

## BUYING PROPERTY AT **FORECLOSURE SALES:** WHAT YOU SHOULD KNOW

by *Stuart Gold*



With the increase in mortgage default rates, an increased number of foreclosure sales in New Jersey are likely this year. Foreclosure sales often provide an opportunity for an investor with available cash to purchase property at below market prices and to see their investments increase in value when the market rebounds. However, there are various roadblocks and risks that one should consider before investing in foreclosed properties.

### WHEN DOES PROPERTY BECOME AVAILABLE FOR SALE?

The foreclosure sale is the last step in the foreclosure process and does not occur until the property owner has exhausted all other avenues, such as workouts, state court

litigation and, quite often, bankruptcy. The foreclosure process begins with the filing of a complaint by the lender. The property owner may contest the proceedings or allow the foreclosure to proceed by default. Eventually the lender obtains a judgment of foreclosure and a writ of execution directing the sheriff to sell the property at public auction.

There are alternatives to buying distressed property. Some lenders will sell defaulted loans at a discount. The purchaser of the loan then incurs the risks, delay and expense of litigating with the property owner.

One can also purchase distressed property on a "short sale" if the lender is willing to discount its loan. The primary disadvantage to the short sale is that the purchaser buys subject to all other liens and encumbrances.

*(Continued on pg. 2)*



## CONTENTS

Buying Property at Foreclosure Sales: What You Should Know	1
Commercial Auto Insurance Policies: The Elimination of Step-down Clauses	3
The Intellectual Property Inventory: Critical in Protecting a Company's Assets	4
The Eminent Domain Process	5
Limited Liability Loans May Not Always Be So Limited	6
Court Reverses Construction Lien Claim Filed Against Landlord's Property	7
Closing Costs and Adjustments: To Know Them Is to Budget for Them	8

# BUYING PROPERTY AT FORECLOSURE SALES: WHAT YOU SHOULD KNOW *(Continued from pg. 1)*

## WHEN AND WHERE WILL THE SALE TAKE PLACE?

The Sheriff advertises the sale in a local newspaper four times starting at least 21 days in advance. Most sales take place at the county courthouse. The property owner has the right to two, fourteen-day adjournments, which are usually requested. The property owner may also file a bankruptcy petition shortly before the sale, which stays the sale until the lender gets relief from the Bankruptcy Court.

## HOW TO FIND OUT ABOUT PROPERTIES IN FORECLOSURE

The most common way to learn about foreclosure sales is through the advertisements in local newspapers. There are also Internet services, such as:

[foreclosurefreesearch.com](http://foreclosurefreesearch.com)  
[bankforeclosuressale.com](http://bankforeclosuressale.com)  
[sheriffsonline.com](http://sheriffsonline.com)

which provide information about foreclosures. Some of the basic information is free, but there is often a charge for detailed information about the properties.

You may also find out about foreclosure properties by contacting the workout department of a bank.

## HOW IS THE SALE CONDUCTED?

The sale is conducted by public auction. The lender has the right to credit bid its judgment and is often the successful bidder. However, there is an opportunity for a third party bidder to win the auction if the judgment amount is considerably less than the property's market value or if the lender is more interested in cash than in the property. The successful bidder must leave a 20% deposit immediately upon the conclusion of the auction. Failure to provide the deposit, or to pay the purchase price, will result in another auction and the defaulting purchaser will be liable for any difference in price.

Foreclosure sales are governed by the rule of *caveat emptor*. The sale is made without any warranties or representations as to conditions and the property is

purchased "as is." Rarely is there an opportunity to inspect the property prior to sale, making it difficult to evaluate physical or environmental conditions.

## HOW DOES THE PURCHASER GET TITLE?

Even after the auction, the property owner has 10 days to redeem the property by paying the full amount of the judgment to the sheriff. If the property owner redeems, the sheriff returns the deposit. The redemption period may be extended by the court for good cause, usually because the property owner has found either a buyer or a new lender. The property owner may also extend the redemption period for an additional 60 days by filing a bankruptcy petition before the 10-day redemption period expires.

Once the redemption period expires, the sheriff will issue a deed to the successful bidder upon payment of the balance due. From a title perspective, the judgment of foreclosure will eliminate all

junior liens and encumbrances that were included in the foreclosure complaint, so title insurance is usually available. It is the successful bidder's obligation to record the deed and pay the transfer fees.

## HOW TO GET POSSESSION OF THE PROPERTY

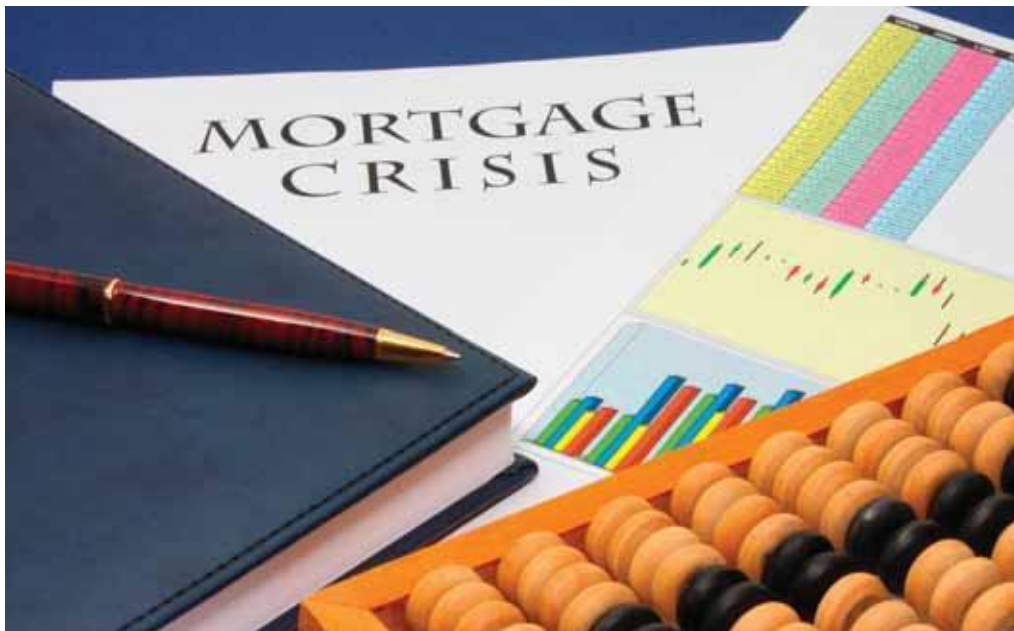
If the property is vacant, or the property owner is cooperative, possession can be taken by simply changing the locks. More likely, however, a writ of possession from the Superior Court will be required and the sheriff will have to execute on the writ. However, the court may delay execution if the property owner is having difficulty finding a new place to live.

## WHAT ABOUT TENANTS?

Tenancies are not affected by the foreclosure unless the tenants are named as defendants to the foreclosure action. As a practical matter, only commercial tenants may be affected by a foreclosure. Residential tenants who are protected by the Anti-Eviction Act cannot be removed from the property by means of foreclosure. The purchaser is entitled to the rents that accrue after the sheriff delivers the deed and the former property owner is required to turn over any security deposits, with interest, to the purchaser within five days of the delivery of the deed.

For those who have the financial ability to make an all cash purchase, and can accept the risks of buying a property without extensive due diligence, then foreclosure sales may provide a viable opportunity.

*Stuart Gold is a partner in the firm with substantial experience in bankruptcy and complex commercial litigation.*



# COMMERCIAL AUTO INSURANCE POLICIES:

## *The Elimination of Step-down Clauses*



by Joseph J. Peters & Justin S. Black

In the fall of 2007, the New Jersey Legislature amended automobile coverage policies to prohibit the use of step-down clauses in commercial auto insurance policies only. No longer can these policies “provide less uninsured or underinsured motorist coverage for an individual employed by the corporate or business entity than the coverage provided to the named insured under the policy.”

By law, insurance companies that underwrite policies in New Jersey are required to offer uninsured motorist (UM) coverage to compensate an insured for injuries and losses that occur from uninsured drivers. Additionally, an insured can make a claim for underinsured motorist (UIM) coverage if the individual meets three criteria. He or she (1) has UIM coverage; (2) has suffered losses for which another person is responsible and such losses exceed the responsible party’s liability coverage; and (3) the insured’s own UIM coverage is greater than the limits of liability available to the responsible party against whom recovery is sought.

### STEP-DOWN CLAUSES

Prior to September 10, 2007, New Jersey law permitted vehicle insurers that wrote these policies in the State of New Jersey to employ “step-down” clauses in their policies. A “step-down” provision allows the employee’s UM or UIM coverage on his own personal auto insurance policy to “kick in” instead of the employer’s vehicle insurance policy even if the employee is engaged in the employer’s business at the time of the vehicular accident. This occurred with commercial policies because employers/owners want to provide some protection to their employees, but do not want to spend too much money on that coverage.

Consequently, business owners could choose to have a higher level of UM/UIM insurance for themselves, and a reduced level for employees who drove company vehicles. Such “step-down”

provisions only minimally protected employees if they were injured in a UM or UIM accident while using a company vehicle. The employee’s recovery would likely be significantly less than that of his or her employer in the same accident.

### THE NEW STATUTE

In the fall of 2007, the New Jersey Legislature amended automobile coverage policies to prohibit the use of step-down clauses in **commercial auto insurance policies only**. No longer can these policies “**provide less uninsured or underinsured motorist coverage for an individual employed by the corporate or business entity than the coverage provided to the named insured under the policy.**”

The statute further states: “A policy that names a corporate or business entity as a named insured shall be deemed to provide the maximum uninsured or underinsured motorist coverage available under the policy to an individual employed by the corporate or business entity, regardless of whether the individual is an additional named insured under that policy or is a named insured or is covered under any other policy providing uninsured or underinsured motorist coverage.”

### IMPACT OF THE CHANGE

Now employers must have the same UM or UIM coverage for both themselves and their employees at an extra cost. Since employers generally desire a high amount for themselves, the effect of the new law will be to increase the value of the policy limit available to employees as well. Increasing the policy limits will then result in higher premiums to the owners, and such increases could be substantial if there are a large number of employee drivers. Thus, while employees will be better off because of the changes that are made, employers will still only be getting the same coverage for themselves while having to pay out more in premiums to cover their employees at the same limits.

### WHAT SHOULD EMPLOYERS DO?

In light of the new law, employers/owners should carefully review their present commercial auto insurance policies to ensure they have enough UM/UIM coverage for themselves. In addition, they should balance their coverage needs with the costs of increased UM/UIM coverage for employees, especially if they have a fleet of vehicles under a commercial policy.

*Joseph J. Peters is a partner in the firm with litigation experience in many areas of law. Justin S. Black is an associate in the firm’s Litigation Department.*





# The Intellectual Property Inventory: Critical in Protecting a Company's Assets

by Gary S. Poplaski



Taking an inventory of Intellectual Property (IP) and then determining its valuation is essential to assessing a business entity's assets and protecting its operations. In most corporations, as much as 70% of the total market value of the corporation is derived from intangible assets, particularly in technology-based companies where IP assets can be their most important assets.

An IP Inventory can be especially difficult to conduct; particularly when the company to be inventoried has ancillary business entities. Nonetheless, when a company conducts an IP inventory, the broad areas that require examination include:

- Pending and existing Patents and Inventions;
- Works of Authorship, such as videos, books, manuals, plans, specifications, and software;
- Business processes, trade secrets, and other proprietary information; and
- Brands, trademarks, service marks, and trade names.

## HOW TO INVENTORY

The first step to conducting an IP Inventory is to create a list of the existing IP assets broken down into categories, like those above. The initial inventory in most cases will not be complete, largely because IP assets take many different forms, and may not be apparent at first glance. In addition to the list, it is prudent to implement other methods, including researching the U.S. Patent and Trademark Office website to determine the status of applications and ownership, conducting Internet searches to see if others are using the marks and names, and interviewing company personnel, from the executive ranks down through first line management, including research and development personnel to identify specific "works in progress" that may eventually ripen into IP assets.

The individuals conducting the search may also wish to develop and disseminate an IP asset questionnaire to all pertinent personnel to help facilitate the process.

Questionnaires and/or interviews of company personnel are crucial and they should focus on processes and procedures that are commonly implemented and followed in the normal course of business, because they may themselves be trade secrets and part of the IP of the company.

## NEXT STEPS

Once the investigatory process is completed, the initial inventory should include:

- A list of all existing patents with expiration dates, and pending patent applications;
- A list of all trademark registrations with renewal/maintenance fee dates, and pending applications; and
- A copy of form consulting and non-disclosure agreements.

After this list is compiled, research must be conducted to insure that all of the identified IP assets are still actively protected under current law. Patents and trademarks must be searched to insure that they have not expired and it must also be determined that all applicable maintenance fees that are due in periodic increments to the U.S. Patent and Trademark Office have been paid or are appropriately calendared to be paid when due. It is also crucial to ensure that any patent protection registered in foreign countries through the Patent Cooperation Treaty, or trademark registrations registered in foreign countries, are up to date with any required maintenance fees or renewals.

If the company's products include copyrightable material, such as software or books, it is critical to know whether the copyright for such works has been registered and to insure that confidentiality and non-disclosure agreements are in place with the authors of those works under the "Work for Hire" doctrine, so that ownership rests solely with the company.

If the company also possesses proprietary information or trade secrets, it is important to ensure that employees and consultants have signed non-disclosure confidentiality agreements and intellectual property assignment agreements to assure that their works have also been assigned to the company through the "Work for Hire" doctrine.

## INTERNAL CONSIDERATIONS

Once all IP assets have been identified, it is important to determine whether adequate agreements exist between the separate business entities to insure that any of the intellectual property assets that are being used by a business entity are being used properly and lawfully. For example, if one business entity is using a specific trademark that may be owned by another business entity or the parent, it must be determined that there is an agreement between the entities to allow that specific entity to use that IP asset.

## TAKING ACTION AGAINST INFRINGEMENT

After that process is complete, the company may then begin to research for potential infringement of its IP assets. Potential infringers should receive cease and desist letters and the company should seek to obtain licensing revenue for those assets from the infringing parties. The result could potentially be a large windfall in licensing fees if the company has a wide based IP asset pool.

## REMAINING DILIGENT

Finally, a plan must be implemented to continually audit and monitor the IP assets of the company and to include IP assets that are created in the future. All future IP assets must be added to the inventory on an ongoing basis and appropriately maintained.

*Gary S. Poplaski is an associate in the firm's Intellectual Property and Commercial Real Estate Departments.*

# The Eminent Domain Process

by Avrom J. Gold



“Eminent domain is the rightful authority which exists in every government to control rights of a public nature, which pertain to its citizens in common, and to appropriate and control property, for public benefit as public safety, necessity, convenience, or welfare may demand.”

Most landowners never have to deal with a governmental entity when it exercises its power of eminent domain and condemns property. However, in those situations where a landowner refuses to sell his property voluntarily, the government can condemn it. Of course, the validity of the condemnation process depends upon the manner in which the property is to be used after it is taken for a “public purpose.” It’s easy for the state to establish a public use if a park, a school or a road is the intended use; but simply to give the property or resell it to another citizen to use for private purposes is confiscatory and prohibited.

## WHAT’S FAIR IS FAIR

But all is not lost, because the Constitution proclaims that “Private property shall not be taken for public use without just compensation.” If the use is truly public, the condemning agency must pay “just compensation.” What is “just compensation?” Who says how much is just? How does the state prove it?

Here is the way the process works. First, the condemning body has the statutory duty to negotiate with the landowner in a *bona fide* manner to purchase the property. “Just compensation” is generally equated with “fair market value” – what a willing buyer will pay to a willing seller when neither is compelled to buy or sell. The evidence of fair market value is presented by appraisers based upon a review of comparable sales and other market data.

Only if the amount that it offers is not accepted by the landowner can the authority condemn the property, which means simply, to take it without permission. The state will first decide how much of the property it needs. It may take all or a portion. It may take it in fee (ownership) or as an easement to use it, which can be temporary or permanent. The type of taking – partial or total – and whether it is temporary or permanent, will dictate how much the government will have to pay. If the taking is only partial, then any diminution of value to the remainder of the property not taken is also considered in the compensation formula.

## APPRAISER PLAYS ROLE

The state, for example, may decide to condemn a commercial property to widen a highway, which may require using a portion of the property’s parking area utilized by tenants and their customers. The state will hire an appraiser to value the property to be taken and any diminution in value to the remainder. The appraiser will render a detailed report with an opinion as to the “fair market value.” The appraiser’s opinion can be based on a variety of factors, including sales of comparable properties, the capitalized net income derived from a market analysis of rentals of similar buildings, the replacement cost of the structure plus the value of the land or a combination of all those methods. If the taking affects the remainder, the appraiser will place a value on that as well. The state will provide the owner with a copy of the appraisal and will generally offer to pay the amount indicated.

The owner, in turn, can either accept or reject the offer. The state may engage in negotiations or start a condemnation action. In the case of the latter, it will file a complaint, issue a declaration of taking and deposit the full amount of its offer with the Clerk of the New Jersey Superior Court. At that time, the state becomes the owner of the property. The owner can withdraw the money from the court while the condemnation action is pending, without penalty and without prejudice. The court will appoint three commissioners before whom the state must make its case as to value while the owner can make its case as to a higher value. The commissioners’ decision is final only if both sides agree to accept it. If one party does not, an appeal may be taken to the court, where a trial will be held, with or without a jury, depending upon the owner’s preference. Again, testimony is taken and the judge or jury makes the decision, which may be appealed to an appellate court.

## RECENT COURT RULING IMPACTS PROCEEDINGS

In a recent New Jersey appellate court ruling, the landowner’s rights to recover attorney’s fees in condemnation cases were more clearly defined. In *West Orange v. 769 Associates, LLC*, the landowner fought the taking of the property all the way to the New Jersey State Supreme Court in an effort to block the taking of its office building to construct a road. When the court decided the taking was supported by a legitimate public purpose, the landowner and West Orange negotiated an agreement on fair market value. The municipality then dropped the condemnation case.

The landowner subsequently petitioned the court for an award of attorney’s fees under the statute. The basis for the petition was that West Orange abandoned the condemnation action. In agreeing with the landowner and awarding \$145,825 in attorney’s fees, the Appellate Division held that unlike most fee shifting statutes, the condemnation law does not require the landowner to show that it was the “prevailing party” but only that the public entity abandoned the condemnation action.

The valuation of real estate is a matter of expertise, and owners faced with condemnation proceedings should never attempt to negotiate with a public body in an eminent domain matter without the assistance of counsel and a certified New Jersey appraiser.

*Avrom J. Gold is one of the founding members of the firm and has represented clients in all types of commercial disputes.*



# Limited Liability Loans May Not Always Be So Limited

by Robin E Lewis



When shopping around for a real estate loan, many knowledgeable borrowers prefer to deal with lenders who offer “non-recourse” financing rather than loans that require personal guarantees.

A non-recourse loan is one in which the lender’s sole recourse if a borrower defaults is to the mortgaged property and not to the other assets of the property owner or guarantor. Under the usual non-recourse scenario, if a borrower defaults, the lender’s only option is to foreclose and take back the property. In contrast, with a more traditional loan backed by guaranties, the lender can look to the guarantors for payment of the loan immediately upon a borrower’s default, and is not required to start a foreclosure action before seeking to collect from the loan guarantors.

## NOT FOR EVERYONE

Non-recourse loans are not for everyone. It is important that borrowers understand how a non-recourse loan works and how, in some cases, the limited liability that such a loan provides is not always applicable. Non-recourse loans are often offered by lenders who sell them, grouped into a portfolio of many loans, on the secondary loan market. These are known as “securitized” or “conduit” loans. The underwriting criteria and documentation requirements for these types of loans are strict and often make it difficult for borrowers to qualify for a securitized loan.

While the rates are often more favorable than those offered by local commercial or savings banks, the additional requirements and costs in the application process, closing and maintenance of such loans may discourage many borrowers from taking a non-recourse loan.

## NOT WITHOUT RISK

Even a non-recourse loan, however, is not totally without risk to the borrower and its principals. To ensure that the borrower does everything that it should to protect the mortgaged property, non-recourse lenders typically require that the borrower and its principals guarantee certain specific losses, which are commonly known as the “non-recourse carve-outs” (or “bad boy acts”). Examples of typical non-recourse carve-outs are: fraud or misrepresentation, misapplication of insurance or condemnation proceeds, misapplication of rents, and losses related to environmental matters.

Carve-outs impose personal liability on the borrower and guarantors for losses suffered by the lender due to the wrongful acts of the borrower or its principals. The borrower and guarantors would be required to compensate the lender for losses to the lender resulting from the occurrence of one or more of the carve-out items. While most securitized lenders use a similar list of “carve-outs,” they do vary from one lender to another and can also, at times, be limited by negotiation.

Certain categories of bad acts are considered even more risky to lenders and so, as an additional precaution, many lenders also require the borrower and guarantors to guarantee the full amount of the loan if any of the specified events occurs. For example, the bankruptcy or insolvency of the borrower or related parties, an unauthorized transfer of the property or of shares or interests in the borrower and a violation of the single purpose covenants imposed by a conduit lender are all events that could convert a non-recourse loan to a fully recourse loan. When this happens, the borrower and guarantors become liable for payment of the entire loan amount.

In most cases following a default, even if the conduit lender takes back the property, no further liability is imposed under the carve-outs. But it is important to note that many borrowers who enter into conduit loans relying on the “limited liability” nature of the loan never understand that, under certain circumstances, significant liability can – and will – be imposed by the lender. If the borrower fails to meet the requirements of the loan documents, the resulting default can often trigger personal liability to compensate the lender for its actual losses or for the entire loan amount.

## LEARNING THE HARD WAY

A borrower and guarantors in Massachusetts recently learned this lesson the hard way. In *Blue Hills Office Park, LLC v. J.P. Morgan Chase Bank as Trustee*, a federal court found that a borrower’s transfer of a \$2 million dollar settlement award violated its loan documents with a securitized lender and triggered the full recourse liability provisions of its note and mortgage. Consequently, the court held that the borrower and the loan guarantors were liable to the lender for the full amount of the loan – more than \$17 million dollars. The *Blue Hills* case was the first reported case enforcing the non-recourse carve-outs in a conduit or “securitized” mortgage loan.

The *Blue Hills* case underscores the following important lessons for borrowers and guarantors:

- Be sure that you review the term sheet and commitment letter for a new loan with your attorney before signing these important documents in order to try to negotiate as narrow a list of non-recourse carve-outs as possible.
- Be sure that you understand that under certain circumstances, a “non-recourse” loan could lead to personal liability for the borrower and carve-out guarantors, including full liability for all losses incurred by the lender.
- As a borrower, recognize that the term “collateral” or “mortgaged property,” as used in a mortgage, may include any and all rights related to the real estate, including money and damages awarded in a litigation or settlement if the case is related to the real property covered by the mortgage. The court in *Blue Hills* found that a settlement award related to the mortgaged property was included within the “property” secured by the mortgage. The borrower’s failure to advise the lender about the dispute and its eventual settlement violated the loan documents and triggered the personal liability of the borrower and the guarantors.
- Know that once the loan closes, it is not “over.” Borrowers and guarantors alike must recognize that they have continuing obligations to the lender under their loan documents and these obligations cannot be ignored.

## GOOD PRACTICE

Specifically, borrowers and guarantors must remember that many of the recommendations noted here are simply good practice for any property owner and manager, regardless of whether it enters into a “non-recourse” loan or a loan supported by guaranties. It is important that any prospective borrower and guarantor be well aware of the potential benefits and risks of any financing option. A non-recourse loan is an attractive financing option for a knowledgeable borrower. It is important to keep in mind, however, that there are certain limitations on the limited nature of non-recourse loans.

*Robin E. Lewis is a partner in the firm and specializes in commercial real estate law, secured lending and workouts.*

# Court Reverses Construction Lien Claim Filed Against Landlord's Property



by Cheryl H. Burstein

The Appellate Division of the Superior Court of New Jersey recently considered the question of whether a construction lien arising out of work performed by a contractor for a tenant can be filed against the landlord.

In an unreported decision, *Cherry Hill Self Storage, LLC v. Racanelli Construction Company, Inc.*, the court held that unless the landlord authorizes the construction contract in writing, filing a lien claim would be improper.

The premises at issue was a building containing both warehouse and showroom space. The lease provided that if the landlord chose to occupy the warehouse portion of the leasehold, upon notice to the tenant, the tenant would be obligated to undertake certain improvements.

The lease also provided that the tenant was to give “prompt notice to the landlord of the commencement of any work or alteration or improvement on the Demised Premises” and that the “landlord had the right to post notices of non-responsibility... in connection with all work of any kind upon the Demised Premises.”

The lease also provided for a rent credit to the tenant so long as the work was completed. After the work was performed, the tenant ultimately failed to pay its contractor.

Although the trial court found that the various lease provisions taken together “were more than adequate to provide the requisite written agreement,” for filing a lien under the State construction lien law, the Appellate Division disagreed. The statutory language provides in relevant part: “If a tenant contracts for improvement of the real property and the contract of improvement has not been authorized in writing by the owner of a fee simple interest in the improved real property, the lien shall attach only to the leasehold interest of the tenant.” This language led the appellate court to hold that there must be an authorization of the specific contract of improvement before that construction contract can be the basis of a properly filed lien claim against the property.

*Cheryl Burstein is a partner in the firm and specializes in construction litigation.*



# Closing Costs and

## TO KNOW THEM IS TO BUDGET FOR THEM

by Craig W. Alexander



The terms “closing costs” and “closing adjustments” are ubiquitous. Like “appraised value,” they are used indiscriminately throughout the real estate industry. But like other quasi-legal phrases, they are also ambiguous. The brokers never discuss them when negotiating business terms. The clients do not include them in letters of intent, and attorneys often include only a brief reference to them in contracts of sale.

By failing to carefully consider the anticipated closing costs and adjustments for a transaction *before* executing a contract of sale, a seller or buyer

may discover at the closing that its budget for the deal was substantially off the mark, resulting in either insufficient capital for the closing or less net proceeds of sale than anticipated. To avoid this unpleasant surprise, several costs and adjustments should be reviewed and appropriately budgeted at the outset of a deal.

### REALTY TRANSFER FEE

All residential and commercial real estate is subject to the realty transfer fee. While the seller customarily pays the transfer fee, it is a negotiable expense which can be shifted to the buyer. The transfer fee is based on a schedule set by the State. For sellers of commercial property, it is essential to factor the transfer fee into a pro forma prior to executing a contract of sale, as the fee can be very substantial (currently, the transfer fee for \$2,000,000 is \$21,675; for \$10,000,000 it is \$118,475).

### MANSION TAX

Sellers and buyers should be aware of the so-called “mansion” tax which applies to all real estate other than vacant land, industrial property, apartment buildings, and real property owned by charitable organizations. The mansion tax is triggered when the sale price exceeds \$1,000,000, but the tax is based upon the total sales price (not just the amount in excess of \$1,000,000). The tax will be 1% of the consideration. The mansion tax is customarily paid by the buyer, but like the transfer fee, this obligation can be shifted. The mansion tax may be triggered even if a deed is not recorded upon the sale of a controlling interest in the entity that owns the real estate. In such cases, the equalized assessed value of the asset before and after the transaction must be evaluated to determine if the mansion tax applies.

### ROLLBACK TAXES

Sellers and purchasers should also be aware of the “rollback” tax. Subject to certain conditions, property not less than five acres which has been actively devoted to agricultural or horticultural use may be valued as farmland for tax purposes. When property is assessed as farmland, the real estate taxes are substantially lower than standard rates. When the property is no longer used as farmland, it will be taxed at full and fair value like other property in the area. It will also be subject to additional taxes, called “rollback taxes,”



# Adjustments:

which are essentially equal to the difference between the property's assessment at full and fair value and the amount paid under the farmland assessment. Rollback taxes will be imposed for the two tax years immediately prior to the tax year in which the change in use of the land occurs.

For large tracts of land, the rollback taxes can be substantial. Since unpaid rollback taxes constitute a lien, the buyer must make sure they are addressed. There is no custom as to whether a seller or buyer pays the rollback taxes; it is a negotiable cost. However, if the seller is responsible for the rollback taxes, it will be necessary to escrow an appropriate sum from the proceeds of sale, since the actual amount of the rollback taxes will not be determined until after the closing. The municipal tax assessor can estimate the amount of the taxes. The escrow will insure that sufficient funds are available to pay the taxes when they are assessed without having to pursue the seller after the closing.

## LEASING COMMISSIONS

For rental property, it is critical to determine the status of broker commissions for the leased space. The parties should determine if the commissions are paid in full for the current lease terms, and whether any commissions will be due upon their renewal or extension. A buyer should request and review all lease agreements and commission agreements. Appropriate representations should be made in the contract addressing the status of all commission arrangements. Because leasing commissions are often based upon the total rent paid for the entire lease term or option term, the amount of the commission can be substantial and the failure to address this issue could be costly.

If the buyer is responsible for paying the commission upon a lease renewal or extension, the contract of sale must include an express assumption of this liability and appropriate indemnification language. Similarly, the contract must explicitly state that the buyer does not assume the liability if the seller will remain responsible for paying the commission. Under current case law, a seller remains liable to pay leasing commissions provided there is no express assumption of this obligation by the buyer in either the contract of sale or the closing documents. The conveyance of the property, by itself, will not transfer this liability to the buyer.

## RENT OR TAX ADJUSTMENTS

Buyers and sellers should be conscious of rent, security deposits and real estate taxes involved in a transaction. These adjustments are typically made by annualizing the figures, and then basing the adjustment on a per diem amount based on the closing date. Sometimes, rent will be adjusted based upon only the number of days in the month of closing. Both methods are valid. The goal is to use the method that produces the most advantageous adjustment.

Security deposits are customarily adjusted by providing a closing credit in the total amount of the deposits. With residential tenants, caution must be exercised to ensure that all interest earned on the deposits has also been

transferred, and for this reason the bank accounts holding the security deposits are sometimes transferred to the buyer instead. With commercial tenants, it is important to know in advance the amount of the security deposits. If it is a large amount, this adjustment will lower the cash needed at closing by the buyer.

The method of adjustment for real estate taxes depends upon the closing date. If the closing occurs during the first half of the year before issuance of the third and fourth quarter tax bills, the custom is to calculate the per diem adjustment based upon the preceding year's total tax bill. With this method, the parties will often escrow funds until the tax adjustment can be reconciled after the tax bills have been issued. If the closing occurs in the second half of the year, the adjustment will be based upon the annual tax bill for the year of closing using a straight per diem method.

## LOAN FEES AND ESCROWS

With the dizzying array of loan products currently available today, it is critical when budgeting for a deal to know the amount of loan fees and escrows a lender will require. These amounts should be identified and quantified before accepting a loan commitment. The lender will often charge fees for an appraisal, environmental review, legal, and structural inspection of the property. Escrows will often be required for tenant improvements, leasing commissions, and taxes and insurance premiums. All of these items are negotiable and depend upon the particular situation. Although there are some established parameters within the industry, lenders often make unusual requests at the time of closing. To avoid surprises when the lender furnishes closing figures, the loan commitment should clearly list the category and amount of all fees and escrows for the credit facility. Like other closing costs, this information will assist the borrower in adequately budgeting for the transaction.

## AND THERE'S MORE

This article is not a comprehensive list of all closing costs and adjustments. There are other transaction costs, such as title, survey and sales commissions, which are important and should be carefully considered. There is no great mystery to them, however, and they can be approximated with an attorney's assistance.

If the transaction involves real estate outside of New Jersey, even greater caution must be exercised in reviewing the types and amounts of closing costs and adjustments. Each jurisdiction has different statutes and practices. For example, New York has a very substantial mortgage tax. In Pennsylvania, it is customary for the buyer and seller to split the transfer fee. And in Florida, the seller typically pays for the buyer's title insurance policy. Because these costs can be significant, it is important to identify and quantify them before executing a contract of sale.

*Craig W. Alexander is a partner in the firm's Real Estate Department who specializes in commercial real estate transactions, land development, leasing, and corporate and financial transactions.*

# FIRM NEWS

# VIEW FROM THE BAR

## Our People:

**William H. Healey**, a shareholder in the firm, has been designated by the Supreme Court of New Jersey as a Certified Civil Trial Attorney, a distinction limited to less than 2% of the lawyers in New Jersey. Through its Board on Attorney Certification, the New Jersey Supreme Court designates as a Certified Civil Trial Attorney only those lawyers who demonstrate sufficient levels of experience, dedication, knowledge, and skill in civil trial practice.

Healey, of Rumson, is a member of the firm's employment law and litigation practice areas. He represents and counsels businesses in the full range of employment law matters and related litigations, including the defense of discrimination, harassment, retaliation, breach of contract, wage and hour, and wrongful discharge claims. He also specializes in cases

involving fraud, trade secrets, employee disloyalty, independent contractors, non-competition and nonsolicitation agreements, business dissolution, shareholder rights, and other commercial issues.

Healey received his Juris Doctorate degree from Rutgers School of Law-Camden, and his Bachelor of Arts degree from Rutgers College. He is admitted to practice law in New Jersey, New York, and Pennsylvania, as well as the United States District Court for the Districts of New Jersey, the Southern District of New York, the Eastern District of New York, the Eastern District of Pennsylvania, and the United States Court of Appeals (Third Circuit).

**Paul Gregory**, has been named a Director of the firm. Gregory specializes in small business, corporate, and transactional law. He received his B.A. in Political Science from Bucknell University and his J.D. from Widener University School of Law in Wilmington, Delaware. He is admitted to practice in both Pennsylvania and New Jersey. He was a law clerk to the Honorable Michael Winkelstein, Presiding Judge of the Civil Division and Assignment Judge for Atlantic and Cape Counties. Paul is a member of the Atlantic County and New Jersey State Bar Associations, the Inns of Court, and Chatham Area Chamber of Commerce.

**David S. Carton**, a partner in the firm in the Family Law Department, was recently Qualified as a Mediator pursuant to the Rules of Court. Also, on December 12, 2007, David spoke at Beth Israel Hospital in Newark, New Jersey, on the issue of Domestic Violence.

**Lynne Strober**, a partner in the firm and chair of the Family Law Department, has been re-appointed to serve in 2008 on the Board of Editors of the Matrimonial Strategist, a nationwide publication of Law Journal Newsletters.



**MANDELBAUM • SALSBURG**

*Depth. Distance. Dimension.*

[www.msgld.com](http://www.msgld.com)

155 Prospect Avenue, West Orange, NJ 07052

Commercial Real Estate | Corporate & Employee Benefits | Criminal Defense | Family Law  
Health Care Intellectual Property | Labor & Employment Law | Land Use | Litigation & Dispute Resolution  
Personal Injury | Tax Law | Trusts & Estates | Workers' Compensation