

# Discussion on Local Asset Management Companies' Approach to Revitalizing Uncompleted Real Estate Projects: Taking ZS Asset Management Company as an Example

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**Abstract:** In recent years, with the vigorous development of the real estate market, the price and scale of real estate have been growing explosively year by year. At the same time, the continuous macro-control of the state and the debt of real estate enterprises are both thundering. The high turnover and leverage operation mode is challenged, and uncompleted real estate projects are constantly emerging. Uncompleted residential buildings are considered scars to developers or cities where these projects are located. If this issue can be solved, uncompleted residential building projects can be revitalized, and the parties involved will also benefit from it. Asset management companies play a key role in the revitalization of uncompleted real estate projects by injecting new vitality into these projects and obtaining relevant policy support from the local government for the pain points and difficulties in these projects, thus promoting the revitalization of uncompleted projects. In order to discuss the approach taken by local asset management companies to revitalize uncompleted real estate projects, this paper takes ZS Asset Management Company as an example.

**Keywords:** Local asset management company; Revitalize; Uncompleted projects; Real estate

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## 1. Introduction

Real estate is an industry that is subjected to strict policy regulation. Price fluctuations and industry prosperity have a significant impact on real estate. Some real estate projects are affected by the downturn of the real estate market, and the sales progress is slow. Especially in recent years, with the popularity of online e-commerce platforms such as JD and Taobao, commercial real estate is in serious recession. Due to the large proportion of business in some real estate projects, the funds returned from sales are unable to cover the high financing costs and project construction costs, thus leading to uncompleted projects that are difficult to revitalize. For uncompleted real estate projects in the local stock, the local government makes effort by establishing a linkage leading group, organizing regular working meetings, studying and coordinating the settlement of issues, as well as coordinating and promoting the disposal of uncompleted real estate projects from judicial, financial, planning, construction, acceptance, and other perspectives.

Local asset management companies tend to focus on non-performing assets and bear the responsibility of defusing local financial risks, with their main business scope in revitalizing uncompleted real estate projects. However, each uncompleted project has its own reasons. There are several cases and studies that

focus on the role of local asset management companies in revitalization. Two acquisition methods, transfer of development projects and equity transfer, have been proposed by Yan <sup>[1]</sup>. In a study <sup>[2]</sup>, Yan analyzed the advantages and operation path of trust in the disposal of uncompleted residential buildings. Wang <sup>[3]</sup>, on the other hand, discussed the steps and pricing methods for the securitization of uncompleted residential buildings. Several measures and the legal basis for the disposal of uncompleted residential buildings have also been proposed <sup>[4]</sup>. This paper discusses the approach taken by local asset management companies to revitalize uncompleted real estate projects, taking ZS Asset Management Company as an example.

## **2. Local asset management companies' approach to revitalizing uncompleted real estate projects**

### **2.1. Direct acquisition of uncompleted real estate project assets**

Local asset management companies would establish a two-layer special purpose vehicle structure (generally, a limited partnership and limited liability company) with the new project company, directly participate in judicial auctions to purchase the assets of uncompleted real estate projects (including but not limited to land, construction in progress, *etc.*), change or rehandle the development certificates of the original projects, and carry out subsequent development and sales. Not only can local asset management companies develop and sell by themselves, but they can also act as investors of judicial auctions. The transaction structure is designed as follows:

- (1) as a shareholder in the new project company (the acquirer of assets), local asset management companies participate in judicial auctions for asset acquisition in the form of shareholder contribution or shareholder contribution and shareholder loan in addition to carrying out subsequent development and sales;
- (2) local asset management companies and investors with real estate development capabilities form a limited partnership to participate in asset acquisition; the modes of establishment of this limited partnership include the following: local asset management companies as the priority limited partner and investors as the inferior limited partner and general partner; financial institutions as the priority limited partner, local asset management companies as the mezzanine limited partner, and investors as the inferior limited partner and general partner.

### **2.2. Participation in the bankruptcy reorganization of uncompleted real estate projects**

Local asset management companies may participate in the bankruptcy reorganization of uncompleted real estate projects as reorganization investors, without changing or rehandling the development certificates of the original projects or changing the property owner of the project assets. They can then carry out subsequent development and sales after paying off the debts of the original projects according to the bankruptcy reorganization plan ruled by the court.

#### **(1) Roles of local asset management companies**

The roles local asset management companies include the following: (1) restructuring investors, where local asset management companies and investors with real estate development capabilities set up limited partnerships to participate in project restructuring; (2) creditors, where local asset management companies purchase the financial claims involved in uncompleted projects, apply to the court for bankruptcy reorganization, and obtain the basis for project intervention; they are paid-off after the adoption of the subsequent reorganization plan, thus generating income; (3) co-beneficial creditors, where their rights are paid-off preferentially during bankruptcy reorganization, and funds are provided by local asset management companies for the continued construction of projects that belong to the co-beneficial creditors.

#### **(2) Transaction structure involved in bankruptcy reorganization**

The transaction structure involved in bankruptcy reorganization includes the following: (1) local asset management companies independently invest in reorganization, directly hold shares in the project

company, and carry out subsequent development and sales through shareholder capital injection, shareholder loans, *etc.*; (2) local asset management companies and investors with real estate development capabilities form limited partnerships to participate in project restructuring and subsequently develop and sell the project through shareholder capital injection, shareholder loans, *etc.*

The advantage of the approach taken by local asset management companies that participate in the bankruptcy reorganization of uncompleted projects is that local asset management companies can continue with the existing real estate development procedures of projects, accelerate the progress of project development and sales, as well as reduce the relevant tax and expenses of these projects. The advantage of a local asset management company's direct acquisition of uncompleted project assets is that it is completely isolated from the original project and is developed as a new project, so as to be protected from the adverse impact of the original project and the related problems of the project company. However, the disadvantage is that local asset management companies have to pay more taxes when handling the transfer of land, the projects under construction, and other assets. In addition, the acquisition cost will also be taken as the tax basis in subsequent land value-added tax, generated by the project. At the same time, changing or rehandling the development certificate of the original project would take up more time and cost.

### **2.3. Key points to revitalize uncompleted projects**

#### **(1) Comprehensive due diligence on the project**

Local asset management companies need to investigate the history of projects in an all-rounded way, including the equity situation, business license, past tax payment, payment of land transfer fees, asset mortgage and pledge, and litigation of the project company. They also need to evaluate and calculate the feasibility of project planning adjustment, various nodes of subsequent projects, development, and construction costs, the completion of sales cycle, *etc.*

#### **(2) Renewal of projects under construction**

Local asset management companies need to investigate the quality of the original projects under construction, the completion of municipal supporting projects and project supporting facilities, as well as hire professional institutions to issue complete feasibility plans for the continuation of uncompleted projects.

#### **(3) Support from the local government**

Uncompleted projects may have different planning requirements from those approved, incomplete real estate development certificates, and problems in maintaining the stability of creditors, which require the government to issue relevant policy support. Some uncompleted projects are more likely to have expired planning and construction permits due to long downtime, which may require re-approval by relevant government departments. The rights and debts of creditors from the long history of uncompleted projects are complex, and the legal disputes caused by them require the government's communication and coordination support. Therefore, in order to ensure that the revitalization of uncompleted projects is effective, a full support from the local government is a prerequisite, especially in aspects of housing construction, judicial, administrative approval, taxation, *etc.*

#### **(4) Public opinion support**

Uncompleted projects are like scars to cities, and they tend to be the focus of the media and the public. In the process of revitalization, local asset management companies should strengthen communication with media institutions, carry out positive and effective publicity, and create a good public opinion environment, which are all conducive to creating a positive market reaction toward these projects.

### **3. Case analysis of ZS Asset Management Company in revitalizing a stale real estate project**

#### **3.1. Background of the uncompleted real estate project**

In 2014, a real estate development company obtained a piece of commercial and residential land in Guilin city through public listing and bidding for land transfer, covering an area of 82.44 mu. The planned use includes commercial land and residential land, including 33,363.1 m<sup>2</sup> of another commercial land and 40 years of land use right. The residential land area is 21,596.7 m<sup>2</sup>, the tenure of land use is 70 years, the total building area is 122,057 m<sup>2</sup>, the plot ratio of the commercial land is 2.5, the building height is limited to 40 m, the building density is 40%, and the green space rate is 20%; the residential land is compatible with commerce, with a compatible proportion not higher than 30% of the total building area, its floor area ratio is 2.0, its building density is 30%, its building height limit is 34 m, and its green space ratio is 20%. There are some projects under construction on the land, including the first phase basement, D1 #, D2 #, H1 #, and H2 # buildings, with a built area of 57,327.62 m<sup>2</sup>; the second phase basement, A8 #, A9 #, and A10 # buildings, with a built area of 19,525.14 m<sup>2</sup>. The actual controller of the real estate developer was arrested by the Shanghai Municipal Procuratorate due to suspicion of economic crimes; most of the assets were preserved and frozen by litigation. This led to the rupture of the project company's capital chain, which affected the construction and operation of the real estate project and the ability to pay off due debts; thus, it was ruled bankrupt and liquidated in 2019. Due to the impact of COVID-19 and the national real estate industry regulation policies, the project has been auctioned repeatedly by Ali judicial auction without participation. In 2021, ZS Asset Management Company and Guilin Company A reached an intention to cooperate on revitalizing the project by means of bankruptcy restructuring investment.

On June 14, 2020, the web portal of Guilin Municipal People's Government put forward the Notice of Guilin Municipal People's Government Office on Printing and Distributing the Implementation Plan for Disposal of "uncompleted residential buildings" in the main urban area of Guilin. The notice made it clear that an overall coordination mechanism for the disposal of "uncompleted residential buildings" at the municipal level should be established, along with a leading group, which will be led by the People's Government of Guilin, with the involvement of the Municipal Intermediate People's Court and the participation of the Municipal Housing and Urban Rural Development Bureau, the Natural Resources Bureau, the Urban Administration Bureau, the Real Estate Registration Center, the local financial supervision and administration and other departments, as well as relevant urban people's governments, for the coordination and promotion of "uncompleted residential buildings."

#### **3.2. Motivation for revitalizing the uncompleted project**

- (1) The uncompleted real estate project is located in the core area of the main urban area of Guilin city. The surrounding facilities are complete, and the transportation is convenient. There are minimal competing residential products in its surrounding areas. The residents have a strong desire to improve their living conditions. In addition, the sales of residential products are expanding rapidly.
- (2) The uncompleted real estate project is Guilin Municipal Government's target. Revitalizing the uncompleted real estate project can help the local government solve the residual problems from history, improve the city appearance, and optimize the allocation of resources in the local real estate market.
- (3) Although the residential proportion of the uncompleted real estate project is only slightly more than half, the local government of Guilin has made clear the policy support to adjust the project use function, land nature, plot ratio, and other planning and design conditions according to the actual situation of the project and in accordance with laws and relevant policies and procedures as well as to confer appropriate preferential policies on other projects to the development enterprises that are taking over the "uncompleted residential buildings" project in accordance with the law, so as to increase the operability of the project. In addition, Guilin Natural Resources Bureau, in view of the pain point of the project's

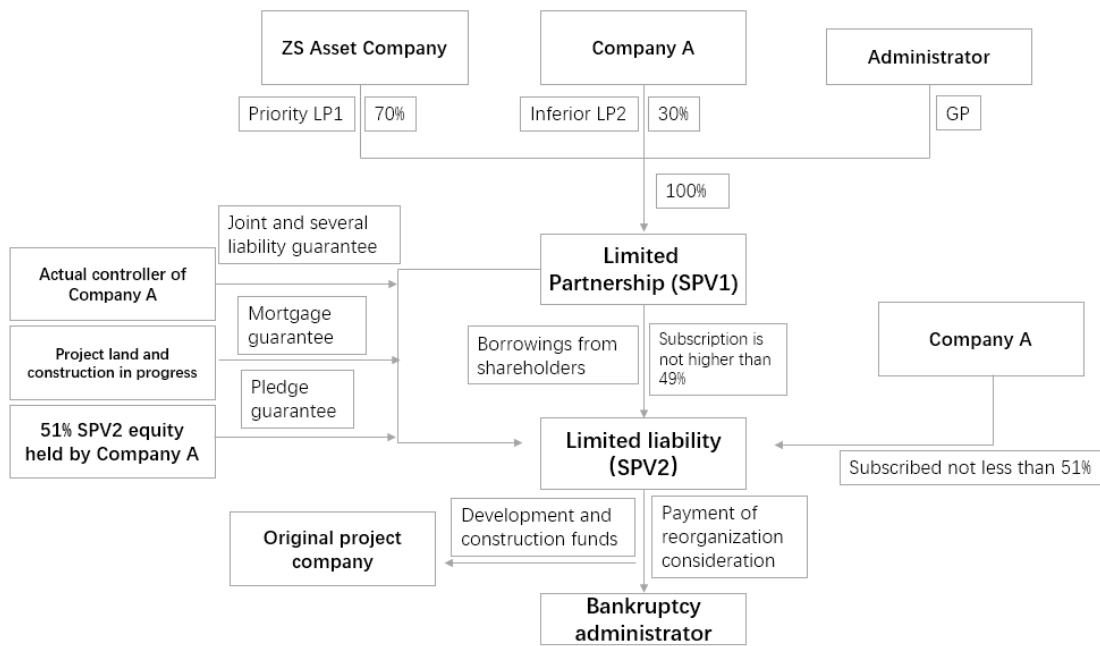
high commercial ratio, issued the SNZZ [2021] No. 139 document, namely the Notice of Guilin Natural Resources Bureau on Printing and Distributing the Implementation Rules for Adjusting the Ratio of Commercial and Residential Buildings to Real Estate Projects under Construction in Guilin (for Trial Implementation), which clarified the scope of application, working procedures, application conditions, and review focus of the Implementation Rules for Adjusting the Ratio of Commercial and Residential Buildings to Real Estate Projects. It will greatly help investors to promote the progress of the uncompleted real estate project's reorganization.

- (4) The uncompleted real estate project has obtained four licenses, namely land license, construction land planning license, construction project planning license, and construction project construction license, as well as several pre-sale licenses. After taking over the real estate project company, subsequent development, construction, and sales can be carried out. The original construction, design, earthwork, and other development costs can still be used as tax credits to reduce relevant tax expenses.

### 3.3. Specific operation mode and risk control means

#### 3.3.1. Specific operation mode

The real estate project adopts the mode of “participating in the bankruptcy reorganization of the uncompleted real estate project.” ZS Asset Management Company, together with Guilin Company A, as the investor, forms a limited partnership to participate in the project reorganization, pays for the bankruptcy reorganization consideration through shareholder capital injection and shareholder loans, and carries out the subsequent development, construction, and sales of the real estate project. The specific transaction structure of the project is detailed in **Figure 1**.



**Figure 1.** Transaction structure

The specific operation steps are as follows: (1) ZS Asset Management Company, Guilin Company A, and the general partner jointly set up a special purpose vehicle 1 limited partnership; special purpose vehicle 1 limited partnership and Guilin Company A jointly fund the establishment of special purpose vehicle 2 limited liability company, with ZS Asset Management Company, as the priority financial investor, whose contribution shall not exceed 70%, and Guilin Company A, as the inferior investor, whose contribution shall not be less than 30%; special purpose vehicle 2 participates in the bankruptcy reorganization of the

original real estate project company; (2) special purpose vehicle 2 submits a bankruptcy reorganization plan to the People's Court, and after the bankruptcy reorganization plan is approved by the creditors' meeting, the People's Court makes a ruling, which takes effect; special purpose vehicle 2 pays the reorganization consideration to the bankruptcy administrator; (3) after the payment of the reorganization consideration, special purpose vehicle 2 acquires 100% of the original real estate project company's equity and takes over the original real estate project company's seals, licenses, and certificates; (4) after the real estate project starts development, construction, sales, and other work, the return on investment generated is returned and distributed to ZS Asset Management Company and investor company A according to the agreement made by all parties.

### **3.3.2. Risk control means**

#### **(1) Guarantee measures**

A total of 51% of the shares of special purpose vehicle 2 held by investor company A are pledged to special purpose vehicle 1. The actual controller of investor A provides joint and several liability guarantees. The project land and construction in progress are mortgaged to special purpose vehicle 1 (after consulting the local mortgage registration department of Guilin, special purpose vehicle 1 can be assumed as the mortgagee to go through the mortgage registration procedure). The original real estate project company is added as a co-borrower of the loan from special purpose vehicle 1 to special purpose vehicle 2.

#### **(2) Supervision measures**

The supervisors appointed by ZS Asset Management Company and the investors appointed by Company A jointly supervise the official seal of the project company, the name seal of the legal representative, the special financial seal, the bank account, the online banking key, and the business license. A supervisor appointed by ZS Asset Management Company and an employee appointed by Company A jointly manage the capital account, financial seal, U shield, password, *etc.* of special purpose vehicle 2 and the real estate project company. The capital, shareholder loan capital, principal of creditor's rights and capital occupation fees, daily expenses, management fees, taxes and other capital transactions, receipts, payments, and settlement of special purpose vehicle 2 and the real estate project company should be implemented through a regulatory account.

#### **(3) Decision making mechanism**

At the level of special purpose vehicle 1 limited partnership, the general meeting of partners is the highest decision-making body, voting on major issues such as entering and exiting partnerships, capital increase and reduction, share transfer, project investment, project exit, income and principal distribution beyond the authority of executive partners, foreign financing loans, foreign guarantees, liquidation, and cancellation. One partner has one vote, and all major issues shall be unanimously approved by all partners. At the level of special purpose vehicle 2 limited liability company, the company's authority belongs to the shareholders' meeting. Shareholders exercise their voting rights at the shareholders' meeting in accordance with the proportion of their capital contributions. Major matters involving equity transfer, merger, division, dissolution, dividend, foreign investment, asset transfer and disposal, foreign financing loans, foreign guarantee, and other major issues must be unanimously approved by all shareholders at the shareholders' meeting.

#### **(4) Income distribution mechanism**

Before the exit of ZS Asset Management Company's priority principal and interest, the inferior part of the income of Company A will not be distributed.

### **3.4. Effect of revitalizing the uncompleted real estate project**

Under the extremely complex macroeconomic environment, the revitalization of the uncompleted real estate project has a positive effect.

- (1) By resuming the uncompleted real estate project, it becomes a landmark building in the center of the city, reviving the urban scars, meeting the needs of the residents, and improving their living conditions. The completion of the investment promotion and supporting facilities for the commercial part of the project addresses the issue of insufficient proportion of surrounding businesses.
- (2) The overall plan for the participation of local asset management company in bankruptcy restructuring investment provides a more referential case support for the local government and also solutions for other local real estate projects that have not been completed.
- (3) The issuance of policy plans by the local government to address the issues in the uncompleted project helps solve the pain points of the project and further promotes the reorganization and revitalization of the project more smoothly.

### **4. Conclusions and suggestions**

The revitalization of uncompleted real estate projects by local asset management companies belongs to the comprehensive “non-performing and investment bank” business. The ability of local asset management companies to professionally dispose non-performing assets, effectively control risks, and take into account of social and economic benefits can be effectively played out by establishing a reasonable transaction structure based on the actual situation of the project. From the perspective of revitalization, if the original real estate project planning is clear and the development and construction procedures are complete, it is recommended that local asset management companies and investors form a limited partnership to participate in the bankruptcy reorganization of uncompleted real estate projects. If there are many residual problems from the original project and given a complex relationship between the creditor’s rights and debt, it is recommended that local asset management companies and investors form a limited partnership to directly purchase the real estate project assets through judicial auctions. From the perspective of risk control, most local asset management companies lack the ability to operate real estate projects. Hence, they should choose partners with strong financial strength, rich real estate development experience, and good reputation as cooperative investors. At the same time, they should obtain relevant support from the local government in the early stage of the project and obtain relevant written documents on communication and coordination with relevant departments from the local government. Local asset management companies should try their best to acquire policy support from the local government for the pain points and difficulties in the uncompleted projects, so as to promote the reorganization and revitalization of uncompleted real estate projects.

### **Disclosure statement**

The authors declare no conflict of interest.

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