



Real Estate Roundtable 2020

Overcoming Obstacles: Acquisition and Financing in a Pandemic

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Background

- Cowboy Jim has decided to deploy capital from refinancing his family's Blueberry Farm in the Agricultural Land Reserve.

Background

- He has his eye on a Main Street mixed use development, “Shady Mews”:
 - 4 floors of office space;
 - 32 residential rental units; and
 - 7 ground level retail units.

Background

- Shady Mews ground level retail tenants are:
 - Nacho Daddy Mexican Restaurant;
 - Wok This Way Japanese;
 - Everyone's Welcome Credit Union;
 - Get the Funk Out Laundromat;
 - Hyper Slow Yoga Studio; and
 - Julius Scissor Hairdressing.

Background

- Cowboy Jim has an accepted offer on the site and is currently completing due diligence on the property.

Background

- Cowboy Jim has obtained an initial commitment for acquisition financing.
 - Includes specific financial covenants:
 - E.g. a net operating income covenant.
 - No flexibility!

Background

- The seller has granted the tenants certain rent concessions.

Background

- Concession #1: Wok This Way was granted 3 months deferred rent (April, May, June 2020).
 - To be repaid by the end of 2021.

Background

- Concession #2: Nacho Daddy defaulted on rent payments in April and May, 2020.
 - Caught up on rent after opening an outdoor patio.
 - But what about the rainy season?

Background

- Concession #3: All current office tenants are up to date on rent payments, but there are various requests for the Seller to consider reducing rent, and consent to subleases or transfers of space.

Background

- Cowboy Jim informs his lender and the bank amends the deal, including:
 - revised financial covenants; and
 - a requirement for additional guarantees from two of Cowboy Jim's business partners.
 - Both are reluctant to agree.

Issues

- Issue 1(a): What should Cowboy Jim consider addressing in the contract before going firm?

Discussion: Issue 1(a)

- Due Diligence
 - Consider requiring additional documentation and information from the seller (eg. tenant correspondence and deferral negotiations, information on tenant revenue, government benefits and outstanding rents/receivables).
 - Ensure sufficient time to review and analyze deliverables and impacts of same.
 - Discussions with material tenants may prove to be invaluable

Tenant Deliverables

“a listing of Deferred Rent for the Property on a monthly basis for the previous 18 months, including a summary of any free or forgiven rent given to any Tenant, copies of all such agreements and copies of all communications with all Tenants who have requested that the Landlord grant them Deferred Rent;”

Discussion: Issue 1(a)

- Adjustments and Deferred Rent
 - Should Cowboy Jim assume any deferred rent or reduced rent which occurs after closing?
 - What should Cowboy Jim do when he receives the deferred rent which is in connection with the period before closing?
 - Ensure strong restrictions on additional amendments or deferrals granted to tenants

Deferred Rent

“Deferred Rent” means any Rent that is payable, or would have been payable, by any Tenant in respect of any period preceding the Closing Date, but such Rent has not been, or will not be, paid prior to the Closing Date because the landlord and the Tenant have agreed in writing that:

- a) the due date or payment date for such Rent will be deferred or postponed to a date after the Closing Date; or
- b) some other accommodation will be provided by the landlord to the Tenant with respect to such Rent.

Collection of Arrears and Deferred Rent

“No adjustment will be made in favour of the Vendor on Closing in respect of any Arrears or Deferred Rent. All Arrears and Deferred Rent shall remain the property of the Vendor on Closing. After Closing, the Purchaser shall co-operate with the Vendor and use commercially reasonable efforts to collect Arrears and Deferred Rent on behalf of the Vendor, and provide an accounting in respect of same from time to time upon the reasonable request of the Vendor, provided that the Purchaser shall not be required to bring any legal action or proceedings in respect of any Arrears or Deferred Rent, terminate any Leases, take possession of any premises under any Leases, exercise any right of distraint or spend any money on legal fees or otherwise. Any Rent (including, for certainty, any amounts in respect of Rent pursuant to any rent relief programs of any Governmental Authorities, including the program commonly known as the Canada Emergency Commercial Rent Assistance program) recovered after Closing by the Purchaser (including, for certainty, where rent relief amounts are paid to a third party on the Purchaser’s behalf or for the Purchaser’s benefit) from, or in respect of, a Tenant owing Arrears or Deferred Rent, or otherwise, at Closing shall be applied as follows:

- a) first, against current Rent (and applicable GST) due and owing to the Purchaser by such Tenant;
- b) second, against any arrears of Rent (and applicable GST) accrued in respect of such Tenant after the Closing Date; and
- c) thereafter, the excess, if any, against the Arrears or Deferred Rent of such Tenant (and applicable GST) accrued on or prior to the Closing Date and not adjusted on Closing.”

Discussion: Issue 1(a)

- Closing Conditions
 - Focus on the content of estoppel certificates and ensure that they reflect disclosure and deliverables provided by Seller
 - Consider closing condition where there are new tenant defaults. This is particularly important where the Cowboy Jim's lender has included strict financial requirements.

Issues

- Issue 1(b): How the issues with rental income might impact Cowboy Jim's ability to close with his acquisition financing?

Discussion: Issue 1(b)

- Relevant factors:
 - The type of loan
 - The timing in the course of the deal of when the issue arises

Discussion: Issue 1(b)

- Existing loans:
 - When financial covenants are impacted, ask whether the preference is for a temporary reprieve, or an amendment to the terms of the loan
 - Potential for short payment deferral or temporary conversion to interest-only payments *if* payments were previously blended.
 - If the loan is an operating line and borrower misses a financial covenant, they may be allowed to continue to access the line at a lower maximum.

Discussion: Issue 1(b)

- Committed but unfunded loans:
 - Potential for lender “easy out”.
 - Lender may ask for increased equity, new guarantors, etc.
 - Borrowers may have to deliver updated information for all loan parties.

Discussion: Issue 1(b)

- Takeaways:
 - Lender considerations are situational – each situation is unique.
 - Quality of the existing relationship is key.
 - Borrowers should be proactive, prepared and cooperative.

Issues

- Issue 1(c): What arrangements might Cowboy Jim propose with the lender and/or his partners to induce them to agree to the lender's guarantee request?

Discussion: Issue 1(c)

- Potential options:
 - Limited guarantees
 - Several (as opposed to joint and several) guarantees
 - Side agreements to apportion guarantee-related liability
 - E.g. apportioned on *pro rata* basis

Discussion: Issue 1(c)

- Takeaway: Raise any issues early with the lender, before an amended commitment letter is signed.



THANK YOU FOR LISTENING



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Additional Thoughts

- Give everything extra time
- Wire transfers vs. certified funds
- Video witnessing
- Watch out for fraud!