Bubble boy: Verrone's securitization deals helped inflate the commercial real estate market

The Ballad of “Large Loan” Verrone

By Devin Leonard
Photograph by Michael Edwards

During the boom, Wachovia banker Robert Verrone made money by slicing and dicing billions of dollars in commercial real estate loans. After the crash, he made money by restructuring those loans before they blew up. What has he learned?

Robert Verrone is standing on the roof of an office building in midtown Manhattan. In his hand is a list of commercial properties, almost all of which he financed through securitization, the now-infamous process through which debt is minced and extruded into bonds that can be bought and sold by Wall Street traders. During the real estate boom, Verrone was head of Wachovia Bank's large loan group, and on this August afternoon he has come up to the roof to point out some of his biggest deals.

“I'm not sure where I should start,” he says. He walks over to the east side of the building. “How about that one?” Verrone points to a lovely glass tower just across the street—650 Madison Avenue—for which he arranged a $100 million second mortgage two years ago. He gestures through the forest of skyscrapers to a boxy one on Park Avenue. That was his, too. Wachovia wrote the building's $430 million mortgage in 2006.

Verrone, 42, looks and sounds like a thinner James Gandolfini, so when he gets revved up on the roof, it's as if Tony Soprano himself were holding forth, smiling and waving a hand toward the high-end residential district just east of Central Park. “We made deals all through that corridor,” he says. “I don't know how many.” He gestures toward Central Park South. “We did the land under the Ritz-Carlton.” He cranes his neck to look around the corner, down Fifth Avenue, but can't quite manage it. He looks disappointed; he arranged mortgages for 11 buildings on that street alone. And then there are the boutique hotels he did like the Royalton in Times Square, the Wall Street tower he refinanced for Donald Trump, the warehouse in Chelsea where Martha Stewart runs her company, and on and on. “It was a great 14 years,” he says later. “I miss it every day.”

Specializing in loans of $50 million or more, Verrone helped make Wachovia the No. 1 underwriter of securitized commercial real estate debt between 2002 and 2007, with a total of $69 billion in loans during these years, according to Trepp, a New York research firm. (Verrone won't say how much he made in those days.) His prodigious run came to an end in May 2008. He resigned just months before Wachovia nearly collapsed and was acquired by Wells Fargo at the fire sale price of $15.1 billion.

Verrone can't be blamed for Wachovia's near-death. The bank was probably doomed at the peak of the housing market in 2006 when it paid $24 billion for Golden West, a prolific subprime mortgage dispenser. Still, his department's losses were substantial. In 2007 and 2008, according to Foresight Analytics, Wachovia wrote off $771 million in bad commercial real estate loans; Bank of America and Citigroup by comparison, wrote off $565.8 million and $457 million, respectively. In terms of total dollar amounts of delinquent securitized loans today, Wachovia leads the parade with $5.81 billion.

By his own admission, Verrone's methods helped inflate the real estate bubble. He says he lent huge sums to developers such as Harry Macklowe and Jerry Speyer—sometimes via interest-only deals with little money down—so they could buy skyscrapers. Then he carved up the debt, bundling the safest pieces into multibillion-dollar pools and selling them on the bond market. The riskier portions he offered to hedge funds hungry for higher returns. For Wachovia, the beauty of these deals was that the debt vanished from its books, but not before the bank slurped up juicy fees.

"Large Loan" Verrone, as he was known, became an outsize figure in the New York real estate world: the blustery guy who quoted *The Godfather* during client meetings and threw parties on the rooftop of the Philippe Starck-designed Hudson Hotel. Verrone insists that the image has been exaggerated, though not by much. "Did I use a *Godfather* quote? I don't know any 42-year-old male that hasn't," he says. "But I never sat at the table quoting *The Godfather* while we were trying to work out a deal. That's ridiculous. Look, I'm just a guy who works really, really hard."

You might think Verrone is just another unsavory character from the boom years, the real estate equivalent of those bugs you see when you turn over a big rock. Don't be so sure. For years, before everything got out of hand, bankers like him provided an important service: They made capital available to developers and spread the risk rather than keeping it on their institution's balance sheets, which had a disastrous effect during the savings and loan crisis of the 1980s. The problem this time was that the Rob Verrones of the world didn't know when to stop providing. They underwrote anything rentable and thought they were immune. It was only a matter of time before the bubble burst and everyone in the business, including Verrone, got splattered.

Now Verrone is back—and this time, he says, he is part of the solution. His job these days is to help the commercial real estate market avoid the second crash predicted by economist Nouriel Roubini, among many others. The same lenders that are foreclosing on cash-strapped owners single-family homes are quietly striking deals with cash-strapped developers, extending loans and restructuring debt so the big borrowers can avoid default.

Why are Verrone's former clients now paying him to salvage the same bad deals he got them into?

Verrone, with President George W. Bush and the First Lady, in 2005

Large Loan is in the thick of these deals. In January 2009, he started a company called Iron Hound Management, which in the past year has negotiated interest reductions, extensions, and payoff discounts on $2 billion worth of loans and is currently wrestling with $4 billion more. In some cases, Verrone has been tapped by his old Wachovia clients to repair the very deals he crafted when he was the bank's big loan guy. "It's unusual," says Robert Ivanhoe, chairman of the global real estate practice at the law firm Greenberg Traurig. "I'm not saying there is anything wrong with it. But it is unusual."

Why would Verrone's former clients pay him to help salvage the same bad deals he got them into? Faced with this question, Verrone responds with something you rarely hear from Wall Street types who got rich during the boom: contrition. "I'm one of the few guys who will admit it," he says, conceding that he made some deals that look dreadful today. "The wind was at our backs. We definitely made mistakes over the years."

As he restructures loans he never should have written in the first place, Verrone says, he's learning some valuable lessons. "We need to keep it simple," he says. "We sold every penny of cash flow to anybody in the world who wanted to buy it. That makes it really tough when things start to go sideways."

He hopes to apply these lessons when the commercial real estate market recovers, as it appears to be doing slowly. According to Trepp, the market for the kind of commercial real estate bonds Verrone used to create hit an all-time high of $251 billion in 2007. Last year only $3.5 billion were issued. The firm expects that this year, however, the amount will triple as lenders such as Wells Fargo and Goldman Sachs get back in the game. In other words, it might not be long before Verrone is back on Wall Street making deals again.

The son of Italian immigrants, Verrone grew up in North Haledon, N.J., a middle-class suburb of New York. He displayed a talent for sales early on, selling Cutco knives to the parents of his soccer teammates at Don Bosco Preparatory High School. His soccer coach, Richard Zawacki, was astonished at his prowess. "I said, 'Robert, what do you know about knives?' " he recalls. "He said, 'Not much.' But by the time he finished talking, I bought two of them. So did my two assistant coaches."

At Moravian College in Bethlehem, Pa., where Verrone majored in business administration, he sold T-shirts emblazed with the slogan, "Do it Doggy Style," in honor of the college football team, the Greyhounds. He also started a student pub called the Doghouse. One of Verrone's soccer buddies had a sister who worked at Bear Stearns; Verrone used the connection to get a summer internship—and decided Wall Street was the place for him. "I liked the pace," he remembers. "I liked the people."

Bear Stearns hired Verrone as soon as he graduated from Moravian in 1990 and assigned him to the mortgage capital department. He worked with a team that bought residential loans from failed banks and securitized them for the federal Resolution Trust Corp., which sold them as bonds to many different investors. Pretty soon, banks like Bear Stearns realized they could do this themselves and turn a tidy profit. First they ran the debt on single-family homes through the securitization machine; then they worked the same magic with bigger loans on office buildings, shopping centers, and apartment buildings.

Verrone was a low-level analyst, but on his lunch hour he would cold-call developers and offer them debt. "It was amaz-

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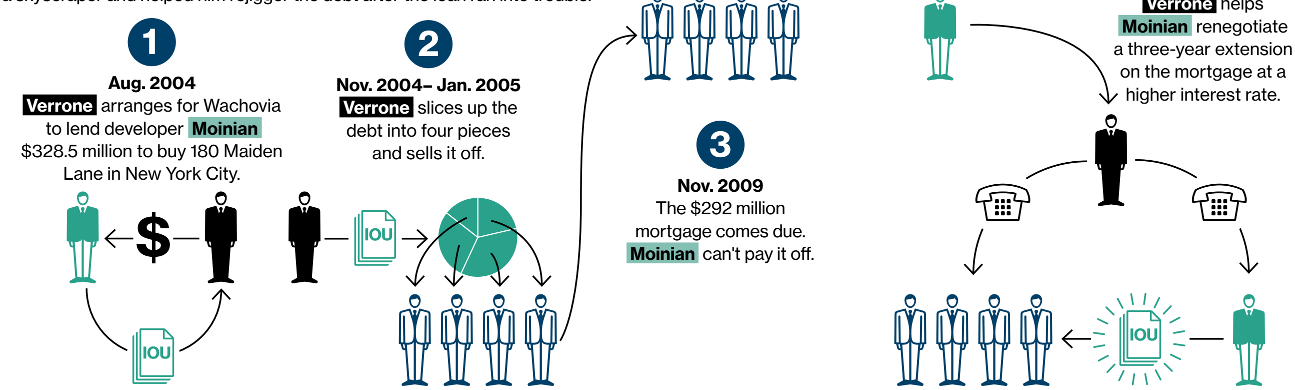
How a Verrone Deal Works

Former Wachovia banker Robert Verrone often ends up at both ends of his lending deals. In this case, he provided Joseph Moinian with $328.5 million loan to buy a skyscraper and helped him rejigger the debt after the loan ran into trouble.



ing," says Mark Finerman, a former Bear banker who worked with him. "He could just pick up the phone and bring in business. People liked talking to him." It helped that he was offering real estate people the thing they most desired: money.

The more successful Verrone became at Bear Stearns, the more frustrated he grew. He saw his competitors at Donaldson, Lufkin & Jenrette securitizing bigger and bigger loans and pocketing humongous fees. His employer wasn't so bold. "We were very conservative," he recalls. "We spent a lot of time looking at deals and talking about deals, but not closing deals."

Finally, Verrone's bosses showed him the door in 1994. He spent the summer "learning how to mountain bike the streets of New York City," he says, then he ran out of money and moved back in with his parents. That was his cue to get his MBA, so Verrone drove to North Carolina to look at Duke University. While staying with a friend in Charlotte, he had another idea. First Union, the bank headquartered there, had just hired some Wall Street hotshots, including Mike Greco, the former head of DLJ's commercial mortgage shop, to ramp up its lending. Verrone borrowed a jacket and tie from his buddy and went to interview at First Union. He landed a job.

The Jerseyite had reservations about Charlotte. As he tells it, the city had only about five bars at the time. But his sacrifice paid off. Four years later, Greco left to start his own firm and offered jobs to his old team. First Union asked Verrone to stick around, and the 28-year-old ended up in charge of the bank's lending and securitization business. Three years later, First Union merged with Wachovia (and took the latter's name). Now it had an enormous balance sheet. Verrone put it to use.

In 2003 he talked the bank into dispatching him to New York to run its large loan group, handling deals of $50 million or more. Wachovia gave him a corner office in the Seagram Building, and Verrone quickly did his first big deal. On Aug. 30, 2003, *The New York Times* ran a story announcing that Wachovia was backing developer Harry Macklowe's $1.4 billion purchase of the General Motors Building. It was the highest price ever paid for a Manhattan office building.

Just before the deal closed, Macklowe's longtime lender, Deutsche Bank, offered the mogul better terms. Wachovia lost the deal, but Verrone made his point. "We got all the press," he says. "Nobody wrote about the closing." He adds that his employer learned a lesson, too. "It made Wachovia realize that things in New York move faster than they do in Charlotte."

Verrone didn't lose many more deals. He courted developers at fancy restaurants in his own refreshing manner. "He didn't have any trouble sitting at the Four Seasons and talking about how his father was a cutter in a clothing factory," says Chad Johnson, a former Wachovia banker. "It wasn't the same bull___ you heard in business lunches. It was part circus and part business, and it led to a lot of successful transactions."

Wachovia's bashes on the Hudson Hotel's rooftop became popular events. It didn't matter that they weren't always executed flawlessly. "The first time, we threw the party on Rosh Hashanah and we didn't have kosher food," Verrone says. "One year we threw it during the World Series. The Yankees were playing. We didn't have TVs. Everybody was leaving to watch the game." What Verrone's clients remember most fondly aren't his parties or his jokes, but his willingness to show up at the closing table with sizable checks. "He never cut our loans, which some lenders are prolific at," says Jeff Ratzer, vice-president of Executive Capital, a real estate investment firm in Big Rock, Ill. "If Rob said it was $20 million, he didn't come back two months later at the closing and say it was $18 million."

As Wachovia and its rivals threw money at developers, real estate prices soared. That only seemed to whet Verrone's appetite. In 2006 he structured a $5.4 billion deal that allowed Tishman Speyer and BlackRock to acquire Stuyvesant Town-Peter Cooper Village, an 80-acre, 11,232-unit middle-class apartment complex on the East River in lower Manhattan. Tishman and BlackRock saw that 71 percent of the units were rent-controlled. That meant the residents of these units paid an average of about $1,300 a month, while the market rate for comparable rentals in the area was roughly $3,900. The new owners thought they could convert 40 percent of the rent-controlled apartments in seven years and increase the property's annual net operating income from $105 million to $397 million.

The new owners loaded up with so much debt–$2.9 billion from Wachovia, $1.4 billion from Merrill Lynch–that there was no room for error. They didn't expect the property to be cash-flow positive until 2011, according a private placement memorandum. Until then, they planned to cover interest payments–$262 million in the first year alone–from a reserve fund Verrone had arranged.

$5.4
Billion

Size of the deal Verrone structured for New York's Stuyvesant Town

The goal of flipping 40 percent of the units proved unreachable because Stuyvesant Town is no ordinary housing complex. Built in the late 1940s by

DATA: TREPP

Metropolitan Life, it was that rarest of things: an affordable middle-class enclave in Manhattan. Most residents had waited for years to get an apartment there, and after winning this lottery they weren't going anywhere without a fight. Tenants filed a lawsuit accusing Tishman Speyer and BlackRock of illegally raising rents. An appeals court ruled in their favor, effectively dooming the owners' conversion campaign. In January 2010, they defaulted on their mortgage, sending tremors though the bond market.

Verrone says he got the debt off Wachovia's books before the credit markets froze in 2007. He insists that holders of the senior \$3 billion mortgage, which had been carved up into six different bonds, will get their money back. Holders of the \$1.4 billion mezzanine debt, such as S.L. Green Realty, a real estate investment trust, won't be as lucky. They've been wiped out. "That's one of those investments we would have liked to have taken back," says Andrew Mathias, chief executive of S.L. Green. However, he adds: "We don't blame Robert for that."

As the Stuyvesant Town deal was closing in December 2006, Verrone says, he got a whiff of the coming financial crisis. His bosses were nervous about the state of the bond market, and everything was slowing down. It used to take Wachovia two days to sell a commercial real estate bond. Now it took two weeks. Verrone says he began to worry that it was just a matter of time before the bank was stuck with a heap of toxic waste.

Those worries did not prevent him from closing the \$10 billion worth of loans he had in the pipeline, among them the Lightstone Group's \$8 billion purchase of Extended Stay Hotels, which Wachovia underwrote with Bear Stearns, Merrill Lynch, and Bank of America. Verrone says he couldn't make much of this debt disappear from his employer's balance sheet. "We lost a lot of money on that," he says of the Extended Stay deal. (Last year the hotel chain filed for bankruptcy.)

Yet Verrone and his team did try to limit the damage by selling off Wachovia's remaining loans at bargain prices. "It was 'First bid, best bid,'" he says. In response, Wachovia was deluged with calls from hedge funds and private equity funds that—as Verrone tells it, at least—thought he had lost his mind. He estimates that his group unloaded \$7 billion worth of rapidly souring debt in 2007. "I had lunch with someone the other day," he chuckles. "The guy says, 'I'm still trying to work out that loan you sold me.'"

Verrone insists these efforts saved Wachovia, though even if this claim is true, the bank was still encumbered by Golden West's portfolio. In the end, the only way out was the hastily arranged wedding to Wells Fargo. By then, Verrone was gone. In March 2008, Wachovia consolidated its real estate department under Bob Reid, a conservative 30-year Wachovia veteran. Verrone resigned two months later. "I knew I wasn't going to make it under that guy," he says.

In May 2008, after less than a month of unemployment, Verrone was in Tucson, celebrating his 10th wedding anniversary with his wife at an upscale spa, when his cell phone rang. It was Elias Cababie Daniel, head of Cabi Holdings, a development company that had borrowed \$1.5 billion the previous year from Wachovia to buy 59 office buildings in Southern California. Now Cabi was having trouble paying off the debt. The developer was flying from California that night to Mexico. Could he stop in Tucson and see Verrone?

Verrone took a cab to the airport and met with Daniel in one of the hangars. Verrone says the developer pleaded with him to serve as a restructuring consultant on the deal. Ten days later, Verrone took the assignment. "I always try to help my clients," he says. "It wasn't his fault the world fell apart."

Verrone didn't succeed in getting a deal done that would enable his client to keep his buildings. He'd sliced the debt into so many pieces it was impossible to get all the holders to agree on a restructuring plan. "We tried," he says. "But there were 11 different lenders on the deal. Ten agreed. One didn't, so the borrower had to hand back the keys." Cabi Holdings has since filed a lawsuit in California against Wachovia and the other borrowers over the failed deal, claiming breach of goodwill. The developer's lawyer declined comment. Wachovia, in court documents, denies wrongdoing.

It wasn't long before Verrone, who is now divorced, was spending all his time restructuring deals like this. The securitization system that he had helped pioneer had never weathered anything like the financial collapse of 2008. Now it would be severely tested. Wachovia and its competitors had structured their bond offering so that third parties called "special servicers" stepped in when borrowers couldn't pay. Before the crash, it was a pretty easy job. Delinquency rates, after all, were less than 1 percent. Since the real estate bubble burst, delinquencies have soared to 8.5 percent this year, according to Trepp.

Even though the second crash that Roubini and others predicted hasn't come to pass, that doesn't mean there hasn't been chaos in commercial real estate. Special servicers are swamped with busted deals. "No one thought the system would implode," says Norman Radow, founder of Radco Development Solutions, a firm that manages property for banks that have foreclosed on real estate loans. "The special servicers are playing catch-up."

For developers, it was often an ordeal just to get these loan officers on the phone. Verrone found that if he just kept calling and working his connections, he could cut a path through the red tape. Executive Capital's Ratzer says Verrone did exactly that with a \$24 million loan from Wachovia to his firm that was coming due this year and tucked away inside an enormous securitization. "We couldn't get anybody to return our calls," Ratzer says. "I said, 'Robert, do you know anybody at Wachovia?' He said, 'A lot of people have changed, but I know the system.'"

Iron Hound has done similar interventions for Joseph Moinian. The New York developer—one of Verrone's most acquisitive clients during the boom—is now fighting to keep his empire intact. In January, Moinian announced that Verrone had helped him restructure the debt on two of his Manhattan trophies. "Robert understands the loan documents," says the developer. "Robert negotiated the same set of documents a hundred times. He has been a great translator of what the other side expects."

The irony of his situation is not lost on Verrone. "This job is making me a better banker," he says. "We are seeing what happens when things go wrong." He adds: "Anyone who wants to get into this business and thinks it's easy, each loan takes 6 to 18 months to work out. And they are never easy."

Verrone is watching the apparent rebirth of the commercial real estate bond business—and thinking about heading back to Wall Street if things pick up. "We love our little Iron Hound gig," he says. "It's been great. But at some point, maybe we go back to a big shop and rebuild the lending business based on what we've learned." In other words, it may not be long before Verrone is once again throwing parties, quoting *The Godfather,* and disarming clients with tales of his Jersey roots. To show he has been properly chastened, the banker says he may hold his parties on the roof of the Marriott this time around. Then he changes his mind. "I'd rather go to a party at the Hudson," he says. When Large Loan Verrone starts partying on the roof, you'll know the next commercial real state cycle has begun. Ⓑ