentation can integrate what they hear and learn in order to ascertain for themselves whether benefits exist or not, both for them and/or their respective clients.

When someone declares they are a **TAKER** of any sort, or something is “worth it,” they have addressed to their satisfaction one or all of the following:

1. I am content and complete with what is presented.
2. I can pass on what is presented to one of my contacts, associates or network more expeditiously now.
3. I can convert what is presented into the benefits I seek.
4. What is presented is a more efficient means to achieving my goals.
5. What is presented creates an opportunity for future profits.
6. What is presented makes debt easier to pay or more manageable.
7. What is presented provides sufficient tax advantages.
8. What is presented creates greater self-esteem and a sense of self-worth.

The ultimate goal is to have someone, either participant or client, proclaim: “Under the following conditions, the presentation or transaction idea is worth it; therefore, I’LL TAKE IT!” Those are the sweetest words that you, as the Presenter, can ever hear. It is at this point that the Presenter or client, and the **TAKER**, have reconciled in their respective minds the price-benefits-value components.

Moderators who understand the elusive concept of value allow the participants to identify for their clients or themselves the benefits available. Formulating questions which allow the Presenter to reveal, in an orderly fashion, information about the property and the ownership create value in the audience’s eye. The more benefits that can be interpreted from a presentation, the more value it has!

III. Society Columns A. Top Ten Multifamily Performance Tips from 2011

“Top Ten Multifamily Performance Tips from 2011”

Ernie M. Eden, S.E.C., CCIM

Most people like top ten lists because you know when they end, right? But if you manage, invest in, finance, or own apartments, you never want to see an end to good ideas for better performance.

1. **Location:** Buy or build in locations that will drive rent and occupancy increases over time. Look at the long-term history and the future potential of the area. Have there been consistent growth patterns in population, housing units, and businesses in the area? Are there proposed new developments, factories, hospitals, or other job generators in the area? Are there barriers to entry in the submarket?
2. **Tenant Retention:** Build your business plan in such a way as to reduce turnover. Build or improve for the long haul. Install improvements that will encourage renters to stay. Consider using 24-month leases instead of 6-month or 12-month leases.
3. **Improvements:** Make sure that your planned improvements will drive rents and occupancy as well as decrease operating expenses. This may include energy-saving improvements or those that shift utility costs to tenants, or improvements that dramatically reduce cleaning costs or replacement costs over time. Examples include replacing carpeted areas with ceramic tile or wood laminate flooring.
4. **Technology:** Don't overlook technology items in new developments. Young renters moving in will have had recent student housing experience that far outshines most of the competition in most non-student housing. If you include some of these improvements and the competition does not, you may attract those who now depend on some of these “must-have” technological items.
5. **Upgrade:** Repositioning existing communities can be very profitable. Exterior curb appeal is one part of it. Upgrading unit interiors is another part. Upgrading the rents and the tenant profile is still another dimension. Eventually the goal is to improve the property dramatically by making moderate investments that have far-reaching results.

6. **Young & Old:** Don't overlook niche apartment submarkets like student housing and the senior market. Students often rent by the room, and the resulting total rents may be higher per square foot than typical. Some senior housing developers tell us that they can achieve higher rents because seniors will pay a premium to be around other seniors. In addition, their operating costs are substantially lower due to a number of factors, including lower maintenance costs and substantially lower turnover rates.
7. **Analysis:** Make sure you do a good rental market survey in the submarket area you are considering. Use apples-to-apples comparisons, regarding utilities and fees included or not included in the rent, pay attention to both per unit and per-square-foot rents, as well as year of construction and amenities.
8. **What If:** When preparing operating pro-formas, make sure to include several scenarios for each opportunity. Best, worst, and probable are three good ways to do this. This may include different occupancy levels, different rent levels, and different expense scenarios. By the time you're finished, you may have 10 to 20 different combinations. It is a good idea to know the range of possible outcomes.
9. **Show Me the Money:** Recapitalizing a property can often make a real difference. We have brought in cash investors forming joint ventures to pay off loans, sometimes at a discount.
10. **Low Leverage:** Consider using a lower loan to value ratio for financing your property. It will be a much safer investment if you borrow less. The power of leverage is hard to resist, but the power of no debt can be a liberating experience.

These are our top ten performance tips for 2011.

“Perception Drives All Transactions”

Hunter Quistgard, S.E.C.

Able walked into our office to hear about how to exchange. He had bought a promotionally sold lot in a distant “recreation” development on terms a few years back. He paid \$11,500 for the lot and still owed \$7,218 and was paying \$115 per month including 7% interest. A quick check of its sale value found the lot would sell for \$4,500, more or less, so Able had a negative equity (not uncommon in today’s market), although no one discussed those facts with Able.

Baker had walked into our office a couple weeks before and listed a duplex that was negative cash flow on the net income vs. the existing mortgage of \$48,000 in the amount of \$350 per month.

It was proposed to Able that he might trade his lot equity, subject to its existing loan, for the equity in the duplex and that if he did all the management, maintenance and upgrades with his own time and effort, the duplex would only be negative cash flow about \$100 per month. In which case, maybe future rent increases, lowered payment from a refinance, or some other windfall might get him to break even and the project would be a forced savings program for his young family with the renters paying down the loan over time to gain him a bigger equity, regardless of what appreciation might happen.

There was no cash to pay commissions, but Able had an old “dirt” motorcycle he presented the broker for his fee, which worked perfectly for the broker’s Christmas present to his son. The duplex owner had a time share he was tired of maintaining, so that was the broker’s fee from him.

Able’s lot was originally purchased with seller carry back loan in California which does not allow personal liability, but only seeks the collateral (just for such circumstances). Baker gave a deed in lieu to the note holder on the lot and saved \$350 per month out of pocket + \$945 per year maintenance fees on his timeshare (= definance).

Able was enthusiastic to use the duplex to teach his kids property management and equity growth as he gave the equity to them for their college fund, but they had to run it themselves (ala Tom Peterson, S.E.C., whose kids are now real estate tycoons). He made them do carwashes, yard work and bake sales to pay the closing costs. He agreed to pay the \$100 negative cash flow, but no more. If there was more negative, they would have to contribute from their allowance or from other earnings. He kept the title to get the depreciation, but the kids got a contract to own it for \$1 when they needed the money for college.

Baker used the extra cash flow from his salary to pay down his credit card debt and was free and clear inside of 18 months, and then was able to qualify for a refinance on his home to raise funds to invest at higher yield than the 4% his new home loan was costing.

The broker was creative, but not successful, so he lost the time share to his ex-wife, and his son crashed the dirt bike and ended up in the hospital. He was, unfortunately, uninsured and now the broker stands by the freeway entrance holding a sign that reads “Will develop real estate for food.”

“Finding Transactions in ‘Dead’ Listings”

Stephen R. England, S.E.C., ALC

It is my observation that the typical commercial brokerage company has within their stagnant exclusive listings many potential transactions. However, many brokers don't seem to be able to find them so they spend hours cold calling for new products and clients.

Why does this happen? First of all, many brokers think that probably the only potential transaction is to a Buyer that has cash or can bring financing. Many suggest the only action to take with inactive listings is to convince the client to lower his asking price. This may not best serve the clients and their goals, thus nothing happens.

The reality is that there are many more potential transactions when considering exchanging of equities than there ever will be only looking for cash buyers. These exchanges can create the “benefits” that your client is seeking and by exchanging, there are many more potential “takers” for their property than just cash buyers.

How does one analyze his company's listings to find these transactions?

1. Review everything you know about each property and the “benefits” to give a new owner. Will it provide cash flow? A good opportunity for growth in value? Pride of ownership? Little management?
2. Review what your client's capabilities are.
 - a. Why are they selling? Maybe only to reinvest in something they like better? Will they add cash or equities in other properties to exchange up to a larger investment that they like?
 - b. What types of other real estate do they own or have experience with? What types of real estate do they prefer?
 - c. Do they own your listing free and clear or what is the current financing? Is it assumable or easily financed? Can they make it free and clear?
 - d. If this is a problem-based sale do you understand their situation fully? Do they have negative cash flow they cannot handle? Do they have developable land but no expertise or resources to develop themselves? Do they need to dissolve a partnership?

The above are only a few of the counseling questions that need to be known to do a complete job of representing clients and finding successful transactions. Counseling finds transactions!

Examples of exchange transactions closed with counseling:

#1: Seller has free and clear office building that is 60% occupied.

Buyer would like to own but doesn't want to borrow in this economy. Potential Buyer is found to own a good commercial site that is not selling in this market.

Broker suggests that Buyer create a 40% LTV down payment note against the commercial lot to give to Seller and the Seller carries back 60% LTV financing on the office building. Transaction closes with Buyer activating dead equity while waiting for a land buyer. Seller gets out of management and has a permanent income stream. Seller gets his down payment in cash when the land actually sells.

#2: Seller is a bank with a foreclosed irrigated farm for sale. No current cash buyers seem to be available at or near the asking price the bank needs.

Buyer prospect found but has no down payment cash available. In counseling Buyer, the Broker learns prospect owns a lake cabin free and clear. Broker suggests that the Buyer offer the cabin as the down payment and ask the bank to create the balance of the financing. Exchange transaction closes.

Selling bank discounts the cabin by 50% and sells immediately for cash. Even with the large discount on the cabin, the total net on the farm is substantially higher than the price potential from cash prospects previously found.

#3: Seller listed a 103 room motel that had excellent cash flow but required major remodel and upgrade to keep franchise. Seller currently had other priorities and didn't want to finance this large rehab.

Cash Buyer prospects were very few and initial prospects wanted to severely discount the property due to rehab necessary.

Broker attended a national marketing session and found a motel contractor that wanted to do the rehab but didn't have the ability to put cash in for down payment or secure the final larger loan needed. Broker located a third investor that liked hotels and had some condos in another state that he owned free and clear and was willing to let them be used for the down payment plus qualify for the loan. Transaction successfully closed because all parties achieved the benefits they were seeking. Motel Seller sold the condos for cash a few months later.

Summary: Find these transactions and it will be fun and profitable for the client and the broker. Counseling and exchange formulas are the key! Anyone can attend Society classes to learn if you need more knowledge.

Why not perfect counseling and creativity skills to find transactions for clients and inventory that you *already* control?

“S.E.C. Takes It on the Road to Ohio”

Wes Dinger and Brandon Sanders recently ran the Ohio Creative Real Estate Association (ORCEA) in Columbus, Ohio. This effort was supported in part by your S.E.C. Education Foundation in an effort to bring our style of marketing and the formulas we use to regional marketing groups. Both Dinger and Sanders moderated many packages and did an excellent job running the meeting.

S.E.C.s also in attendance were Lance Warner, Harry Kennerk, Ron Bowden, and Gary Vandenberg. Warner assisted with sound setup and various other tasks to keep the meeting running smoothly.

At one point Bill Bussey, CCIM from Grand Rapids, Michigan, asked for input on how to deal with a bank OREO client that had unrealistically high expectations of their large vacant building's worth.

Bowden said to contact the decision maker and agree with them on price IF:

1. They went to the trouble and expense of leasing the property and paying lease fees, and making tenant improvements.

If they don't want to do that, a somewhat reduced price could be obtained IF:

2. They finance for the buyer with easy terms.

If they don't want to do that and only want an all cash sale, they will need to:

3. Discount the price heavily.

Bussey loved the suggestions. Instead of arguing with the client, he can agree with them and still get the message across.

That was the type of counseling that took place in the regional marketing session, bringing S.E.C. ideas and knowledge to exchangers across the country.

“S.E.C. Takes It on the Road to Indiana”

Larry Browning, S.E.C., was lead moderator at the 33rd IREX (Indiana Real Estate Exchangers) Fall Marketing session September 29th and 30th. There were over fifty in attendance at the fast-paced event. Other S.E.C. members in attendance were Ron Bowden, Harry Kennerk, S.E.C. President Chris Dischinger, and Gary Vandenberg.

By calling on S.E.C. members and other local experienced equity marketers to assist in moderating, Larry presented a great mix of moderated formal presentations along with opportunities for quick presentations.

It is great that the S.E.C. continues to offer moderating leadership in this active equity marketing area. We are rewarded with a steady stream of quality guests from Indiana and the surrounding states at our national marketing meetings.

“S.E.C. Takes It on the Road to Kansas”

Peter West, S.E.C., led the Kansas CCIM Invitational Marketing Session October 19th. Peter did an excellent job of combining Counseling Questions with his other moderating skills. The results created a terrific atmosphere where people new to equity marketing learned what they needed to learn from their clients while all participants discovered information they needed to write creative and closable transactions. Peter received rave reviews from all those in attendance.

Rod Stewart, S.E.C., is the brainchild behind the Kansas meeting which has been going on for many years. Rod was assisted by other local S.E.C. members, Leo Goseland, Nick Esterline, Colby Sandlian, and S.E.C. guest Vicki Hunt. Out-of-town S.E.C. members in attendance were Jim Smith, Bill Richert, Jon and Steve England, Wes Dingler, and Gary Vandenberg.

“S.E.C. Takes It on the Road to Texas”

Brandon Sanders, S.E.C., was lead moderator at the 3rd Annual CCIM West Texas Marketing Session held in San Angelo, TX on October 7th. This is a start up group consisting of several CCIMs across the western area as well as some new faces trying to get into the business. There were 25 in attendance covering a 3 hour radius of surrounding towns. Other S.E.C. members/candidates in attendance were Wes Dingler, Steve Eustis, Cindy Snell, and Bryan Neal.

Brandon realized that this was a newer group of exchangers that needed some additional knowledge, so he put together a special morning class and flew in Mr. Bill Exeter to teach and answer questions for about 3 hours. Mr. Exeter gave a very professional and formal discussion on exchanges and then opened for several questions and scenarios from the group. It was truly a hit and many positive comments have been circulating since that time. Mr. Exeter also attended a special reception the night before and presented his information to a group of local attorneys and CPAs from the area. Many had questions and all received thorough and thoughtful answers.

The session continued through the rest of the day with a chance for everyone to present properties, and with the valuable help of the other S.E.C. members and guests in the room it was

very beneficial to those in attendance. There have been several letters and emails that have been circulating in appreciation of the hard work and excitement that the sessions generated.

The ideas and advice that entered the room from those who understand the creativity and brainpower that comes from the S.E.C. Exchange Meetings really made this a successful event with positive and lasting impressions on the local contacts.

Please contact the S.E.C. Office sec@secounselors.com if you would like to apply for assistance from the S.E.C. Education Foundation to send one of our approved moderators to assist you with your marketing session.

S.E.C. National Invitational Marketing Session

**Las Vegas, Nevada
*January 22-25, 2012***

The S.E.C. National Invitational Marketing Session will be held at the [RIO All Suites Hotel, 3700 W. Flamingo Road, Las Vegas, Nevada, 89103.](#) The special room rate for S.E.C. meeting attendees is \$60.00 for Sunday and Monday, and \$125.00 any other night, single or double.

Call (702) 777-7776 for reservations. Make your hotel reservations early; we have a limited number of rooms available. The cut-off day for reservations is January 3, 2012, or when we fill our room block.

Visit www.playrio.com to learn about the hotel, and visit www.visitlasvegas.com to learn about the Greater Las Vegas area. For rental cars, call AVIS, (800) 331-1600, and give our AWD# D833386 for special rates.

Visit www.secounselors.com and click on the “Society Marketing Meetings” tab for more information. Please contact the S.E.C. Office, sec@secounselors.com, if you have any questions about the Las Vegas meeting.

“Ten Things that Should be on Your Due Diligence List ... But Probably Aren’t”

John Brennan, S.E.C., CCIM & Vicki Yeoman, S.E.C., CCIM

“Due Diligence on our Food & Water for Environmental Contamination”

Roy Moore, S.E.C.

The S.E.C. Education Foundation is pleased to present two important programs that focus on due diligence in both real estate and in our environment, from 1:00 p.m. to 5:00 p.m. on January 22, 2012, in Las Vegas, Nevada.

The courses will teach you due diligence techniques to use in your real estate practice and your life.

Mark your calendars now! Please visit the *S.E.C. Observer* at www.secobserver.com and click on “Upcoming Events” to access the calendar of events and view a brochure for the course.

S.E.C. National Invitational Marketing Session

**San Antonio, Texas
March 18-21, 2012**

The S.E.C. National Invitational Marketing Session will be held at the [historic Menger Hotel, 204 Alamo Plaza, San Antonio, Texas, 78205](#). The special room rate for S.E.C. meeting attendees is \$119.00, single or double.

Call (210) 223-4361 for reservations. Make your hotel reservations early; we have a limited number of rooms available. The cut-off day for reservations is February 25, 2012, or when we fill our room block.

Visit www.1859historichotels.com to learn about the hotel, and visit www.visitsanantonio.com to learn about the San Antonio area. For rental cars, call AVIS, (800) 331-1600, and give our AWD# D833386 for special rates.

Visit www.secounselors.com and click on the “Society Marketing Meetings” tab for more information. Please contact the S.E.C. Office, sec@secounselors.com, if you have any questions about the San Antonio meeting.

This article was submitted by Steve Eustis, S.E.C., with permission to reprint from Jeffrey Weil.

officetimes.com

Corporate Office Perspectives

Jeffrey S. Weil,

MCR.h, CCIM, SIOR

Colliers International

Senior Vice President

Charles Dickens once said, "It was the best of times, it was the worst of times ..." and this is so true regarding today's office market. There are office building owners who either purchased at the market heights of 2006/2007, over-leveraged, lost their major tenants or otherwise fell into that dark tunnel that causes financial and emotional pain, and we are still seeing office building foreclosures as a result. I know smaller and medium-sized companies which are struggling just to cover expenses, and U.S. bankruptcy filings are nearing a five-year high. On the other side of this equation, office tenants still have a field day in most U.S. submarkets with substantial landlord concessions such as free rent, lowered rent, generous tenant improvement allowances and other inducements still the name of the game. Several stronger submarkets such as San Francisco's South of the Market have experienced substantial office rental rate increases and building sales prices approaching the high-water mark of the 2006/2007 "frothy times." Investors fortunate enough to buy at the bottom of the market in 2007/2008 are making huge profits when they sell in 2011. In short, it is either a great time, or a terrible time to be in the office market industry, depending on where and when you got in, and your particular circumstances. To put more wrinkles in this fluid equation, factors totally out of our control dictate the stock market, lending practices and the corporate hiring appetite. Greece or Italy's fiscal policy mood can send Wall Street sharply up or down but how can companies make long-term business decisions based on such short-term volatility? Perhaps we will look back one day and make more sense out of what we are going through, but until then...

What a cool idea! Researchers from the University of California San Diego have concluded that solar panels on your building's roof not only provide clean power, they cool your workplace as well. They determined that during the day the building's ceiling was 5 degrees cooler under solar panels than under an exposed roof, and at night the panels helped hold heat in, reducing heating costs in the winter ... like getting a 5 percent discount on the solar panel's price over the panels' lifetime What would a skyscraper office building tower look like if it were all spread out as low-rise suburban development ... in *Wired*, (November 2011) they dissected a typical 1.3 million square foot mixed-use skyscraper, which in New York would cover 60 percent of the average block ... but spread out in a suburban setting with open parking the same amount of mixed-use construction would eat up more than 21 blocks ... yeah, I know you have been staying up all night wondering about this ...

Office buildings have seen utility and fixed expenses decline between 2009 and 2010 for U.S. private-sector office buildings, with a 5.5 percent decrease in utility expenses and a 9.2 percent decrease in fixed expenses, according to the Building Owners and Management Association's 2011 recent report. One reason behind these decreasing costs is more low and no-cost energy reduction strategies on the part of property managers to cut costs and more expense management ... so if you are an office tenant and you are still getting billed for operating expense passthrough increases ... *Buildings Magazine* (October 2011)

Boosting employee productivity and happiness through telecommuting ... a recent survey by Staples showed that 40 percent of respondents claim they would rather take a pay cut than give up telecommuting. "About 86 percent of respondents say they are more productive when they work from home, with 73 percent adding that they even eat healthier when working from the home office. More than 80 percent say they now have a better work/life balance even though nearly as many - 76 percent also said they are more willing to put in extra time at work." *Buildings Magazine* (September 2011)

TM way back in the 1970s stood for Transcendental Meditation and please don't ask me what that means, but today it more aptly describes our national office scene - Transitional Market - Subregions such as San Francisco are experiencing "frothy" sales prices and spiking rent rate increases, while only 30 miles away, other subregions have Class A identity office buildings selling for \$80 to \$120/square foot and rental rates so low that after expenses, tenant improvements and leasing costs, there is barely any return to pay the mortgage. Commercial development is almost nonexistent with the exception of apartment house construction, there are still millions of homes yet to be foreclosed, an estimated 25 percent of all U.S. homes with mortgages are underwater, and yet for our young folks with good jobs there may not be a better time to buy a home with 30-year fixed rate financing in the mid-4 percent range. Other than major office campuses such as Apple (2 million square feet), Salesforce and a handful of others, office development is in long-term hibernation. In many regions, office rates will have to double before new construction begins to make sense. Corporate America appears in no hurry to increase permanent payroll, instead relying on off-shoring, technology and contract hiring. The stock market jumps up or dives down 300 points in a day, decisions made in Greece or Italy impacts American business confidence almost at random, and when all is said and done, business basics remain critical. Hiring the right workforce, marketing your product or service effectively, taking advantage of low office rents to lock in long-term quality office space that synergizes your employees, helps with retention and takes advantage of new trends in worker mobility and teaming. My daily commercial real estate blog at www.blog.officetimes.com addresses issues of the moment, and thank you for reading this 190th issue of OfficeTimes!

The future of teleconferencing ... just out is the new Polycom system which brings web-based videoconferencing to iPad and other tablets ... it may not be too long when almost any conference room can be turned into a teleconference center, with a future iPad wireless doing the connectivity to the wall-mounted large flat screen in real time for teleconferencing at super-low cost, and smaller teleconferencing off iPads anyplace and anywhere (except while driving ... can

you see the next driving citation- not just "Don't text and drive" but "Don't teleconference and drive ...") *Bay Area News Group* (October 11, 2011)

A number of cities are mandating that building owners report their energy usage, including San Francisco, New York, Seattle and Washington DC ... the disclosure typically includes reporting the past years' utility cost, being rated based on projected energy usage, and being rating based on actual performance ... energy efficiency proponents want more transparency, while office building owners may object to these mandatory reporting requirements which can create budgetary pressures to go green when there might not be the green to do so ... *Buildings Magazine* (October 2011)

Collaboration over isolation ... according to a recent study by Johnson Controls, by 2020 collaborative workspaces will dominate over private offices ... "office workers anticipate spending more time working in team spaces that incorporate collaborative technologies, interactive digital screens, touch surfaces, and global live streaming will become the norm, according to over 1,700 respondents in seven countries." *Buildings Magazine* (October 2011) ... basically there is a huge growth in virtual and office teaming, while at the same time employees are decreasing the time spent at their desks ... companies understanding this shift in dynamics can free up underutilized office facilities and lower the cost of doing business ...

California State ranking in July/August 2011 *Business Facilities* magazine ... #3 in Installed Wind Power Capacity, #1 in Installed Solar Power Capacity, #1 in Biotechnology Strength, #5 in Alternative Energy, #4 in Best Transportation Infrastructure, and for Medical Devices Industry Leaders out of the top 10 cities, California had three spots: #1 Los Angeles, #6 San Jose and #7 San Francisco/Oakland ... For clean tech, again three of the top ten spots with #3 San Jose, #4 San Francisco and #9 Pasadena ... if you want to see the entire report, [click here](#). *Business Facilities* (July/August 2011)

LEED certification for office buildings ... 101 California St., San Francisco, a 48-story, 1.25 million square foot Class A office building in the heart of the financial district just received 94 points out of a possible 100 points, beating out 7,306 buildings worldwide which have won LEED certification under the existing building program. Here is what they did: restroom fixtures were replaced, landscaping revamped to monitor water usage, all cleaning products are now green-seal certified, cleaning equipment stresses reuse vs. disposable, all vacuums use HEPA filters, bike parking was expanded, electric car chargers were installed in the front of the parking garage, they hired a loading dock sorter who opens and analyzes the trash bags and then sorts for recycling (yummm), they replaced standard light bulbs with LED lighting ... and no, they don't recycle their leasing agents ... *SF Business Times* (October 7-13, 2011)

Energy use by major corporate office and data centers continue to decrease as new forms of energy reduction and energy harvesting are discovered. HP has designed their new servers with new processors that take up less space and consume only a tenth of the electricity needed to power conventional servers, offering huge savings potential to companies expanding their data

centers. The new solar power system Facebook plans to use for its new Menlo Park headquarters will combine solar cells, mirrors, and fluid-filled tubes behind the solar cells. Curved troughs of mirrors will concentrate sunlight on the cells, while motors will keep the troughs pointed at the sun as it arcs across the sky. This is being installed by Cogenra Solar, a Mountain View startup, and the payback on initial investment is estimated at less than five years. *Bay Area News Group* (November 2, 2011)

Electric charging stations for cars at office buildings ... we are starting to see a variety of office building responses to the rapidly increasing fleet of 100 percent electric cars, including special signs for electric car parking near the front of the building, but without any outlets to charge the car. I have also seen electric car owners seek out the sometimes-rare and hard to find 110 volt outlet in the office building garage, and as one Nissan Leaf owner told me, if he can't charge his car during the day he has no way to get home with his 50 mile range ... what is the cost, ballpark, for this use of juice? I saw one quote, based on a national average electricity price, of \$3 per day to charge a Leaf ... how will this be fairly allocated to a multi-tenanted office building ... not a problem with one or two cars, but one day there may be hundreds needing daily charges at larger office buildings ...

The New Workplace - Contract employment, hiring for the task and project, not necessarily for life. Collaborative, idea-sharing, synergistic environments that foster teaming, innovation, creativity ... which does not work well if everyone is in their own private offices ... less entitlement/reward based space assignments-getting the big private office may not be a perk like it was ... working anywhere, any place, mobile and nimble ... global teams supported by technology, teleconferencing, Skype, teaming with associates in India, Europe, Asia ... generational challenges, new workers are iPad, iPhone and text-savvy, older generations may still have issues trying to email docs - iPad vs. fax machine ... *SF Business Times* (October 28, 2011)

Facebook's new headquarters in Menlo Park has the overhead heating and cooling ductwork exposed, with power and data cables hanging from the ceiling to the individual work spaces. Facebook employees work side by side at long, undivided tables and there aren't offices or cubicles to impede collaboration. Floor-to-ceiling blackboards allow employees to self-express themselves, and as one architect commented, "It's architecture as a management tool." *Bay Area News Group* This portion of my newsletter is often the hardest to write. Dealing with industry trends, transactions and factoids is so much easier than attempting to impart a philosophical thought or two, especially with the overriding objective to have a positive, upbeat message. How the priest, pastor or rabbi must be gifted to deal with this on a weekly basis! As we approach the Season of New Year Resolutions I'm reminded of those I have made in the past, only to neglect and forget while they fell by the wayside. However, the power of the pen will make this year different, and perhaps the reader will reflect and follow suit in their own mode and method. I resolve that no matter how I feel or what has happened or is happening around me, that at least once each day I will be a positive influence on a fellow human being. We are only in control of and responsible for our own thoughts and actions but just think if we each made our own

personal positive-impacting resolution ... have a safe, wonderful holiday season, and if I can be of any positive assistance in your commercial real estate needs please don't hesitate to contact me ... and if you want to post your own New Year resolution feel free to do so on my blog!
www.blog.officetimes.com.

Have a safe and wonderful holiday season!

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“Ask These Questions First”

Richard R. Reno, S.E.C.

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Many things have been written and said about real estate counseling. Here are some random questions which should be answered prior to exposing the property and the client to the marketplace.

1. Why does the client desire to move his equity and what is the real motivation for selling or exchanging the property?
2. Is the client a buyer and what are the guidelines in using equity for a down payment?
3. What will the client take “in lieu of” his existing equity?
4. Is there a mandatory cash requirement needed in the transaction?
5. The client has an immediate objective. Have I really determined what it is and what is behind the immediate objective motivation?
6. Does the client understand “benefits” (money, appreciation, depreciation, income etc.)?
7. Why would someone want to own the property being offered by my client?
8. Is the client mentally committed to a fixed price for his real estate or is the client oriented toward increasing benefits?
9. Have I determined what items the client can add to the real estate offering to make the entire “package” more attractive?
10. Has the client verbally accepted other properties in our counseling sessions?
11. Have I explored the idea of the client being a user for a business opportunity?
12. Will the client make offers to solve his real estate problems if the offers solve his immediate objectives and lead toward his long range objectives?
13. Is the client capable of a joint venture with his equity or portions of his equity?

14. Is the client under a third party influence?
15. Has the broker done all of the homework needed to move title?
16. Does the client have any geographical limitations?
17. Has the property been offered on the market prior to my listing?
18. Does the client or his real estate offer management problems?
19. Frankly, is the client a realist?
20. Do I really feel I have a client who *does* have a real estate problem?

The above are just a few questions that real estate agents should determine in their counseling sessions prior to offering the property to the marketplace.

“Personal Money Management”

Clifford P. Weaver, S.E.C.

Editor's Note: This article first appeared in the July 1975 edition of the Real Estate News Observer.

If you are having a problem with cash flow, the reason may be one of the following eight traps in Personal Money Management.

Too Much House:

Frankly, it is very easy for the American public to buy a home which can be acquired from “nothing down” to “very little down.” The bright side of the picture is the fact that “little or no capital” is required for the initial down payment. However, the other side is that the monthly principal and interest is high. Few buyers take into consideration the inflationary cost of water, gas, electricity and other utilities. There are five factors to be considered by a potential home buyer:

1. The cost of furnishing each room in the house.
2. The cost of equipping a home for indoor and outdoor maintenance.
3. The tax collector raising property taxes to meet governmental obligations.
4. A simple lawn turning into a botanical garden or tribute to a weed patch, depending on the occupation of the owner.
5. The physical and time-consuming effort required by a working wife.

Too Much Automobile:

Most people do not pay cash for automobiles and most “over buy” autos. This means they buy larger autos than actually needed. This trend was curtailed somewhat in 1974 during the energy crunch. However, heavy payments on automobiles is just the tip of the iceberg when considering the cost of gas, insurance and maintenance. The fact is, since World War II, the American public has kept themselves in heavy debt by keeping up with the neighbors and rolling out a new auto every third year, when the loan is finally paid off. Don't forget how the value of your auto was affected the moment you drove it off the lot.

The Ego Problem:

It is a fact: we all like to be liked! However, many people lack a certain amount of individualism and need a checkbook to solve their ego problems. Some are continual buyers of gifts; others buy for themselves. Think of the first person to wear a “Read the Time” watch. Think of the person who was the first to buy an “ecology garbage pulverizer”—the neatest garbage compacter in town. People buy things to impress friends and business associates in order to maintain their egos, and this is very costly.

The Expense Account:

Some people are “blessed” with an expense account—or are they? On the road, they live like millionaires, and then come back to realism. Outside of the mental problems of living in a make-believe world, most fail financially when they attempt to live that way at home. The company or employer is not funding the home overhead. It isn’t uncommon for this person to end up having a fifty dollar luncheon and then going home to a dinner of Hamburger Helper.

Hobby Time:

Hobbies can be expensive. Give a man a tennis ball and he might end up with \$500 in tennis togs, a \$50 racket and a \$5000 interest in a “Condo Tennis Club.” Did you ever hear about the potential golfer who pyramided a \$1.00 golf ball into a \$6500 golf membership? How about initially buying a simple Polaroid “Swinger” camera and then swinging your interest upwards to \$2,500 in cameras and camera lenses, together with a good darkroom? Why not take up vacuuming instead; your spouse will love you!

Being Fashionable:

This is a potential trap for both men and women. First, there is nothing wrong with being well dressed. But some people attempt to set high fashion standards and set aside a lot of money to maintain that image. This ego trip is costly for many and they do not have their priorities in line. They sacrifice savings and long range benefits for being a pricey fashion plate today.

It’s A Small World:

Take your kids to Disneyland and see the Bank of America exhibit called “It’s A Small World.” You’ll see it *is* a small world, as it is a natural parental wish to want your kids to have everything. The fact is, beyond a certain minimum, your kids could care less. Remember the time you gave a child a big present for his birthday and he played with the gift for ten minutes, and then had fun with the box the gift came in for three hours?

The Itch and Urge:

Impulse and spur-of-the-moment buying is one of America’s greatest money management problems. Many will cop out and say “You only live once.” The fact is that Madison Avenue in New York has the urge to splurge planned to produce a lifetime of results for their customers and clients and it costs you, the consumer, money. Have you ever bought an item at the checkout counter while you were waiting to be checked out? It’s planned by the store to make you wait so your impulses will react to buying an item on immediate display. These items are normally priced a little higher than the same item back on the shelves.

Lastly, if you don’t believe any of the above is true, toss away your credit cards and see how you live (it’s not a bad idea anyhow, as you are most likely paying 18% on your unpaid balance).



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When providing finance for the sale of equipment, the mortgagee should confirm that his interest is correctly defined in the Insurance Policy

Anthony J. Bruozas
Childress Duffy, Ltd.

Recently, in a local newspaper, there was a story about a convenience store owner who suffered a fire that nearly destroyed the entire store. Prior to the loss, the store owner was lucky enough to convince a bank to lend him some money for operating capital. After conducting an investigation and being unable to find sufficient reason to fully deny the store owner's claim, the insurance company reluctantly issued a check to the store owner for a fraction of the policy limits. The check, however, did not also name the lender. The check provided by the insurance company for the damage to the store owner was a paltry sum and only covered a fraction of the costs it would take to rebuild. Therefore, the store owner took the money and left town for greener pastures. The lender learned of the loss and subsequent claim adjustment by the insurance company and decided to make its own claim against the insurance company to cover its loan. Unsurprisingly, the insurer responded that the lender was not listed on the policy as any type of "insurable interest" and therefore owed the lender nothing. Following several rounds of correspondence between the lender and the insurer, the lender decided that it had sufficient grounds to sue both the insurance agent and the insurance company.

After some intense discovery battles during the litigation, the lender was able to obtain a court order to obtain copies of the insurance company's underwriting and claim files. These documents provided important information including the insurance application submitted by the storeowner, the identities of the various "insurable interests" under the policy, coverage effective dates, what coverage applies and deductible(s).

The underwriting file revealed that the insurance agent had neglected to include the lender's name as a loss payee on the insurance application. However, when questioned during his deposition, the agent admitted that the store owner did inform him of the identity of the lender and that the lender needed to be identified on the policy as an "additional insured" or "loss payee". The agent, fresh out of college not yet familiar with the customs and practices of the insurance industry, scrupulously testified that he simply forgot to inform the insurance company

that the lender needed to be included on the policy. When further questioned by the bank's attorney, the agent said that the lender's interest should have been defined as a "lender loss payee." While the insurance company fought as hard as it could as long as it could, it eventually concluded that it would likely lose at the trial. Just days before the trial after many, many depositions, the insurer sent a check to the lender for the full amount remaining under its loan to the storeowner.

This example shows that a lender or anyone financing the sale of equipment, i.e., mortgagee, has little control over whether or not his customer notifies the insurance agent of its insurable interest under the storeowner's policy and even less over the agent in informing the insurance company of that interest. That is why the mortgagee should take the initiative to independently confirm with the insurance agent *and* insurer that his "**loss payable**" interest is properly reflected on the policy. However, knowing that one should just be a "**loss payee**" on the policy is not enough information. Loss payables need to make sure that their interest is correctly reflected on the policy.

Here are a couple of other illustrations of the operation of loss payable clauses.

- * Tornado Bowling Alley, LLC ("TBA"), secured a loan from Johnson Bank. The bank granted the note for the loan without securing an interest in any of TBA's property. This loan is similar to commercial paper. The loan is based upon the good reputation of the person or firm that is borrowing the money. Due to the nature of the transaction, TBA's insurance contract showed Johnson Bank as a "loss payee".

A windstorm totally destroyed TBA's bowling alley including the roof, automatic pinsetters and all thirty-two of the finely polished oak lanes. TBA chose to rebuild as soon as possible. During the process of planning the rebuilding, it became obvious that TBA did not have enough insurance. TBA wanted all of the insurance proceeds and did not want its insurer to give any money to the bank.

The insurer could not ignore a loss payable on its insurance contract and issued a draft that included the names of both TBA and Johnson Bank. Angry that it could not think of a way to avoid paying out on the claim, the insurer did not allocate the amount of the losses to each party. It was up to TBA and Johnson Bank to decide how much each would receive. Had it been described as a lender loss payee, Johnson Bank's claim would be first in payment preference.

- * Torches, Ltd. owned a building and business personal property. It borrowed money from a lender, which was named as a loss payee on Torches' insurance contract. Torches suffered a severe fire loss. The insurance company's special unit investigator ("SIU investigator") conducted an investigation and concluded that the loss was caused by arson and that the owners of Torches had started the fire. (The SIU investigator's compensation structure by

the way, is such that the great majority of his salary is based on how many claims he can have denied in a given year).

Unsurprisingly, Torches' insurer declined to make any payment for the loss. The lender also presented a claim for its interest, but the insurer denied the claim. The insurance company contended that the lender's recovery right as a "loss payee" was no better than that of the insured. The lender did not choose to hire an attorney skilled in suing insurance companies and had to eat its loss.

Lenders Loss Payable

This category of loss payables deals with creditors, mortgage holders or trustees. An insurer will pay these insurable interests even though no money is owed to the named insured.

- * Fast Eddie's Machine Tool Company ("Fast Eddie's") obtaining financing from Smart Finance Company for a new drill press. Fast Eddie's suffers a fire loss. Based on various alleged 'red flags' such as personally hand delivering its sworn proof of loss to the insurance agent, the insurance company's SIU investigator concluded that the president of Fast Eddie's committed arson. As a result, Skinflint Insurance Company declined to honor Fast Eddie's claim. However, Skinflint Insurance Company after much prodding from Smart Financing Co.'s attorneys decides to honor Smart's claim as a "lender loss payee".

When Skinflint Insurance Company makes payment to Smart Finance Co., the insurance company acquires the bank's rights against Fast Eddie. This means that Skinflint Insurance Company can sue Fast Eddie's to get back the monies it paid out to Smart Finance Co. Fast Eddie also will likely need a good attorney.

Summary

In any secured finance scenario, the prudent mortgagee must ensure that the collateral pledged as security for the loan is protected against potential loss. This is advisable whether the collateral is comprised of real estate, equipment, inventory or another form of asset. In order to protect such collateral against losses due to fire, flood or other casualty, the mortgagee should make sure that its borrower provided adequate evidence that the collateral is appropriately insured against loss. Obtaining a certificate of insurance, however, is not the end of the game. The mortgagee should also require the insurance policy to be modified so that it also protects the mortgagee through a policy endorsement which describes the mortgagee's interest in the collateral as that of a "lender loss payee". A mortgagee must ensure at the outset that such endorsements are correct and valid. Otherwise, the mortgagee may not obtain the benefit of the policy in the event of a loss.

The designation "lender loss payee" is distinguishable from "loss payee" in that a lender loss payee is deemed to have separate contractual rights of recovery under the insurance contract independent of the rights of the insured, whereas if the mortgagee is named as "loss payee," their right of recovery will be conditioned upon, or subject to, the actions of the insured. Thus, if the insurance company's investigation concludes that insured had engaged in conduct that would negate the benefits afforded by the policy and thus release the insurer from its obligation to pay the insured under the policy, the mortgagee, if properly identified as "lender loss payee," should still recover under the policy, regardless of the insured's purported misconduct. In contrast, the mortgagee identified merely as "loss payee" will be subject to the same coverage defenses and exceptions applicable to the insured. Thus if the insurance company assert that the insured committed arson, the mortgagee still has a right of recovery regardless of the insured's alleged conduct. In contrast, if they have a "loss payee," the mortgagee will have to fight hard to recover.

To best ensure itself when lending money to its customer a mortgagee should do the following:

- Obtain a **certificate of insurance** which identifies the mortgagee as a "lender lost payee on its customer's anticipated insurance policy;
- Confirm this status in writing with its customer's insurance agent (put's the agent on the hook for possible liability if the agent forgets to do so);
- Obtain a copy its customer's insurance policy to see that it is, in fact, listed and identified on that policy as a lender loss payee;
- On the policy's subsequent renewal dates so long as the customer's loan is outstanding, confirm with the insurance agent and insurance company that the mortgagee's interest as lender loss payee remains on the policy; and
- In the event of a loss under the policy; keep a close watch on the insurance company's adjustor to make sure that the mortgagee's interest is paramount to that of its customer, the named insured under the policy.

When dealing with an insurable interest, the mortgagee should always remember Ronald Reagan's maximum about dealing with the now defunct Soviet Union: "Trust but verify."