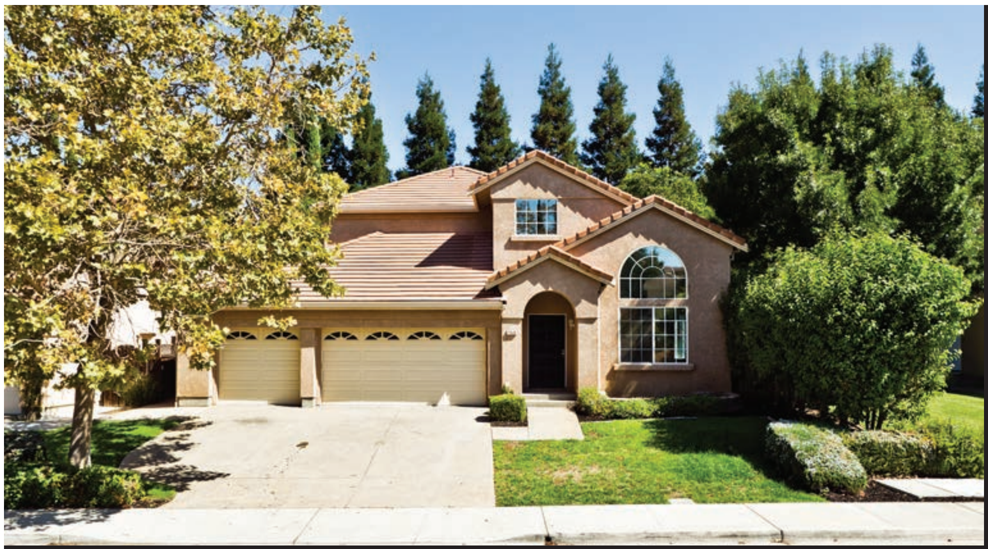
EXTREME REAL ESTATE

An astonishing *half* of California homes on the market are foreclosures—and the crisis could last a decade. But **Doug Brien**, a former NFL placekicker, and **Colin Wiel**, a software whiz with serious quant chops, have invented an assembly line for distressed real estate that could make them rich and, incidentally, recharge the American dream of home ownership. A case study of accidental social entrepreneurship. **BY DIANA KAPP**

FORECLOSURE, A LOVE STORY

PHOTOGRAPHS BY ERIC MILLETTE

In 2009, Colin Wiel (left) and Doug Brien were just two guys with a car, driving from house to house with the idea of buying up foreclosed homes and renting them out. They now own 778, including this one in Antioch, and look to sign up tenants who will eventually want to buy.



IN LATE 2008, WHEN HOUSES IN ANTIOCH WERE SELLING FOR 65 TO 70 PERCENT BELOW THE PEAK, DOUG BRIEN AND COLIN WIEL STARTED TALKING. Both were seasoned Bay Area real estate guys, but even amid the economic and subprime-mortgage meltdown, that figure caught their attention. The two clean-cut Berkeley grads, both in their 40s, had met through the Keiretsu Forum, an angel investor group Wiel had started up locally. The Antioch situation was a great opportunity: Two guys with money in hand, both keen on cash-flowing real estate, both stunned by Bay Area homes selling for under $100,000. So they decided to have lunch.

The two were soon driving around Contra Costa and Solano counties in Brien's navy blue BMW, with area real estate agent Tom Hennigan spouting block-by-block intelligence from the backseat. The detritus of the mortgage disaster was everywhere, from "the Crest" in Vallejo to the San Pablo lowlands, and all along the Highway 4 corridor between Concord and Oakley—"the busiest stretch of freeway in the Bay Area," says Brien. Antioch, Pittsburg, Fairfield, Vallejo: These communities had ballooned to house a growing Bay Area workforce that couldn't afford to live closer in, but now they were shaded dark red on heat maps tracking the nation's foreclosure devastation.

Home prices here had run up so irrationally during the exuberant period that when the economy tanked and values plummeted, banks hoping to recoup some value started unloading the reclaimed homes at a deep discount, which reset values lower and lower, in what Wiel describes as a "death spiral." Homes were going for 80 cents on the dollar, and then 64 cents, and so on. "We were thinking this was unlike anything that's ever happened," recalls the dark-haired Wiel, a serial entrepreneur who looks like an unlikely hybrid of a Santa Cruz surfer and a Boy Scout.

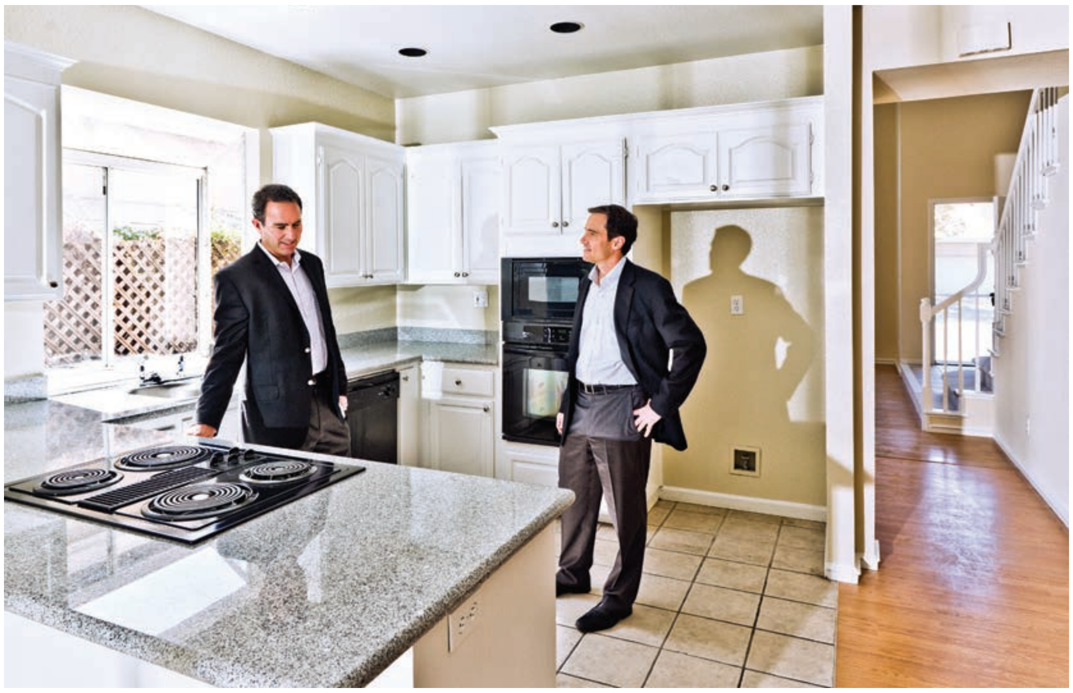
He and Brien figured that the best way to understand the market was to just start buying. The first house they snapped up was a three-bedroom, 1,170-square-foot rambler on Maple Street in Pittsburg, offered by the bank for $90,000. They put in a lowball bid, and because no one else was out buying, they got it six weeks later, in January 2009, for $65,000. (The prior owner had paid $410,000 in 2005.) While waiting for the bank to lose patience, they bid on another home, and another. "People all told us we were absolutely crazy to be buying. Things were just so bleak," Brien recounts. Luckily, the former NFL placekicker, drafted by the 49ers straight from Cal, has the stomach for putting himself on the line. When he retired from football in 2005, he was known for having missed two potential game-winning field goals in the final minutes of the 2004 New York Jets vs. Pittsburgh Steelers AFC divisional play-off game—but he was also one of the top 10 most accurate strikers of all time.

When the two business guys—Brien had made the unlikely move of getting an MBA while playing pro ball—ran the numbers, they confirmed the attractiveness of the rental play. They figured that with an $18,000 renovation, the Maple Street house could rent

for $1,595 a month, or just over $19,000 a year, yielding close to a 15 percent annual return on their cash outlay, minus expenses. Wiel and Brien assumed that once the market caught up and home prices started to rise, the return would be more like 8 to 10 percent, and even that, they thought, seemed impossibly high. Other real estate ventures, such as multifamily apartments, office buildings, and retail properties, were generating returns in the 5 to 8 percent range. "But what we realized," says Wiel, "is that core Bay Area single-family houses, probably for the first time in history, could generate more cash flow than any other class of real estate investment."

The two figured they had six months to exploit this Wild West moment before big real estate players swooped in or the market turned. So, with $1 million of their own money and another $1.5 million borrowed from the bank, they jumped in, grabbing a three-bedroom Pittsburg home within commuting distance of San Francisco and Silicon Valley that was selling for $55,000; Vallejo ranchers in Solano County going for $75,000; Bay Point bungalows for $110,000.

About 10 houses into the game, they had another revelation: Despite headlines declaring the fall of home ownership, the people they were meeting—even those with wrecked finances—still very much wanted to own homes. So they ran a new set of numbers and found that if they created a rent-to-buy option and, in four to five years, sold the homes to the residents for about 40 percent more than Waypoint had paid for them back in 2009, they could generate an additional 10 percent



TOP: **All Waypoint homes, like these in Antioch and Vallejo, are given the same market-proven cosmetic redo—and many of the same amenities.**

ABOVE: **Waypoint is aggressive about making a foreclosed house a place people want to buy rather than just rent, which is why the company often pops for granite countertops.**

annual profit. The key would be choosing tenants who both wanted and were able to buy, which would help the pair mitigate the biggest risk of the rental business. "If people don't take good care of the property, and move out frequently, you can lose all your profits to renovation and vacancy," Wiel explains. They would ask for 3 percent of the minimum purchase price up front for an option to buy, do a quick fix-up, and, at the time of purchase, credit tenants $200 a month toward the down payment for every month they had rented. Hence the name they chose for their new company: Waypoint.

And hence an added, if unintended, value of their business: Waypoint would also help people back to home ownership. The business model involved some tricky elements: evicting current tenants, in many cases; helping new ones get their finances in order; asking people to leave if they couldn't make the rent or afford to buy. But if it all worked, they could create the ultimate win-win: money for themselves and their (future) investors, and a fix for one of society's most pressing problems.

That was 778 homes ago—and the six-month window of purchasing that Wiel and Brien anticipated in early 2009 now looks more like a six-*year* proposition (at least). In January, Morgan Stanley predicted eight million foreclosures nationwide in the next five years, and a recent report estimates that 12,410 San Francisco homes will be in foreclosure by 2012. In the second quarter of 2011, 51 percent of Golden State homes sold were foreclosed on—and banks are choking on the glut. "It's like a grapefruit going down a snake's throat," says Glenn Kelman, the CEO of Redfin, a real estate listing site. "For the guy with a suitcase full of cash in one hand and a toolbox in the other, this is a perfect time."

If Wiel and Brien are that guy, they've blown up the traditional toolbox. The foreclosure world historically has been a sleazy real estate sideshow, in which single contractors and lowbrow outfits compete to capitalize on disasters by flipping homes one at a time for quick cash. But in two short years, just as this corner of the industry has grown exponentially, Waypoint has disrupted it. Scaling up at extreme speed, the firm, which is based in Oakland, now has the ability to identify, appraise, acquire (at auction, on the steps of four different courthouses), renovate, landscape, clean, and lease hundreds of homes—each within a few compressed, intense months. Wiel and Brien have built a 75-person firm. They've acquired a fleet of company Priuses that double as mobile billboards. They've also created what appears to be a game-changing, cloud-based data infrastructure, using the Salesforce.com platform, that dissects and automates everything they do short of cutting the grass. Not coincidentally, Wiel had a software engineering consulting business in the '90s—only a quant geek with a systems orientation could make all this happen without losing his mind.

Their business plan also appears to be exceptionally timely. It seems to ride every current wave in the housing industry, from the boom in rental demand, to the drop in construction costs caused by the building freeze, to historically low interest rates, to the sea of people with a desire to own but no credit. Predictably, competitors have come along. A few are skirting the need for labor-intensive house-by-house purchasing by buying in bulk from the banks. McKinley Capital Partners, also in Oakland, just announced a deal with large New York hedge fund Och-Ziff Capital Management Group to buy 500 homes next year, but the firm isn't talking to the press, so its strategy is unknown. Even the U.S. government is considering getting into the rent-to-own game with homes it holds through Fannie Mae and Freddie Mac, which could mean either intensified competition or partnership opportunities.

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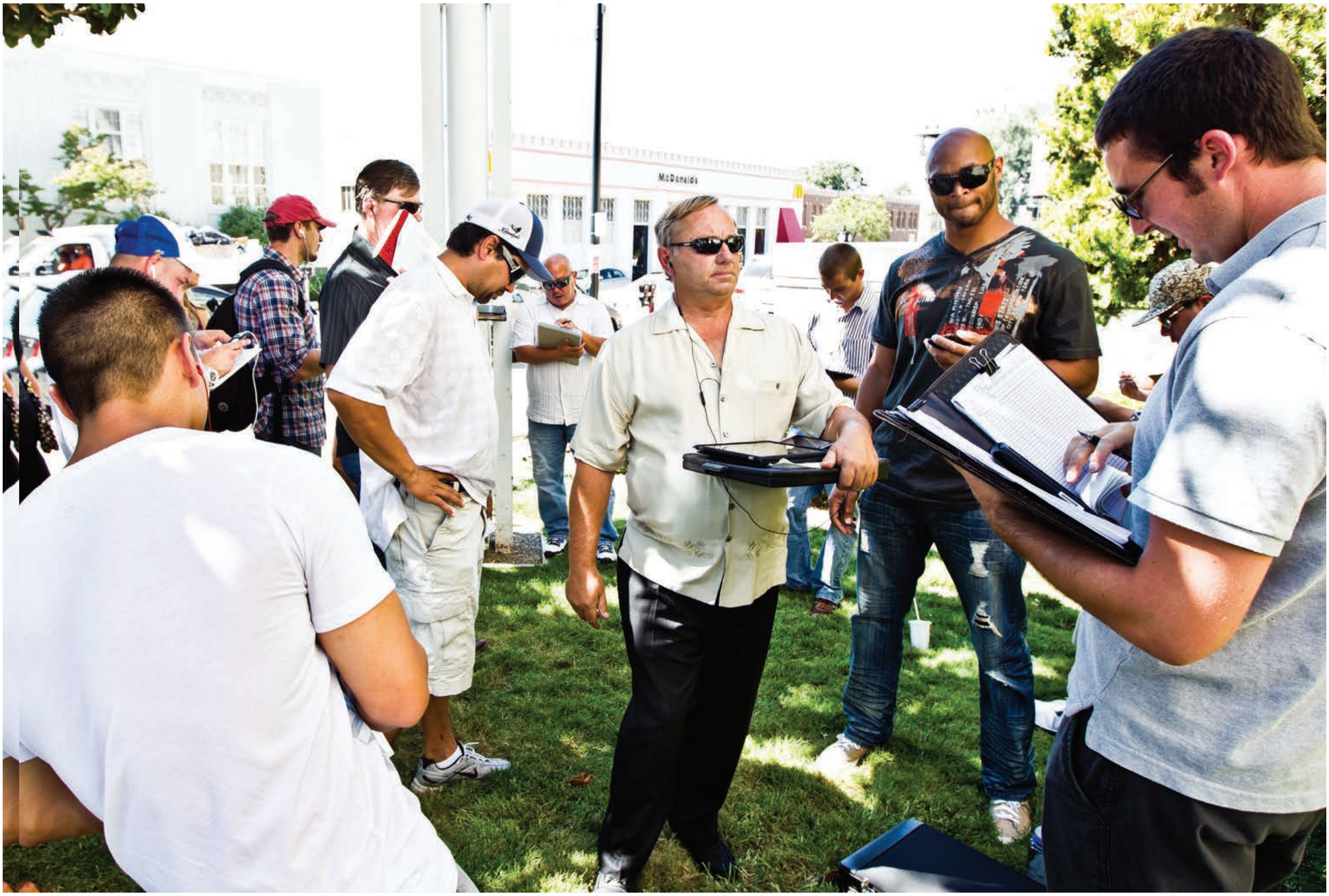
With their cat out of the bag, Wiel and Brien are running as fast as they can. They recently secured their first big investment—$50 million from an Ivy League endowment, the name of which they prefer not to disclose—and they've got others banging on their door, talking about sinking hundreds of millions into the business. And they've already expanded into heavily hit areas in Southern California, like Riverside and San Bernardino counties. Ultimately, Wiel and Brien foresee themselves buying homes in the tens of thousands, moving into other western states, including Nevada, Washington, and Arizona, and making profits in the hundreds of millions.

THE ACQUISITION. It's 10:40 a.m., and Bill Katsaros comes dashing up the Martinez courthouse steps as the auctioneer announces that the sale of the third house of the day has been postponed. Katsaros got hung up at the bank, where he stops every morning to pick up hundreds of thousands of dollars in cashier's



checks—an odd way to walk around town, but these are cash-only affairs.

The broker and former loan agent is the lead bidder for all of the homes Waypoint buys at auction in Contra Costa County. (Waypoint buys about 60 percent of its homes this way and 40 percent the old-fashioned way, with a broker and listings.) Katsaros is on the courthouse steps all day, every day. "We stood out here last week for six hours in the pouring rain," he boasts.

Many of these purchases are sidewalk-view only, meaning that ripped-out pipes, termites, or any other normally deal-breaking damage usually isn't discovered until after the buyer has the house in hand. This April morning, every one of the 20 or so people crowded around the crier has a headset or a phone glued to his or her ear, presumably speaking to someone manning a spreadsheet and calculator on the other end of the line. Voices are hushed, since secrecy rules, partly because the FBI and the Department of Justice just completed an investigation into alleged buyer collusion at the Alameda and Contra Costa county home auctions. Waypoint was subpoenaed along with 150 other bidders, but it wasn't one of the eight parties charged in June with a felony, which carries a maximum 10-year prison term and a $1 million fine.

The auctioneer, in jeans, with a black hoodie pulled up over his head, speaks in a monotone, so he's hard to hear. As he runs through a string of homes in Hercules, a subdivision-stuffed town in Contra Costa County, on San Pablo Bay, Katsaros sits tight—the market rents relative to purchase prices there don't produce the returns Waypoint requires. But he snaps to when the house at 141 Warhol Way in Oakley opens at $165,000. "Get him on the phone quick," he barks to the associate at his side.

"Him" is Doug Pankey, Waypoint's director of purchasing and disposition, who is back in Oakland working at least two computer screens. Pankey's figures determine what Katsaros can bid, and since there's a great deal of subjectivity in assessing home values, Waypoint has built in multiple reviews.

One is something that Wiel and Brien invented, called a livability score, which compresses into a usable data point many factors that affect property value and can be viewed from outside a house—negatives like unsightly power lines or the unkempt lawn across the street and, on the upside, things like the quiet cul-de-sac at the end

Bill Katsaros (middle) is the head bidder for the homes Waypoint buys at auction in Martinez. He's on the phone with his stats guy back at the office, who has applied the company's "livability" formula to help determine how much Katsaros can bid on each property.

A Waypoint "home-rescue agent"—in this case, Austin Gaydos—leaves a note on the door of each house the company purchases, saying that tenants who can't or don't want to buy have 15 days to vacate the premises.

of the block. "It's block by block," Pankey explains. "Go below the 1900 block on 16th Street in San Pablo, and you're likely to get shot. Go above, and you won't." Waypoint has developed a custom app that its staff uses to collect this street-level intelligence. The company also buys or programs in hundreds of thousands of data points that allow it to assess other issues, from crime stats to the local school's API scores to BART station proximity. Any one of these factors can make the few-thousand-dollar difference between a purchase and a pass. For example, when the bid on the Oakley house is $168,000, Waypoint is still in the game—but once it hits $172,000, Katsaros whispers to Pankey that they've passed their max.

Next up is a three-bedroom house in San Pablo, which Katsaros gets for $143,800, $10,000 under his maximum. "Now we usually adjourn to our office," he tells me, pointing to the McDonalds across the street. Inside, he's back on the phone with Pankey. "I need, like, $3,000 more to play ball on Duncan," he says, prepping for the afternoon auction. Unfortunately, Pankey can't budge.

By week's end, Waypoint has analyzed about 500 homes on the foreclosure list (200 in Contra Costa, the rest in Solano County towns like Vacaville, Fairfield, and Vallejo), 34 of which went to auction. That's not an atypical workload; it's necessary because bidders don't find out until the actual auction which homes have been postponed or canceled. Katsaros bid on 7 of the 34 and got 4, the return on almost 200 man-hours of work. One small-scale Martinez bidder revealed that, on average, he wins just 1 in 50 homes, which makes Waypoint's 4-out-of-34 success rate sting a bit less.

THE MESSY PART. Austin Gaydos has come a long way, from being one of "four frat brothers with a kegerator" to being Waypoint's "home-rescue agent," a job that makes the 24-year-old UC Davis graduate the first point of contact between the company and the occupants of a house it has purchased. (He has since been promoted to acquisitions associate.) It's an area of the business where things can get uncomfortable, since most of the time (95 percent), Gaydos must make sure that the residents leave—either because they're not interested in a rent-to-buy deal, or because they are but Waypoint has determined that they're not a good financial bet. Gaydos, who always dresses for work in slacks and a dress shirt or a Waypoint polo—"to be respectful," he says—admits that it's hard going.

The moment a purchase occurs, an email pops into Gaydos's in-box, and he drives to the home. Typically, no one is around, so he leaves a note: "I represent the company that purchased your home at a Trustee's Sale Public Auction. My job is to keep you in the home, as we are investors looking for renters." He began by scribbling these on yellow legal paper and taping them to the door, but he has recently started using stationery, to appear more professional. He also now writes that if the tenants don't want to stay, they need to leave within 15 days or Waypoint "will be forced to move forward with legal action to gain possession of the premises," and that if they do want to stay, they have three days to complete the application process.

When Gaydos does find people in the house, he emphasizes that Waypoint would like to help them stay and buy (or buy back) the home. He also offers many services—free—including a 24-step "Financial Fitness Plan" to raise their credit score, counseling, seminars, and sample creditor letters. "It's enlightened self-interest," explains company investor Bruce Katz, a pioneer of so-called socially responsible businesses; he cofounded Republic of Tea in the early '90s and, before that, Rockport. "The cost of holding someone's hand for months is cheaper than paying a real estate commission to sell to a new person, right?" says Katz.

● THE SPECTER OF OPPORTUNISM HAS BEEN RAISED—THE IDEA THAT WAYPOINT PROFITS FROM PEOPLE'S MISFORTUNES. WIEL'S RESPONSE IS THAT THE FIRM'S "WHOLE MISSION IS ABOUT REHABBING HOMES, FAMILIES, AND COMMUNITIES."

Waypoint acknowledges that only about half of the tenants with whom it signs rent-to-buy contracts will actually buy within the allotted four- to six-year time frame, given all the potential obstacles: job loss, divorce, illness, or unanticipated debts. When the deals aren't completed, tenants lose their up-front payment, plus the $200-per-month credit they've been accruing. The company recently created a contract with a shorter commitment that offers, among other options, a 5 percent recoup of the up-front payment if tenants leave.

On the day I spend with him, Gaydos stops in Pittsburg to deliver the final paperwork to a tenant who wanted to stay but didn't qualify because he didn't have stable employment. When Gaydos tries to finalize his departure date at a few weeks away, the man requests five additional days. Gaydos agrees, yet also offers him cash if he'll get out even earlier than the original date, in addition to a sum Gaydos has already promised for the keys and no trouble. The cash is a necessary tool, Gaydos explains. "We figured out that otherwise they have no incentive to leave. I try not to be that skeptical, but sometimes people don't have the best of intentions."

Later, Gaydos says he could have been tougher. But the job comes with a yin-yang dynamic built in: Hitting his numbers pushes him in one direction, and tattered lives pull him in another. His goal is to be a real mensch.

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Jose Castillo, who works in office maintenance at a janitorial company, and his wife, Felipa Boailla, a housekeeper, were among Waypoint's very first clients. They moved to this Vallejo house after the one they were living in a few blocks away was foreclosed on. They've put in most of these plants themselves, and hope to buy the house in a year or two.