

Tactics for Facilitating Successful Real Estate Transactions

Jane B. Morgan

Member

Watkins & Eager PLLC



ASPATORE

Introduction

Recently, the focus of my real estate practice has been on mixed use development projects, commercial real estate financing, workouts, and foreclosures. At its core, with a few notable exceptions such as flying fee and other air space cases, a real estate practice is about the “dirt” and every property is different, just like every person is different. When working on a real estate development, it is important for lawyers to visit the physical site of the project in order to appreciate the quirks and unique aspects of the landscape and to understand the developer’s vision. One site visit can transform the drafting of project documents from the mere massaging of mundane forms into crafting legal agreements that actually translate the parties’ intent for that piece of real estate.

It is important to never forget the basics. Time spent analyzing riparian rights or debating prescriptive easements with the elder statesmen of the real property bar is never wasted. We are most fortunate in our law firm to have several octogenarian lawyers. Suffice it to say that they have just about seen it all, and a lot can be learned from them. Although today’s real estate lawyers are expected to be versant in everything from conduit financing to TIF bond deals, long-established (and sometimes archaic) state property law is at the core of our practice. For example, in the jurisdiction where I practice, our statutes provide for three types of conveyance deeds, commonly referred to as a warranty deed, a special warranty deed, and a quitclaim deed. If a seller is required in a real estate purchase contract to convey by warranty deed or general warranty deed, then the seller must warrant not only title but also all of the covenants known to common law, namely: seizin, power to sell, freedom from incumbrance, and quiet enjoyment. Miss. Code Ann. 89-1-33 (1972). In contrast, if the contract calls for a special warranty deed, the seller is entitled in the conveyance deed to “warrant specially,” which is a lesser form of warranty. Instead of warranting the five common law covenants, the conveyance by special warranty deed permits the seller to “warrant specially,” which means that the seller, his heirs and personal representatives only promise to warrant and defend title to the property against claims by any persons claiming through the seller. Miss. Code Ann. 89-1-35. Last in the hierarchy of conveyances is the quitclaim, which merely passes all the estate or interest that the seller has in the land—whatever that might be—but also estops the

TACTICS FOR FACILITATING SUCCESSFUL REAL ESTATE TRANSACTIONS

seller and his heirs from later asserting title by adverse possession to the sold property. Miss. Code Ann. 89-1-39. Anyone who buys property in our state and thinks he got the best deed possible just because it was labeled "special," might want to take some time to get back to basics before doing another real estate deal. That said, a special warranty deed may be perfectly acceptable in any given transaction and is commonly used in commercial real estate transactions depending on the business involved and the needs of the developer.

Although each real estate deal is different, my practice has led me to conclude that there are some basic principles common to all that revolve around proper preparation, good communication, document organization, and attention to detail.

Effective Practices for Commercial Real Estate Transactions

First and foremost, the lawyer's job is to listen to the client's evaluation and goals for the project. For example, if the client is a seasoned developer who arrives with a well-developed site plan and approved zoning letter for a traditional condominium development on a tract of land that the client already owns, then my job should be relatively streamlined and the client's legal costs can be kept to a minimum. At this stage, my primary functions might be limited to:

1. preparing a condominium declaration and covenants suitable to the project in proper form for recording;
2. working with the developer-client and engineer to produce a legally compliant and recordable condominium plat with all the proper certifications and notarized signatures required by the applicable governmental authorities;
3. recording the condominium documents; and
4. setting up the condominium association.

If, on the other hand, the client arrives with hopes of purchasing property that is tied up in a contested estate and wants to build a commercial office park, but has no idea how the property is currently zoned, then I immediately know that significant up-front leg work will be required of me and that the jury is out on whether this transaction will come to fruition. In

an effort to keep initial legal costs under control, I would probably suggest that the client begin by contacting the proper governmental authorities to determine the current zoning of the property. If it is not already zoned commercial, then we will discuss the legal and political hoops, time delays, and attorney costs involved in changing the zoning designation. These uncertainties alone, not to mention the seller's ability to transfer clean title, might influence a purchaser to look for alternative sites.

Preparing Clients for Successful Real Estate Transactions

In every commercial real estate transaction, some basic items are generally needed: good title to the property, access, proper zoning, adequate parking, utilities, environmental assurances, flood plain information, and a financing commitment. I will make sure that the client has each of these covered, and if this is not the case, I will explore each more thoroughly with the client. I ask to see a survey because even an old survey is better than no survey at all in the initial stages. An updated survey will be required by the lender prior to closing. I want to know that the client has confirmed that the property site is suitable for the intended use before the client spends a lot of money on legal fees and development costs. I will also ask to see any drawings that an architect has done to date of the project.

Another item that should be dealt with early on is the structure of the transaction and whether new corporate entities will be needed to facilitate the transaction. For example, I will ask the client if a special purpose entity has been formed to serve as the "declarant" for purposes of the covenants in a condominium or subdivision project. I will need to know from the outset if the property is subject to any regulatory agreements (e.g., Land Use Restriction Agreements under Section 42 of the Internal Revenue Code) or is located in a Tax Increment Financing (TIF) District, Planned Unit Development (PUD), or a Public Improvement District (PID), which may require special disclosures in project documents (see example of PID disclosure below) and can result in taxes or assessments that the developer will need to address and budget, to the extent quantifiable. For example, the governing board of a PID district will determine PID assessments annually based on costs of public improvements and services. Such assessments are levied in addition to annual property taxes and should not be overlooked when budgeting project costs. Careful budgeting also is required for

TACTICS FOR FACILITATING SUCCESSFUL REAL ESTATE TRANSACTIONS

projects conducted in TIF districts. If properly authorized, a developer may qualify for reimbursement of certain infrastructure costs by the governmental issuer of TIF bonds, which may be issued once ad valorem and sales tax revenues in the TIF district reach sufficient levels to pay off the bonds. Because of the political and legal variables involved, budgeting for the expenditure of such costs and eventual reimbursement is far from an exact science.

Conducting Research

In any real estate transaction, the key piece of “research” will be the title search. At a closing, the lender will require a mortgagee’s title insurance policy subject only, as a general rule, to taxes and assessments that are not yet due and payable, prior reservations or conveyances of minerals including oil, gas, sand, and gravel, and certain utility and other easements on a case-by-case basis. If the initial title search is not “clean,” additional legal research will be required to correct the exceptions to title. Such research topics might include heirship and estate issues, adverse possession, and the elements of prescriptive easements, to name but a few. Easement research can prove critical if the only access to the property is by virtue of an easement and not by direct access to a public road. Uncertainty over access will make a commercial real estate deal ineligible for title insurance and financing, thereby killing the deal.

If the real property is located in a PID or other statutorily created area, legal research may be required to identify specific disclosures that need to be included in project documents. By way of example, in the state of Mississippi, a purchase agreement for property located in a PID must contain the following disclosure, boldfaced and in conspicuous type that is larger than the type in the rest of the contract:

THE _____ PUBLIC IMPROVEMENT
DISTRICT MAY IMPOSE AND LEVY
ASSESSMENTS ON THIS PROPERTY. THESE
ASSESSMENTS PAY THE CONSTRUCTION,
OPERATION AND MAINTENANCE COSTS OF
CERTAIN PUBLIC FACILITIES AND SERVICES OF
THE DISTRICT AND ARE SET ANNUALLY BY THE

GOVERNING BOARD OF THE DISTRICT. THESE ASSESSMENTS ARE IN ADDITION TO COUNTY AND OTHER LOCAL GOVERNMENTAL TAXES AND ASSESSMENTS AND ALL OTHER TAXES AND ASSESSMENTS PROVIDED FOR BY LAW.

Miss. Code Ann. 19-35-45. In short, the relevant jurisdiction's real property statutes should always be close at hand throughout the life of a real estate transaction, from the initial purchase through the recording of the last document and thereafter.

If the client has not already done the proper homework on the zoning of the property, legal and non-legal (i.e., political) research will be required. In cases where property must be rezoned for the project to go through, compliance with the legal requirements for rezoning may not be overwhelming, but satisfying the adjacent property owners, concerned citizens, and governmental authorities can be a deal killer. Non-legal research to take the temperature of potential opponents to the zoning change cannot be overlooked. This can be accomplished by polling the neighboring property owners. In some cases, the best approach may be to send out letters and post notices that invite the affected owners to a meeting. Such informal meetings give the client the opportunity to explain the project in a non-legal setting, present projections as to increased traffic, environmental impact, and other potential changes, and answer questions that those affected might have. In addition to polling the adjacent owners, the client will need supporters among the members of the governmental authority or authorities whom are authorized to approve or reject rezoning requests. This may require some networking and nonlegal research to figure out where any political opposition to the project might lie.

Other non-legal research on the front end of a real estate transaction might include the gathering of tax assessment information from the applicable taxing authorities, people searches for existing tenants or third parties whose consents might be required or desirable, and seeking referrals and recommendations so that the right team of engineers, surveyors, environmental consultants, and other service providers is assembled to make the closing happen in an efficient and timely manner. If a real estate broker is involved in the transaction, certain non-legal research such as

TACTICS FOR FACILITATING SUCCESSFUL REAL ESTATE TRANSACTIONS

targeting the correct market for advertising and marketing activities may be performed by the broker, provided these duties are covered in the real estate broker listing agreement.

Document Organization

There is a tremendous volume of real estate, corporate, financing, and other documents that may be included in a commercial real estate transaction. Many of these documents will be negotiated, revised, and exchanged electronically numerous times prior to closing. Particularly when a number of team members are working on the same transaction, it is essential in this age of electronic document exchange that a strict document control system is in place and that every team member is required to adhere to that system.

The Benefits of a Virtual Data Room

In large complex transactions, a virtual data room administered by a third party vendor may be the most desirable document control system. Unfortunately, this service comes with a price tag that is not realistic for the vast majority of transactions. Most transactions can be efficiently administered in-house by setting up a central folder on a computer network that contains every piece of paper related to the transaction (title documents, surveys, architectural drawings, contracts, financing documents and security agreements, correspondence, memoranda, invoices, etc.). A standard coding system that identifies the category of document and the chronological sequence of contract drafts must be established and adhered to by all. As new documents and drafts arrive, they must be promptly stored in electronic format or scanned and stored in the central folder. As morbid as this may sound, the goal for a document control system must be that, even if everyone working on the transaction died, a legal team unrelated to the transaction could nonetheless step in and pick up where the first team left off.

Preparing Documents

The documents that I prepare depend entirely on whom I am representing, the precise type of commercial real estate transaction involved, at what stage I enter into the transaction, and any unique property-specific issues

associated with the land being acquired and/or developed. In general, if I am representing the developer or borrower in the transaction, I will likely prepare the real estate purchase contract if the land has not yet been acquired. In the initial purchase transaction, I may prepare (or the seller's attorney will prepare for my review and comment) release documents to remove existing liens and mortgages, various assignments of easements and other rights, title insurance policy, owner's and contractor's affidavit, FIRPTA affidavit, assumption agreement if the mortgage or deed of trust is to be assumed, closing statement, and other documents typical to the specific type of transaction (e.g., tenant estoppel certificates if a shopping center is being purchased, lease assignments, etc.). As a general rule in the jurisdiction where I practice, the seller's attorney will prepare the deed (warranty, special or quitclaim) and other documents necessary to convey title and grant property rights.

In the development phase of the real estate project, the documents that I prepare as developer's counsel will depend wholly on the type of commercial real estate transaction involved. For example, in a simple office park condominium development, I would work with the developer to craft a Declaration of Covenants, Restrictions and Conditions suited for the particular development and recordable under applicable law. I would prepare formation documents, resolutions, and corporate authority documents for the condominium association and declarant/developer, including bylaws. If there are to be multiple office condominiums in one office park, then I will likely need to prepare a master set of covenants to "umbrella" the entire development.

Representing a Lender

If I am representing the lender in a commercial real estate transaction, the typical list of financing documents that the lender's counsel will be called upon to prepare may include the following: commitment letter, promissory note, loan agreement, mortgage or deed of trust (depending on the jurisdiction), leasehold mortgage (if applicable), security agreement, assignment of rents and leases, other collateral security documents, UCC financing statements, guaranties, estoppel certificates, SNDA (subordination, nondisturbance and attornment agreement), environmental indemnification agreement, form of opinion of borrower's counsel, certifications from various third parties such as the surveyor and architect,

other affidavits and certifications related to property-specific or borrower-specific matters, intercreditor agreement if mezzanine financing is involved, and a closing checklist—the key to making sure that all documents are on track and stay on track until closing. A sample closing checklist for a real estate financing transaction is included as Appendix K. Of all of the foregoing transactional documents, the cornerstone of most commercial real estate financing transactions will be the mortgage or deed of trust.

Because all of the above-listed documents may go through numerous drafts at a rapid pace before a final, execution copy is agreed upon by the parties, it is imperative to establish a strict document control system from beginning to end of any real estate transaction.

Filing Deadlines

Filing deadlines are entirely dependent on what type of transaction is at issue. The mortgage or deed of trust and all other recordable documents should be recorded as soon as possible upon closing of the transaction to avoid intervening lien attachment. Other deadlines may be driven by construction schedules, funding availability or marketing opportunities.

A specific type of real estate transaction with explicit and unforgivable deadlines is the 1031 exchange. The basic deadlines in a traditional 1031 transaction are:

1. The property to be received in exchange must be identified on or before the forty-fifth day after the original property is transferred
2. The 1031 exchange must be completed within the earliest of (x) 180 days of the transfer or (y) the due date for the taxpayer's tax return for the year in which the transfer occurs.

In other words, if the due date for the current year tax return falls before the expiration of the 180-day period, then the exchange must be closed on or before the tax return due date.

Creating New Construction Loans and Real Estate Transactions

Most construction financing is short term and at higher interest rates than permanent financing because of the risk that the construction may not be

completed. I generally advise clients to get bids for a take-out commitment, which is a commitment to “flip” from construction to permanent financing once construction is completed to the lender’s satisfaction and other preconditions to conversion are satisfied. Some of the classic preconditions that many lenders require before a construction loan can be converted to a permanent term loan include, among others:

- Giving the lender thirty days or longer prior written notice of the proposed conversion date
- Substantial completion of the project in accordance with the plans and specifications that were approved by the lender
- Evidence that all costs for labor and materials incurred in the construction have been paid and that no mechanic’s, materialman’s, or other statutory liens have been filed against the project
- Evidence that all insurance policies required by the lender are in full force and effect
- Satisfaction of certain financial covenants established by the lender such as achievement for a certain number of consecutive months of a specific debt service coverage ratio
- Achievement of occupancy percentages set by the lender (typically seen, for example, in apartment complex projects and retail shopping center projects) at projected rental rates
- Providing the lender with endorsements to the mortgagee’s title insurance policy
- Payment or reimbursement for all the lender’s expenses and costs, including attorneys’ fees and disbursements
- No defaults under the existing loan documents
- The lender’s inspecting architect must have issued a Certificate of Completion
- Delivery of a permanent certificate of occupancy from all necessary governmental authorities
- Receipt of a final as-built survey for the project acceptable to the lender and the title insurance company, which shows the total square footage and dimensions, access to the property, the location of all improvements, boundaries, encroachments, setback lines, rights of ways and easements

TACTICS FOR FACILITATING SUCCESSFUL REAL ESTATE TRANSACTIONS

Wrapping the construction and permanent financing into one loan agreement and one closing can often save costs for the client.

Steps to Success in New Construction Loans and Real Estate Transactions

Apart from the normal real estate acquisition steps (i.e., confirm good title, confirm proper zoning, obtain an environmental audit, have a survey completed, etc.), a fundamental step is to make sure that the plans and specifications are complete, comply with all local building codes, zoning ordinances and other local restrictions, and are satisfactory to the lender. The plans and specifications will typically be incorporated into the construction contract, which, in many cases, will be based on the American Institute of Architects (AIA) form. The construction loan cannot close, until the construction contract and plans and specifications are final and approved by the lender or the lender's architect.

The client will need to pick the contractor with care and ensure that the contractor is financially viable and able to complete the work on time. The lender will likely require payment and performance bonds, which the client should, in turn, require of the contractor.

Other construction issues that the client needs to consider and include in the construction contract are retention amounts, requirements that the contractor carry sufficient liability and builder's risk insurance that covers both the contractor and client, and covenants by the contractor to comply with all applicable laws including, for example, permitting and building inspection ordinances, environmental laws, and state and federal safety rules.

Working with Third Parties

The key people involved in construction loans and real estate transactions are the borrower's architect and contractor, and the lender's inspecting architect. On smaller loans, some lenders will permit the borrower's architect to certify to the lender when construction milestones are completed. On large construction loans, lenders generally will insist on hiring their own architect or construction expert to inspect the work and

either approve it or report on any corrections needed before a construction draw can be funded.

The contractor is responsible for completing the work according to the plans and specifications and for hitting construction milestones in accordance with the construction contract in a timely and professional manner. The borrower's architect will supervise and ensure that the project is being completed according to the plans and specifications that were approved by the lender. The borrower's architect will sign off on the work as it is completed and coordinate the timing of inspections that are conducted by the lender's inspecting architect.

When working with architects and contractors, it is imperative that the client stay on top of the construction progress. A good approach on some jobs is for the client to name a point person within the client's organization, preferably someone with construction and/or architectural experience. This point person (or "owner's representative" under the typical AIA construction contract) will need to visit the site on a regular basis with the architect and the contractor's project manager in order to identify any problems before it is too late in the game to correct errors or make changes. Variations in the plans and specifications will need to be reported to and approved by the lender and its inspecting architect.

Representing Clients Selling to Commercial Developers

When representing a client selling to a commercial developer, I try to help the client to focus on issues often associated with the sale of raw land. The key issues for a client selling "raw land" to a commercial developer typically will be providing clean title, making sure there are no access problems, making it clear that the client provides no environmental representations or indemnities and no representations as to the property's suitability for any specific purpose, and settling on a price that is at least as good as recent, comparable sales in the area. All of these items, and others peculiar to the property, should be handled in the sales contract. Any restrictions that are to run with the land should be expressly included in the sales contract, and the buyer should acknowledge in the sales contract that the restrictions would be included in the deed or other document of conveyance.

TACTICS FOR FACILITATING SUCCESSFUL REAL ESTATE TRANSACTIONS

I negotiate as many or as few selling terms for my client as the client desires. However, the client always has the final say on the entire package and, without exception, on price. Much depends on the sophistication of the client and sometimes on the time that the client has to invest in negotiating terms without lawyer assistance. I most always find it preferable to draft the sales agreement myself rather than have the client use a broker's form. For expediency and to save costs, many clients want to use a real estate broker's contract rather than pay an attorney to do the drafting. In some cases, the form contract will suffice. However, in deals that have unique aspects such as peculiar deadlines, financing requirements, and inspection or environmental issues, a custom-drafted contract can save money and alleviate arguments on the back end.

The Components of the Sales Agreement

The sales agreement includes some basic provisions that are part of every sales agreement. These include the parties' names and legal status, property description, title requirements, purchase price, deposit requirements, payment requirements, various inspections and the time frame to complete them, disclosures legally necessary or advisable, the allocation of closing costs (including recording fees), proration of taxes, default remedies, and closing requirements such as deadlines, time, and place.

Each deal may require variations on those basic provisions or may also require tailor-made provisions applicable to that specific transaction. For example, with respect to the purchase price, the price may be fixed, it may be a price per acre subject to a final survey of the property, or it may depend on the number of units eventually allowed under a sought-after zoning change. The price per acre may vary depending on the topography of the land (i.e., flood plain land would be sold at a lesser price per acre), or the price can vary depending on when parcels from a large tract of land are released to the seller, if the takeout of parcels is scheduled over a period of time.

If the seller is retaining portions of the adjacent or surrounding property, then the seller may wish to include in the purchase contract reasonable restrictions on the use or development of the sold property. Such restrictions also should be included in recorded covenants that govern the

use of a defined area of land. Any such restrictions will need to pass legal muster under local law and should be reviewed carefully. As a general rule, courts “favor free and unobstructed use of real property.” *Kinchen v. Layton*, 457 So.2d 343, 345 (Miss. 1984). Nonetheless, clearly and unambiguously drafted covenants may be enforced; ambiguously drafted covenants will be subject to a court’s strict scrutiny and will be construed against the person seeking enforcement of the covenant. *Id.* (prefabricated home that was mounted on masonry piers was not a “temporary structure” prohibited by restrictive land-use covenants on the real property).

The Role of Commercial Lenders

As a lawyer, I am governed by the rules of professional responsibility, which require that I deal directly with the lender’s lawyer and not directly with the bank officer in charge. That is not to say that I never speak to the lender. All-hands meetings and conference calls, where the lender and its counsel are present, are often helpful and necessary in moving a deal along. As a general rule, I try to keep good lines of communication open with lender’s counsel at all times. The use of e-mail has certainly improved the ability to communicate with opposing counsel rapidly and has eliminated many problems associated with phone tag in the past.

Lenders and Structuring the Transaction

Lenders will always have the final say on the transaction’s structure, particularly from the standpoint of what collateral must be pledged and from whom, what personal and/or corporate guaranties will be required, whether special purpose entities (SPEs) will need to be formed and how, and with respect to funding amounts and timing. Simply put, if a lender is not comfortable with the structure of the transaction, the deal is dead.

Recently enacted financial reform legislation is expected by some to have a negative impact on lending to commercial real estate markets. The Dodd-Frank Wall Street Reform and Consumer Protection Act, signed by President Obama on July 21, 2010 as Public Law No: 111-203, has been described as the most sweeping regulation of financial services in this country since the New Deal Programs were enacted in response to the Great Depression. Even though the Dodd-Frank Act arguably has a more

TACTICS FOR FACILITATING SUCCESSFUL REAL ESTATE TRANSACTIONS

direct and immediate impact on consumer mortgage financing (by virtue of the creation of the Consumer Financial Protection Bureau) than on commercial real estate transactions, financial reform has tightened capital and compliance requirements on banks, which, in turn, has slowed the underwriting process for commercial lending and made the process more onerous for potential borrowers. Additionally, Dodd-Frank has imposed greater disclosure requirements on issuers of commercial mortgage-backed securities and further has required that issuers retain no less than a 5 percent unhedged economic interest in the securitized assets that they transfer. Some observers expect these added layers of regulation to contribute to an even more restrictive commercial lending market than what we currently have.

Whether or not the cause is directly or indirectly attributable to Dodd-Frank, commercial real estate lenders are proceeding cautiously and are “kicking the tires” more thoroughly than in past years. In some areas, the process has slowed to a standstill. The general rule of thumb now is that a borrower/developer must present to the lender thorough project plans, budgets, and analyses in order to win approval from the typical loan committee or investor group.

Organizing Commercial Real Estate Documents

Document drafts for commercial real estate transactions are generated in electronic format and then distributed by e-mail to all parties involved for review and comment. Once all comments are received and discussed with the client, new drafts are generated and distributed in “clean” and “black lined” versions, which show all changes from the prior drafts. This process will continue until final, execution copies are agreed upon.

The basic information needed to begin drafting real estate transaction documents includes true and correct names and addresses of the parties involved, corporate formation information, all information needed to prepare statutorily correct notarial acknowledgments in the relevant jurisdiction (e.g., in Mississippi, one must know whether limited liability companies are member-managed or manager-managed), proper legal descriptions, an accurate survey, a current title report with copies of the documents listed in the report, a zoning letter to confirm zoning

representations, and any deal-specific information required for a particular transaction. In the drafting of bank documents, the lawyer needs the signed loan commitment in order to commence document preparation.

The primary challenge involved in real estate transactions is usually timing. Parties generally wish to close yesterday. Clean title, access, zoning, and permitting issues can slow down the process tremendously. These types of problems are overcome with patience, hard work, and sometimes, luck.

Tax Considerations and Closings

Some of the basic tax considerations are the recognition of gain or loss and opportunities to defer gain. A Section 1031 like-kind exchange, mentioned above, is a common vehicle for avoiding the recognition of gain in a real estate transaction. Other tax driven opportunities should be considered such as GO Zone bond financing and other tax incentives, which became available in the states of Louisiana, Mississippi, and Alabama after the devastation of Hurricanes Katrina and Rita in 2005. Congress recently extended, and President Obama signed into law, certain GO Zone tax incentives, which were originally enacted following the devastation of Hurricanes Katrina and Rita on the Gulf Coast in 2005. The centerpiece of the hurricane relief contained in the Gulf Opportunity Zone Act of 2005 (Public Law No: 109-135) was a package of tax incentives designed to help revitalize and rebuild the areas hardest hit (aka "the GO Zone") by Hurricanes Katrina and Rita. The federal tax benefits that were made available to businesses under the GO Zone legislation included 50 percent bonus first-year depreciation, a nearly doubled Code Section 179 expensing allowance, partial expensing of demolition and cleanup costs, a five-year-NOL carryback, and increased rehabilitation tax credits.

Approaching Complex Tax Issues and Closing Commercial Real Estate Loans

Because I am not a tax lawyer, I often work with the client's accountant to ensure that a transaction is structured in a tax efficient manner that complies with the accountant's overall goals for the particular client. Certain transactions may be dependent on Internal Revenue Code (the Code) provisions, such as low-income housing projects under Section 42 of the Code or the rehabilitation of certified historic structures under Code

TACTICS FOR FACILITATING SUCCESSFUL REAL ESTATE TRANSACTIONS

Section 47, and will require the hands-on involvement of the client's tax accountant or advisor. The tax professional will be called upon to render tax compliance certifications to the lender and investors and to fulfill reporting requirements to the IRS.

In every commercial real estate financing transaction, I always create a closing checklist from the very beginning of the transaction so that each party knows what everyone is required to bring to the table and when. The closing checklist can often be the most important document in the transaction.

Construction, Permanent, and Mezzanine Loans

All parties including the developer, lender, contractor, architect, and lawyers, must work together on a strict timetable when working to create a successful construction loan. They must also be flexible enough to deal with unique problems as they arise, and timing is key. Weather is the classic and uncontrollable variable that can play havoc with the best-planned construction schedules. Labor and supply shortages (e.g., sheetrock shortage during the building boom of 2004 to 2006, which lead to the Chinese drywall problems being litigated today) also can cause deviations from the schedule. Construction and development projects must be properly permitted, and approvals from governmental authorities often take longer to obtain than anticipated.

Construction and permanent financing may be wrapped into one takeout commitment. If structured in this manner, the flip to permanent financing should not require a "second" closing but can be streamlined to satisfying the lender that completion requirements have been met. With respect to mezzanine financing, such loans are typically large loans that are highly paperwork intensive and primarily seen on larger projects. Mezzanine loans are supplementary financing and are analogous to second mortgages, but the collateral for the mezzanine loan is the equity ownership interests (stock or limited liability company membership interests) of the owner of the real property rather than the property itself. Organized due diligence and document control is key when closing a mezzanine loan as part of a real estate financing transaction.

Conclusion

Since being struck by the financial crisis that spawned legislation such as Dodd-Frank, the commercial real estate market has gone through a serious decline; experts are now arguing over whether we have seen the bottom or whether further decline is in store. In our practice, we have seen some recent increase in activity, but I think it is fair to say that, in the first quarter of 2011, the commercial real estate market remains anemic. While there are some signs that fuel optimism such as statistics that show an increase in Real Estate Investment Trust (REIT) annual returns and some perceived easing in the underwriting standards for commercial loans, there still are difficult problems on the horizon. Primary among these concerns is the spike in commercial real estate debt maturities that is predicted to be in the \$350 billion range from 2011 through 2013. *See* testimony of Matthew J. Anderson, Managing Director of Foresight Analytics, before the Congressional Oversight Panel Hearing on Commercial Real Estate's Impact on Bank Stability, Washington, D.C. (Feb. 4, 2011) (website links for oral testimony and written research: <http://cop.senate.gov/documents/testimony-020411-anderson.pdf>; <http://cop.senate.gov/documents/testimony-020411-anderson-oral.pdf>)

There is no question that we still have difficult times ahead. The best advice to transactional real estate practitioners might be simply to remain patient—depressed prices should eventually translate into increased activity, including an increase in foreign investment. In the meantime, dirt lawyers who find themselves absent from the closing table can always bone up on foreclosure and workout skills, which, in these difficult financial times, seem likely to remain in demand.

Key Takeaways

- Complete the necessary legal and non-legal zoning research on properties if the client has not already done so.
- Consider using a virtual data room administered by a third party vendor in order to organize large complex transactions.
- Keep in mind that the client always has the final say on the entire package, even when the lawyer conducts the negotiations.

TACTICS FOR FACILITATING SUCCESSFUL REAL ESTATE TRANSACTIONS

- Collaborate with financial advisors if you are dealing with complicated tax issues that you are not familiar with in order to ensure that the real estate transaction is financially secure and proper.
- Make sure that lines of communication with lenders are open and healthy so that you and your client will be more likely to have successful transactions.

Related Resources

- American Bankers Association Dodd-Frank Tracker:
<http://regreformtracker.aba.com/p/dodd-frank-tracker-topics-list.html>
- Gulf Opportunity Zone Bonds, IRC ' 1400N(a):
<http://www.irs.gov/taxexemptbond/article/0,,id=155664,00.html>

Jane B. Morgan is a member of Watkins & Eager PLLC in Jackson, Mississippi. After graduating with honors from the Georgetown University Law Center, she served as law clerk to the Honorable E. Grady Jolly of the United States Fifth Circuit Court of Appeals. Ms. Morgan was admitted to the bars of Pennsylvania, the District of Columbia, New York, Louisiana, and Mississippi, and now practices exclusively in Mississippi. Ms. Morgan regularly serves as Mississippi counsel and local opinion counsel in complex transactions that involve Mississippi real estate. Ms. Morgan has been named a "Mid-South Super Lawyer" and has received Martindale-Hubbell's "AV" peer rating.