

The Plain & Simple

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The small (but quite worrisome) sale of a small parcel of land out of a bigger parcel

Did you ever have a situation in which you own Blackacre – which is an office building with, say, 50 acres appurtenant to it – you paid \$100,000,000 for the property overall and you are planning to sell off the land for about \$3,000,000. Possibly, your instinct is not to worry about it too much – after all, it is a tiny little deal compared to the big deal – maybe just gravy. Maybe you even had one law firm (your main law firm) do the “big” deal and you plan to use a local solo practitioner for the sale of the land. After all, what could go wrong? Well, here are a few things: First, do you have a lawful subdivision – if not, you are selling something you can’t sell and, worse yet, once you sign a contract without a way to get out of it you have now tied up your \$100,000,000 deal into a mess. Second, did someone check your loan documents on the “big” deal – is lender’s consent required? It would be a bad day if you need lender’s consent to release the land parcel and cannot get it – worse yet if the loan is securitized or in a REMIC. Third, do any of the leases in your office building give any of the tenants rights over the vacant land – e.g., parking, access roads, etc.? If so, you are probably breaching your leases unless you deal with this. Fourth, do you need a reciprocal easement agreement – it would be a truly awful thing to realize after you sold the parcel that you need access to it for your office building. There are other transaction-specific issues as well; however, the big point here is that a “small” sale can cause you “big” problems if you are not aware of the complexities.

Possibly the worst issue in a ground lease

Ground leases are tricky enough. However, possibly the toughest issue to grapple with arises when there is land plus a pre-existing building thereon that is leased to a tenant under a long-term ground lease with leasehold mortgage financing. What happens to the insurance proceeds if the building burns down and, at the same time, the leasehold mortgage is in default? The leasehold lender will insist that the proceeds must go to the lender to pay down its leasehold mortgage because its loan is in default. The landlord will say, “No way! The proceeds must go to an escrowee to be used for restoration of the building.” So what should happen? Well, ultimately, there just may not be a great answer here. Securitized lenders may flat out refuse to permit the proceeds to be used for restoration if the loan is in default; other lenders (banks, for example) might reluctantly agree to live with this result, but will not like it and may insist on holdbacks or additional guarantees. Ultimately, if you are the tenant (ground lessee) in this situation, you need to either win the point (that the insurance proceeds go to your leasehold lender) or recognize that the financeability of your leasehold interest will be impaired for some lenders and blocked for others.

Firm Facts

Duval & Stachenfeld LLP will be celebrating its 10th anniversary in October of this year.

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

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