

The Plain & Simple

November 2006

Real Estate Business Law

Volume II

A hole for the borrower in a portfolio loan

Whenever you negotiate a portfolio loan the lender's customary form says that a default pertaining to "any" property will trigger a default under the overall loan. However, this is not good for the borrower. Possibly there is a portfolio with, say, 40, properties; a problem with a single property should not bring down the house of cards (says the borrower) and, of course, the lender does not want to give the borrower impunity to have property level violations occur without downside.

Several possible compromises are as follows: (i) the borrower and the lender could agree on a concept that if property-level defaults occur for properties constituting more than, say, 5%, of the overall collateral then that constitutes a default (but if the defaults are less than that, then the property-level defaults are not loan defaults; (ii) the borrower and the lender could agree that if a property-level default occurs for a single property then the interest rate kicks upwards until the default is cured but it does not trigger a loan default, or (iii) our preferred compromise, which allows the borrower to cure by purchasing the property out of the portfolio and making a required allocated loan paydown (note that you want to attempt to negotiate this "without" prepayment penalty, if applicable). Our view is that the foregoing compromises give the borrower some reasonable protection without putting the lender unreasonably at risk.

A hole for the tenant in a long-term lease

Did you ever see a lease with, say, a 50 year term and a ten year renewal right thereafter. Did you ever wonder who would be alive to remember to renew the lease? Did you think about the lease being unfair to the tenant when it provides that if the tenant forgets then it forfeits its entire estate and presumably grants an enormous unbargained-for windfall to the landlord?

There is a way to solve this problem and make the lease fair to both parties. That is to insert into the lease the concept of a "reminder notice". This means that when both the landlord and the tenant fall asleep on the clause in 50 years the first one to wake up effectively reminds the other of the renewal obligation. If it is the tenant that wakes up first, then the tenant merely sends the renewal notice and if it is late the landlord cannot object if it was sleeping too. If it is the landlord that wakes up first, then the landlord has to send the tenant a reminder of, say, 60, days and if the tenant fails to renew in that time period then the tenant forfeits its rights.

We think the foregoing is "fair" as no one is penalized if they forget something that is pretty hard to remember - something very far in the future.

Firm Facts

Terri Adler (co-chair of the real estate department) gave birth to a baby boy last month- Aaron Adler Goldstein was 7 pounds 2 ounces.

Please contact Caitlin Velez at (212) 672-3747 or newsletter@dslip.com with any questions or comments.

