Northwest Arkansas Developers, Banks Spar Over Deals Gone Bad

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SPRINGDALE — Everyone got along during the Northwest Arkansas land rush from 2000 to 2005. Banks, many new to the area, competed for the chance to loan money to developers. Developers, many jugging several large projects at once, scooped up the loans and kept building at breakneck pace.

Now area developers are suing banks for lack of funding, while bankers foreclose and write off more delinquent real estate debt with each passing quarter.

Sean Morris, general contractor for ARC Construction and Development in Centerton, said the lot bonanza got firmly out of control as land prices escalated to their 2005 peak.

“Developers forgot the word ‘phase’ and began cutting up area pastures into subdivisions by the hundreds of lots, instead of smaller, more manageable size chunks,” Morris said.

He said the market overheated in 2005 and land prices went out of control, but somehow developers still got loans.

Case in point: Fayetteville developer Gary Combs recently settled a lawsuit with Bank of the Ozarks in which the bank took back 510 residential lots in Prairie Grove as well as 185 lots, a clubhouse and commercial track in Goshen. The bank wrote off $10.5 million related to the properties’ declining values.

The high profile settlement has since spawned other legal complaints by developers aimed at lenders in hopes of a similar outcome, insiders said.

The loans to Combs were made in the summer 2005 at a time when land prices hit their peak, said Kathy Deck, director for the Center for Business and Economic Research at the University of Arkansas.

Morris said builders flocked to outlying areas such as Centerton, Elkins and Prairie Grove as land prices along the Interstate 540 corridor got out of reach for affordable housing.

In May, the Skyline Report commissioned by Arvest Bank indicated there were 8,615 residential lots approved in Northwest Arkansas. The area’s lot inventory is sufficient for the next 10 years, according to the Center for Business and Economic Research, whose researchers compiled the report.

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Streetsmart Data Services of Fayetteville recently estimated the available lot supply for new housing to be about five years’ worth, when discounting a few projects that never were viable because of location or pricing.

Deck agreed some developers and bankers believed the market was infallible in 2005, assuming strong employment growth would continue at a record pace and fuel the need for more housing.

By the time the excess lot inventory peaked in the fall 2006, the region’s job growth began to decline, she said. And by mid-2007, Deck said the banking community began to pull back lending, leaving over-leveraged developers in a lurch.

Warnings Overlooked

Arvest Bank contracted with the University of Arkansas to publish a Skyline Report, to track construction, absorption and real estate prices in Benton and Washington counties, said Rob Brothers, president of Arvest Bank in Rogers.

The first Skyline Report was released for the second quarter 2004. The reports showed building activity was robust at a time when population and job growth kept pace, but after a year or two, the Skyline Reports also showed building activity remained robust as job and population growth began to wane.

By 2005, Buddy Adcock, state bank commissioner, warned in the competitive climate, banks eager to make loans must not do so at the expense of thorough underwriting standards. Economist Jeff Collins said in 2005 the region’s burgeoning banking sector likely would take on more risks in their eagerness to acquire new loans.

Banking analysts agree the hyper-competitive lending climate among Northwest Arkansas banks fueled much of the excess development the region faces today in both the commercial and residential sectors. Deck said there is not one commercial building sector in this region that doesn’t face increasing vacancy rates including retail, multifamily, warehouse and office space.

Now the business of lending and developing has moved from the boardroom to the courtroom as bankers and developers fight over projects never finished because of a lack of lender funding, lack of borrower payment or both.

Barber's Blunders

Brandon Barber jumped into the real estate market with both feet by age 27. Barber said he committed the sin of gluttony with respect to an insatiable appetite for the next deal.

"We just had too many projects going at once, and there was no shortage of banks wanting to provide the financing," Barber said Tuesday.

Two of his high profile projects announced in 2005 did not work out as planned.

Barber and former partner Seth Kaffka unveiled an upscale condominium project near Dickson Street in downtown Fayetteville — The Legacy Building — in 2005.

The concept of modern living in a quaint, historic downtown area was attractive and rich with possibilities, so the $18.7 million project got under way. Legacy National Bank partnered with Metropolitan National, First National Bank of Green Forest and First National Bank of Fort Smith to provide financing.

Barber also was juggling a large mixed-used office and condo space near the Northwest Arkansas Mall known as Bellafont. The price tag was an estimated $250 million, Barber said in March 2005.

The complete Bellafont complex was never built, but the first phase of the retail segment got under way in late 2005. Barber said at the time out-of-state banks provided the lending.

By early 2007, financial troubles were brewing on both projects. Contractors began suing Barber for nonpayment, filing claims against both projects and prompting Barber's lenders to proceed with foreclosure. Lenders got the Legacy Building back via foreclosure in summer 2008 after a nasty legal entanglement, court appointed receivership and eventual bankruptcy filing by Barber's shell company, Lynnkohn LLC.

Barber said in bankruptcy court last October he worked out about $100 million in real estate loans with other banks who were willing to cooperate. He said many of them "took a hit," but did get most of their principal back even in this difficult market.

The bank-owned Legacy Building condominiums now are listed for sale by Lindsey & Associates. The list price averages $350 per square foot, according to the Multiple Listing Service database. Eight of 37 condos have been sold.

Barber said financing for buyers to acquire the high-end luxury condos began to dry up before the project was finished. He said in retrospect the demographics in this area don't really support the lofty price tag and the vision he had for the project.

"If I could go back, I would likely just focus on one large project — like Bellafont," Barber said.

The Bellafont property is still in a prime location and it will go back to Clayton, Mo., lender Enterprise Bank & Trust with his recent Chapter 7 bankruptcy filing. Barber believes someone will eventually make some money on its development.

Mason Hiba, owner of Mason's Boutique, paid Barber more than $1.89 million to purchase the land and construct a retail building in Bellafont that was to be finished in October 2006. Hiba sued Barber a year later after contractors filed liens against his property for nonpayment.

Hiba finally opened Mason's Boutique in August 2007, 16 months after the promised date of completion, according to Hiba.

Another retail tenant, East Meets West Spa owner Helena Gadison, took her business elsewhere when Barber could not finish the space in a timely manner.

As of May, Brandon Barber was party to 27 civil cases in Washington County, including nine foreclosure suits and four foreign judgments filed by creditors in other jurisdictions. On July 31, he filed Chapter 7 bankruptcy listing debts of more than $47.79 million.

Barber said the past two years have been a humbling experience, but he is looking forward to the next chapter of his life. Deal brokering is what he loves to do and will likely always be part of his life whether it's in real estate or widgets.

"I am fortunate to have some good friends, family and former business associates sticking by me as I work through these financial difficulties," he said.

For the time being he is working with some lenders and former partners to structure loan workouts and move nonperforming assets into the hands of a few buyers.

"There are no shortage of developers who need to move property to satisfy lenders," he said.

Terminella's Trials

At the market's height in late 2005, Tom Terminella said he had five major community developments in the pipeline on a 6- to 12-year timetable for total buildout and occupancy.

He said because of the projects' sizes and the full disclosure he made to lenders, the banks knew it would take him several years to complete the projects, "unlike other opportunists and risk takers that were out there."

"I had more than $221 million in real estate assets and put up as much as 30 percent of my own cash equity as collateral in the deals. But, even then, I was too overleveraged," Terminella said Wednesday.

In a 2006 interview with the Arkansas Times, Terminella said he knew the party was over. There were a lot of people who jumped on the development bandwagon, he said, "every hairdresser and fireman and plenty of bankers themselves got on board."

He blames the banks for the majority of his financial losses in recent years.

"When banks changed the rules in the middle of game, demanding more collateral as land prices fell, my assets were reduced from millions, to a home and 2 acres almost overnight," Terminella said.

He waged a public war against Metropolitan National Bank when the lender foreclosed on his Grand Valley Ridge residential development in east Springdale in May 2007. The original foreclosure filing indicated Terminella defaulted on a $9.63 million development loan made to him in September 2005.

A countersuit filed by Terminella alleged the bank breached its contract and failed to complete the funding of Grand Valley Ridge —101 residential lots. The suit alleges the bank's own "unsafe and unsound business practices" as cited by bank regulators had cost him the ability to complete the project.

"The bottom line is Metropolitan needed cash to cover its bet in Northwest Arkansas and breached our agreement so it wouldn't have to fund the remaining $2.6 million of my loan," Terminella said in June 2007.

In February, after more than 21 months of legal limbo, Washington County Circuit Court Judge Kim Smith ruled in favor of Metropolitan National Bank. Smith ruled Terminella still owed Metropolitan National more than $7.61 million, of which Metropolitan would have judgment along with attorney's fees, court costs, plus costs incurred in collecting the debt.

A $6.89 million judgment entered in favor of Metropolitan National Bank against Terminella in February was recently upgraded to a writ of execution, which allows the sheriff to confiscate and auction personal possessions to satisfy the judgment.

Terminella said he has already conceded property back to the banks, and they took his certificates of deposits and cash balances in checking accounts.

He is working on an appeal against Metropolitan National Bank and recently filed a civil suit against CEO Lunsford Bridges alleging bribery and witness tampering with respect to the case tried in February.

Metropolitan National Bank does not discuss pending litigation, said spokesman Barry Jackson.

Bridges also declined to comment on Terminella's pending suit implicating him personally.

First State Bank has begun foreclosure action on the Grand Valley Stables development and a separate property located at 1530 Albright Road in Fayetteville. The bank was awarded judgment on the properties in the amount of $2.23 million by Circuit Court Judge Michael Mashburn on July 31.

More recently, Terminella has been trying to collect money he claims is owed to him. He filed suit against Coco Mountain Ranch LLC and S. Gene Cauley, a former business partner, in Washington County Circuit Court on Aug. 4.

Terminella is in pursuit of $1.87 million for his interest in the Mountain Ranch project located in west Fayetteville along Interstate 540, just south of the Wedington Road exit.

Terminella said if he could turn back time, he would raise and use private equity to fund real estate projects.

"That is what I am doing now, working toward raising $100 million in private capital and when the timing is right I will go shopping in the bargain basement. I will be back," he said.

He has three civil cases pending in area courts and is a party to three foreclosure filings on record.

Lehman's Losses

Carmen Lehman was one of the first area developers to see the possibilities in western Rogers near Interstate 540. She turned a low area often filled with water into 64 acres with three small lakes, fountains, courtyards and suites or stand-alone office buildings.

Lehman, owner of C.R. Lehman Properties started that project in 1993 and has been in the Northwest Arkansas real estate market since 1969.

Village on the Creeks now competes for retail space with Pinnacle Hills Promenade, across the interstate; Shoppes at Pinnacle Hills, just down the road near Embassy Suites; with Scottsdale Center, just a mile north; and with office space scattered throughout Bentonville and Rogers.

Retailers such as Mason's, which used to have a shop in Village on the Creeks, left. Mason's owner Hiba said in January that Lehman raised his rent 1.5 times the previous rate.

Lehman Properties voluntarily filed Chapter 11 bankruptcy Feb. 13. Ownership of Village on the Creeks was transferred to a designee of Arvest Bank, according to Lehman's bankruptcy attorney, Stanley Bond.

"It's the economy, I don't think any of us could have predicted what was going to happen. We have this competitive market out there and developing is a risk," Lehman said Thursday. "There were good times, and now we are in the bad times, and that is just part of life. Nothing is good all the time."

Lehman Properties owed $27.3 million in loans and listed estimated assets at $0 to $50,000 in the bankruptcy filing.

Arvest Bank was the main lender, with 76 percent of the Lehman Properties loan. Metropolitan National Bank had 17 percent and First State Bank of Russellville had 7 percent, according to Brothers of Arvest Bank.

Lehman failed to pay 2007 real estate taxes, a Dec. 20 loan payment and a Jan. 20 loan payment, according to Arvest Bank.

"As the case progressed, it became clear that Arvest wanted the property," Bond said, and not money. The negotiation surrounding Village on the Creeks in the bankruptcy case were "heated" and lasted for more than 90 days, Bond said.

"Arvest is satisfied. The creditors are satisfied," Bond said.

In the meantime, the bank will try to generate income from the property to pay loans.

"We think that this project is a good project. It is well located, it is quality built," Brothers said. Arvest has a branch at Village on the Creeks, but Arvest owns that building and did not lease it from Lehman Properties, Brothers said.

"If you use the benefit of hindsight, would you have still made that loan on Village on the Creeks, the answer is obviously 'no.' We obviously want to make loans on which we can collect," Brothers said.

However, there was nothing wrong with the Village on the Creeks loan at the time.

“If we said ‘no,’ then someone else would say ‘yes,’” he said, noting the number of new banks that had entered the market.

“You can’t blame banks wanting to be represented in the Northwest Arkansas economy,” Brothers said.

Some overbuilding issues in the two-county area were what Brothers termed “self-inflicted supply side problems,” with builders constructing space without thinking about whether there was a demand.

Lehman agreed many builders, including those new to the market, built offices and retail space to take advantage of rapidly escalating prices.

However, she said bankers are not blameless.

“Everybody has to accept some responsibility in all of it. I accept my responsibility,” she said.

She still works at Village on the Creeks, however, it’s from the Century 21 Exclamation Realty office, where Lehman said she is selling commercial and residential properties.

“I don’t know what the future holds. I’m happy to wake up every day and have an office to go to and people to be around. I am thankful for good health, lots of friends and my faith,” Lehman said.

Combs In Court

Gary Combs faces several lawsuits related to unfinished projects. Combs, in turn, is suing banks, including Metropolitan National Bank and First Federal Bank, claiming the banks made promises to lend him money at certain rates for certain periods of time, then demanded new appraisals on those properties and devalued them.

Combs and Bank of the Ozarks settled their complaint over the Prairie Grove and Goshen properties in July, with Combs relinquishing Waterford Estates in Goshen and a large residential subdivision in Prairie Grove to the lender.

Bank CEO George Gleason told shareholders the bank did not seek judgment against Combs and took back the property to move forward with its sale, devoid of future litigation.

The Bank of Fayetteville sued Combs, whose holdings include Basic Construction and Basic Block Group, in early July. The suit, filed in Benton County Circuit Court, states Combs hasn’t repaid a nearly $2 million mortgage on land that was to be a truck stop. The suit names as defendants Wagon Wheel Development LLC, Combs, Chambers Bank of North Arkansas and Benton County Collector Greg Hoggatt.

The suit states Combs on Sept. 5, 2006, promised to pay Bank of Fayetteville $1.95 million with 8.38 percent interest. Combs put as collateral 23 acres in Benton County along Wagon Wheel Road, according to the suit.

Combs refinanced the loan on Sept. 19, 2008, but hasn’t made required monthly payments.

Bank of Fayetteville has asked the court to order Combs to pay the amount due or to sell the land to satisfy the debt.

Combs in June sued First Federal Bank of Harrison after Combs became part of the bank’s efforts to satisfy some loans made to Barber. Barber approached Combs in May or June 2008 and asked Combs to buy property to help clear bad loans off First Federal’s books, according to the suit. Barber negotiated the sale of some property, the location of which wasn’t specified in the suit, to Pinnacle Hotels Group LLC.

Ross Mallioux, president of the Northwest Arkansas division of First Federal, told Combs the bank would fund a development project on the land. Combs bought the property on June 19, 2008, for $2.22 million and got a First Federal loan for $2.33 million, according to the lawsuit. However, First Federal solicited buyers for the property in May of this year when it had no authority to do so, according to the suit.

Combs bought a second piece of property after Barber approached him in September 2008. Mallioux helped Combs negotiate that property purchase and First Federal agreed to finance a building project related to the purchase, according to the suit. Combs bought the property, the Executive Plaza in Springdale, on Oct. 7, 2008.

Combs and his companies finished construction of an Executive Plaza building and began preparing plans for a second building, according to the lawsuit. However, First Federal wanted a second appraisal of the project. Combs and his companies submitted a new loan request in March this year.

Combs spent more than $1 million on the office project but halted construction after First Federal declined to fund it, according to the suit. Combs and his companies claim First Federal breached contracts, acted in bad faith and committed fraud. Combs asked the court to award $10 million in damages; punitive and other damages; and more than $6 million in profit he would have made from the projects.

Combs also suing Metropolitan National Bank for $45 million. The suit, filed June 30 in Benton County Circuit Court, alleges the bank approached Combs and convinced him to refinance with Metropolitan a loan for the Diesel Downs subdivision in Springdale that had been held at Bank of the Ozarks.

Combs refinanced the loan at $13.75 million.

In May and June 2008, Combs asked for a second loan of $8.2 million for Diesel Downs, according to the suit. In June 2008, Larry Olson, Metropolitan’s Washington County president, told Combs the bank wouldn’t honor the loan agreement, according to the suit. Combs alleges fraud and breach of contract and seeks $45 million in damages and a jury trial.

Metropolitan in its filed answer to the lawsuit denies loan officers recruited Combs, but acknowledged the bank financed Diesel Downs, according to court documents. Metropolitan filed a motion to dismiss Combs’ fraud complaint and countersued to foreclose on his property.

Combs has three pending law suits against former lenders totaling $80.5 million in alleged damages, according to his attorney, David Fisher. He also is a party to other civil lawsuits, Fisher said.

Instead of suing banks and being sued, Combs said he could have walked away from the Northwest Arkansas market with about $60 million in 2002 and 2003.

Now, though, “all I want is my day in court, or my money back” from the banks, he said.

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Mith242 wrote on *Aug 16, 2009 7:14 AM:*

" Very good article. I haven't seen so much info on so many developers covered in a single article. "

ifartedandblamedthedog wrote on *Aug 16, 2009 8:30 AM:*

" It's from the Morning News... I'm willing to bet only 5-10% of this article is accurate. It's just another sensationalised article brought to you by the Morning News. "

BCR wrote on *Aug 16, 2009 9:22 AM:*

" Amazing how hindsight is perfect 20-20 vision... I'm not even remotely involved with banking, or real estate, but I read the Skyline reports and SAW the out of control growth, the high vacancy percentage of unsold homes, and vacant commercial property (which is still a big number, and going to get bigger). Why didn't the banks read their own data? "

lifer66 wrote on *Aug 16, 2009 12:29 PM:*

" BCR is absolutely correct. It's amazing just how myopic the bankers and developers were when everyone with half a brain could tell that $$$$ ruled the day, not common sense. It really makes you realize that our so-called local government and business leaders are nothing more than common, money-grubbing fools. "

Lone Star wrote on *Aug 16, 2009 12:53 PM:*

" No drug, not even alcohol, causes the fundamental ills of society. If we're looking for the source of our troubles, we shouldn't test people for drugs, we should test them for stupidity, ignorance, GREED and love of power. "

BCR wrote on *Aug 16, 2009 7:40 PM:*

" From the first skyline report published in 2004, the news was not good. commercial occupancy rates that were high, and getting higher, new homes and resale homes on the market in quantities to last years, not months. Why it took until 2004 to track and publish the numbers is beyond me, but it did. Maybe now, these carpetbagger real estate developers will go to Boulder, or Little Rock, or North Dakota where the growth was not so robust... "

lerret wrote on *Aug 16, 2009 9:14 PM:*

" excellent article and 'right on'...

I watched it play out as an appraiser and refused to rubber stamp a lot of these lost cause subdivisions.

The one missing element is that the counties and cities should burden some of the blame. For instance, Gentry approved over 1000 lots in one year, which would have literally doubled the size of the town. This had consequences. A remote development of several hundred lots forced SWEPCO to buy the 80 ac parcel out to prevent future problems with potential complaints from homeowners over coal ash. The paid way too much for the land and electric rate payers ultimately get the bill to make the Mathias's even more filthy rich. "