The Holding of Foreclosed Real Properties by Insurers

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In the United States, insurance companies have become active lenders in the financing of commercial real estate (CRE). For example, MetLife and Pacific Life Insurance Company provided a 12-year, $500 million mortgage to a joint venture of SL Green and the New York State Teachers Retirement System (NYSTRS) for the 1.4-million-square-foot, Class A office tower at 919 Third Avenue, New York City. MetLife also provided a 10-year, $372 million, fixed-rate loan for the 1.8-million-square-foot office building at 1285 Avenue of the Americas, also in New York City, commonly known as the UBS Building. In Q4 2016, AIG issued between $600 million and $700 million in commercial real estate loans in New York City, giving it a market share of 4%. It was a top 10 New York City commercial real estate lender in 2015. According to the U.S. Mortgage Bankers Association (MBA), as of March 31, 2012, the life insurance industry (in the U.S.) owned approximately 13% of the $2.4 trillion in outstanding commercial mortgage loans.

Life insurers have a variety of reasons for investing in commercial mortgage loans for three primary reasons: (1) to increase the level of asset type diversification in their investment portfolio; (2) to match long-term assets with long-term liabilities, because commercial mortgage loans are generally long-term with fixed interest rates and almost always include prepayment (call) protections; and (3) to minimize credit losses, because, based on historical experience, commercial mortgage loans have had modest realized credit losses.

Indeed, other than banks, real estate financing has been provided by insurance companies. Many insurers are active in mortgage lending operations. This has been a practice since the start of the 20th century.

In the Philippines, one of the investment opportunities for life insurance companies is by lending or extending loans provided that ample security is given by the borrower (Section 204, 2nd par., Amended Insurance Code). Among the acceptable securities may either be a first mortgage on real properties or condominium units (Sec. 204, par. 2, a), first mortgage on agricultural lands (Sec. 204, par. 2, b), or purchase money mortgages, lease purchase agreements or similar securities (Sec. 204, par. 2, c).

These loans and real estate mortgages are subject to some conditions under the Insurance Code. For example, for loans secured by non-agricultural real estate, the loan amount shall not exceed 70% of the appraised value of the land. For loans secured by agricultural land, the loans cannot exceed 40% of the market value of the land. In both instances, the loan shall not have a maturity period beyond twenty-five years (Sec. 204, par. 3, 1). Moreover, no loans shall be allowed for mortgages on improved real estate if the improvements (i.e. buildings) do not belong to the owner of the land, and the owner of the improvements does not sign the deed of mortgages, unless otherwise approved by the Insurance Commissioner (Sec. 204, par.3, 2). With respect to lease-agreements or similar securities received on the sale of real estate property, the loans shall not exceed 100% of the selling price of said property, or 100% of its market value at the time of its disposition, whichever amount is lower (Sec. 204, par 3, 3).

More importantly, no loan secured by real estate shall be allowed unless the title to such real estate shall have first been registered according to law, and the lien or interest of the insurance company as mortgagee has been registered (Sec. 205). Nonetheless, acquiring high-quality mortgages is an underwriting activity left to the judgement of the insurer. Poor underwriting can lead to inflated valuations of the properties.

Upon default of the borrower, such real estate duly mortgaged may then be foreclosed. Under Section 206 (a) of the Insurance Code, the insurance company is allowed to purchase, hold, own and convey such real estate property mortgaged to it by reason of the money loaned. The only condition under the law is that such real property shall be sold by the company within 20 years after the title thereto has been vested in it. Such real properties now held by the insurance company are not subject to the limitations imposed on real properties acquired as investments. Specifically, they are not subject to the 20% of net worth limitation.

In terms of valuation of these foreclosed real properties, Section 214 (e) provides that "real estate acquired by foreclosure or by deed in lieu thereof, in the absence of a recent appraisal deemed by the Commissioner to be reliable, shall not be valued at an amount greater than the unpaid principal of the defaulted loan at the date of such foreclosure or deed, together with any taxes and expenses paid or incurred by such insurer at such time in connection with such acquisition."

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