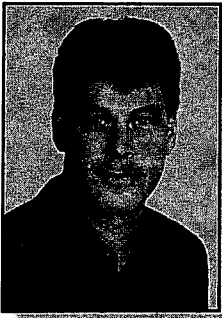


SECURITY DEPOSIT ALTERNATIVES ALLOW APARTMENT OWNERS AND MANAGERS TO MORE SAFELY TAP THE POTENTIAL LEFT IN THE WAKE OF THE SUBPRIME DEBACLE

by Dan Rudd, CFO, SureDeposit



While the multifamily industry stands to gain handsomely as a result of the subprime debacle, it also has become more vulnerable to balance sheet losses. This is due to a surge in rental applications coming from those beleaguered by foreclosures and compromised credit histories and the fact that property owners feel pressured to lower their credit standards to achieve greater occupancy levels.

This scenario had already begun to reveal itself in 2006 when, as the National Apartment Association's 2007 Survey of Operating Income & Expenses in Rental Apartment Properties revealed, industry NOI rose by 3% in 2006 over the previous year, while at the same time, the industry wrote off an estimated \$18 billion due to vacancies, concessions and bad debt.

The confluence of today's volatile market conditions has created a scenario that puts added pressures on property owners and apartment management firms to more proactively protect themselves

against bad risk and market their properties more aggressively as they capitalize on the downturn in homeownership. This means re-establishing and adhering to sound risk management principles while putting in place better safeguards against the kinds of losses the industry sustained in 2006.

Security deposit alternatives are already part of a sound risk management and aggressive marketing approach in some 3,300 communities nationwide. Most often found in the form of a surety bond, security deposit alternatives protect apartment owners and management firms against losses that a unit sustains as a result of damages or a resident skipping out on the rent. At the same time, the surety bond option offers a distinct marketing advantage because it allows the resident to move in at a dramatically lower cost.

Specifically, at lease signing, instead of paying the traditional, refundable and more costly cash security deposit that the landlord holds for the duration of the lease term, residents can opt to pay the lower cost surety bond premium. For example, one program that offers surety bonds offers a minimum coverage of \$500, with coverage in \$250 increments thereafter. For \$1,000 worth of

coverage against losses, the resident only pays \$175 for the surety bond premium as an alternative to the security deposit typically costing more than five times that amount.

How does the security deposit alternative work? At lease signing, if the prospective resident chooses the surety bond over the traditional, refundable security deposit, he pays the premium directly to the surety. The one-time, nonrefundable bond premium remains in effect for as long as the renter resides at the leased apartment. And because the program is available nationally, residents can transfer their coverage to different communities within an owner's portfolio.

At move-out, if the resident meets his rental obligations and vacates the apartment in good condition, he leaves without any further obligation. If, however, any lease-covered damages or rent loss occurs, owners file a claim with the surety for prompt reimbursement of the debt amount up to the coverage limit. The surety then pays the owner's claim from the bond premiums, less a fee to administer the program, which the surety has pooled for that owner/property manager's sole use.

The benefits of the surety bond program to owners can be substantial. It discourages residents from failing to pay their rent or leaving their units in poor condition when they move out. This is because the resident remains fully liable for his lease obligations under the terms of the surety bond. In addition, the lower up-front costs required for someone to move into a new apartment make it easier for a leasing agent to close the sale.

But arguably the most dramatic benefit to owners can be found in their enhanced level of protection and the subsequent and significant impact on a property's bottom line, particularly

in markets where the requirement of full cash deposits puts a property at a competitive disadvantage. While bad debt cannot be entirely eliminated, the surety bond provides a level of coverage to the apartment community against losses or lease violations that often exceeds that of a market-based, traditional security deposit, allowing apartment owners and managers to reduce the amount of unrecovered debt and improve their NOI. By aggregating funds from both "good" and "bad" residents in the pool, the surety leaves more money available to pay for the inevitable losses.

Furthermore, this significantly improved financial protection costs property owners nothing because the surety bond premiums are paid by residents. The only indirect cost to owners is the time required to evaluate and integrate the program into their leasing process.

Apartment owners and managers can seize the moment to achieve higher occupancy rates in the wake of the mortgage industry fallout, but not at the expense of good balance sheet management. By implementing a concerted risk management program that entails a security deposit alternative, owners can more safely tap the potential of a significantly larger renter pool. ☞

By Dan Rudd, CFO of SureDeposit. With more than one million units in nearly 3,500 communities under agreement, SureDeposit is the nation's leading provider of alternatives to traditional security deposits. Founded in 2000, SureDeposit is headquartered in Livingston, N.J., and has regional offices in Arizona, California, Florida, Georgia, Indiana, Maryland, Nevada, Rhode Island and Texas. For more information, call 1-800-531-SURE (7873), or visit online at www.suredeposit.com.