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## Distressed Real Estate: Can Possible Tax Advantages Be As Simple As ABC?

Arnstein & Lehr, LLP, Chicago  
by James A. Chatz, William A. Brandt, Jr. & Catherine E. Vance

What the tempting simplicity of the above title refers to is the possible tax advantages that could be engendered for builders and developers through the use of an “ABC,” otherwise known as an Assignment for the Benefit of Creditors. An ABC is one of those arcane vehicles employed by professionals in the world of restructuring, and it’s just another means of arranging for the disposition of a troubled entity’s assets.

For many real estate developers and home builders, an ABC, because of the potential tax advantages to be garnered, might well be the most recommended course of action during these difficult economic times. Since builders and developers may well benefit from the distinct tax advantage available through the ABC process, as compared to other alternatives such as bankruptcy or, worse, foreclosure, more than a little thought ought to go into weighing these differing solutions when hard times are encountered. Basically, through the employment of the vehicle of an ABC, builders and developers may be able to make use of their current corporate tax loss carrybacks now, instead of waiting for another disposition of their property, such as through sale or

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foreclosure. Moreover, the so-called stimulus bill recently signed into law would expand the ability of entities to use loss carrybacks from the current two-year limitation to a full five years. For qualifying builders and developers this means that current losses could be used to offset income that was earned in the recent heady days of a stronger economy, when real property sales and related values were at or near their peak.

### **What is an ABC?**

An Assignment for the Benefit of Creditors, or ABC, is one of several possibilities that can be employed in arranging for the disposition of a troubled company's assets. The company (or Assignor) executes an agreement to transfer all of its property to a neutral third party (the "Assignee") who is, by definition, independent and disinterested, and willing to undertake the role of acting as a fiduciary for all of the business's creditors. The Assignment itself is accomplished by way of a written contract and has the effect of deeding and conveying all of the assets of the company to the neutral third-party fiduciary who serves as Assignee. The Assignee's obligation thereafter is to timely liquidate all of the assets so received for the benefit of the company's creditors, and to pay over the proceeds derived from this liquidation to the various classes of creditors in accordance with the priorities dictated by law in these matters. Once an ABC is undertaken, the creditors of the business may then look only to the Assignee, and the assets that were conveyed to him or her, for satisfaction of any obligations they may have arising from their business relationships with the company.

Because Assignments are governed by state law, there is a good deal of variance from state to state regarding the specifics of the Assignment. In some states, for example, an ABC is a court-supervised procedure, while in others the Assignee administers the Assignment estate within the bounds of the state's laws but without judicial oversight.

Unlike what occurs in a bankruptcy, there is no discharge of the company's debts in an ABC, but as Geoff Berman (a colleague at DSI) points out in his handbook on ABCs, that is the practical effect. He writes, "A general assignment 'stops' creditors from pursuing the debtor (i.e., the company) through

collection lawsuits” and “when the various individual aspects of state laws are brought into effect upon the making and acceptance of the general assignment, the practical effect is that creditor actions become ineffective.”<sup>[1]</sup>

### **What are the pros and cons of an ABC?**

The good news is that ABCs are customarily much faster, far more efficient and certainly less expensive than a bankruptcy proceeding. Moreover, they often avoid the difficult impact on related businesses that foreclosures may often have. Most companies wisely choose to assign the assets to an experienced professional for whom managing the Assignment is a normal part of his or her business (including, yes, the authors of this very article). It’s widely recognized that the careful selection of professionals involved in an ABC will not only lead to a more efficient and less costly administration of the Assignment, but will also measurably help ensure that the Assignee is disinterested and neutral, thus fostering confidence among the creditor body that the matter is being handled with the appropriate commercial integrity. Absent disinterestedness, creditors could suspect either potential wrongdoing or illicit motives, with the result that they could force the company into involuntary bankruptcy as well as, possibly, bringing suit against the company and its management.

On the other hand, it’s absolutely true that an Assignment will never be the appropriate vehicle if what the company’s owners and management are looking to do is to restructure the business and continue its operations into the future. Remember, an Assignment fully divests the company, on an irrevocable basis, of all of its ownership interests in its assets, including the proceeds derived from their liquidation. Therefore, if reorganization of the enterprise is truly the goal, then a

Chapter 11 Reorganization or, if the parties are amenable, a private workout or composition arrangement would be a far better choice as to a course of action under those circumstances.

### **What about that “distinct tax advantage” mentioned above?**

As mentioned earlier in this article, it’s our belief that developers and builders may be able to preserve, via the vehicle of an ABC, their ability to carry back

losses on real property they part with in conjunction with the conveyance of assets in an Assignment. Some recent articles on the subject have suggested that an ABC can be used for the purpose of accelerating losses such that recognition of those losses comes within an adequate timeframe sufficient to carry it back to the prior tax year, or even earlier tax years, if permitted. [\[2\]](#)

For the purposes of this essay, remember that tax losses may be recognized when real property is deemed “abandoned” as that term is defined for tax purposes, and that an ABC can certainly be the appropriate vehicle and means to effectuate such an abandonment. For example, an abandonment requires that the property’s owner express an intent to abandon the property as well as perform some affirmative act that evidences the intent to abandon and relinquish all rights in the property, including any residual benefits.

In an Assignment for the Benefit of Creditors, the intent and relinquishment requirements can be managed through the language of the Assignment itself, as an ABC you’ll recall is based on a written contract. The affirmative act comes upon the execution of the Assignment when the Assignee takes possession and control of all of the assets including any real estate. Therefore, loss on the property may be recognized when the Assignment takes place and without regard to when the Assignee ultimately actually sells or otherwise disposes of the property.

With respect to any effort that allows a property owner to quickly access the benefit of any loss carryback provisions, not only does an ABC minimize the delays in the resolution of a property’s disposition, as can be encountered in other alternative proceedings like bankruptcy or foreclosure, but it may even be better, from a timing standpoint, than what can happen when one tries to wait out the hoped-for straight sale of a property. It is the rapid disposition of the property, for tax purposes, that can be achieved through the execution of an Assignment that can make all the difference for developers and builders who are trying to realize value from otherwise troubled assets.

### **Conclusion**

As is always the case, and especially where

complicated tax issues are the subject of discussion, this article really just scratches the surface of Assignments for the Benefit of Creditors and why the use of an ABC might be the right choice for either a real estate developer or a homebuilder burdened with property which they are unable to unload given the current economic conditions. Naturally, anyone considering this course of action should consult with his or her professionals to learn more about the ins and outs of the ABC process, as well as to ensure that the language of any Assignment contract will incorporate the purpose and intent of the ABC along the lines discussed within this article.

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[1] Geoffrey L. Berman, *General Assignments for the Benefit of Creditors: A Practical Guide* 2d ed., American Bankruptcy Institute 2006.

[2] See, e.g., Thomas O. Wells and Joseph R. Schortz, *Accelerating Losses with an Assignment for the Benefit of Creditors*, *The Florida Bar Journal*, November 2008.

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Attorney Jimmy Chatz is a partner in the Chicago office of Arnstein & Lehr LLP. He has substantial experience in the field of commercial insolvency and creditors' rights law, representing clients throughout the United States. He also practices in the areas of corporate law and business law, mergers and acquisitions, financial planning, and commercial litigation. Mr. Chatz spends a significant portion of his time in South Florida with the law firm's Boca Raton, Fort Lauderdale, Miami, Tampa, and West Palm Beach offices, providing his knowledge and experience as a resource to businesses and individuals with significant interests in South Florida.

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Bill Brandt has been in the business of workout, turnaround and insolvency consulting for more than thirty years and is widely recognized as one of the foremost practitioners in the field. He is President and CEO of Development Specialists, Inc. (DSI), a firm specializing in the provision of management, consulting and turnaround assistance to troubled or reorganizing enterprises. The firm maintains offices in Chicago, New York, Los Angeles, London, Miami, San Francisco, Cleveland, Columbus and Boston.

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