A PRACTICAL GUIDE TO DOCUMENTING AND CLOSING A CONSTRUCTION LOAN

Commercial Real Estate Financing:
What Borrowers and Lenders Need to Know

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TABLE OF CONTENTS

Table of Contents

Page

I. SCOPE OF DISCUSSION ... 1

II. SPECIAL RISKS, RIGHTS AND REMEDIES ASSOCIATED WITH CONSTRUCTION LENDING. ... 1

A. The Construction Risk ... 2

1. Failure to Comply with Zoning, Other Governmental Requirements, and Restrictive Covenants. ... 2
2. Budget. ... 3
3. Approval of Contractor and the Construction Contract. ... 3
4. Integrity of Construction. ... 4
5. Location of the Improvements and Encroachments. ... 4
6. Construction Schedule. ... 4
7. Availability of Roads and Utilities. ... 4
8. Use of Loan Proceeds/ Funding Risks. ... 4

B. The Leasing or Market Risk. ... 5

C. The Take-Out-Risk. ... 5

1. The Amount of the Take-Out. ... 5
2. Tri-Party Agreements. ... 5
3. Approval of Conditions. ... 6
4. The Nature of a Take-Out Loan Commitment ... 8

D. Lender's Remedies Upon Default. ... 9

E. Lien Priority Issues ... 9

III. ESTABLISHING THE TERMS OF THE REAL ESTATE LOAN ... 10

A. Legal Issues Affecting Commitment Letters and Term Sheets ... 10

1. Reliance by Third Parties ... 10
2. Effect of Commitment Fee ... 10
3. Remedies for Breach ... 10
4. Regulatory Issues ... 10

B. Internal Loan Approvals ... 11

C. Term Sheets ... 11

D. Binding Commitment Letters ... 12

IV. **INITIAL DRAFTING CONSIDERATIONS** ... 13

A. Length and Sophistication of Documents ... 13

B. Distribution of Documents and Methodology for Redrafts ... 14

C. Choice of Law ... 14

D. The Move to Institute Bankruptcy-Proofing Requirements ... 15

1. Bankruptcy Remote Borrowers ... 15
2. Restriction on Other Assets and Other Indebtedness ... 16
3. Controlling the Cash ... 16
4. Personal Liability Inducements ... 16

V. DUE DILIGENCE ... 17

A. Organizational Documents ... 17
B. Title Review ... 18
C. Survey ... 18
D. Flood Certification ... 18
E. Tax Information ... 19
F. Permits and Licenses ... 19
G. Availability of Utilities ... 19
H. Zoning ... 20
I. Confirmation of Compliance With Laws ... 20
J. Plans and Specifications ... 20
K. Architectural Approval/Subdivision Restriction Compliance Confirmation ... 20
L. Waiver of Repurchase Rights ... 21
M. Waiver of Right of First Refusal ... 21
N. Appraisal ... 21
O. Insurance ... 21
P. Environmental Assessment ... 22
Q. Architect/Engineer's Audit ... 22
R. Ground Lease ... 22
S. Space Leases ... 22
T. Equipment Leases and Conditional Sales Agreements ... 22
U. Operating/Service Agreements ... 23
V. Management and Franchise/License Agreements ... 23
W. Purchase and Sale Agreements ... 23
X. Existing Loan Documents ... 23
Y. Other Loan Documents ... 23
Z. Take Out Loan Commitment ... 23
AA. Budget ... 24
BB. Project and Financial Information ... 24
CC. Pledges of Ownerships Interests ... 24

VI. DRAFTING THE LOAN DOCUMENTS ... 24

A. General Drafting Considerations ... 24
1. Notice Information ... 24
2. Format for Recorded Documents ... 25

3. Execution 25
4. Post-Closing Requirements 25
5. Tax Identification Number and Organizational Number 25
6. Corporate Seals 25
7. Multiple Execution Copies 26
8. Out of State Filings 26

B. The Loan Agreement 26

1. The Lender's Commitment to Lend 26
2. The Purpose the Loan 26
3. Repayment Terms 26
4. Representations and Warranties 27
5. Reserves and Accounts 28
6. Covenants 28
7. Events of Default 31
8. Rights and Remedies of Lender 32
9. Application of Casualty and Condemnation Proceeds 32
10. Co-Lender Provisions 33
11. Miscellaneous 33

C. General Considerations Regarding Security Documents 34

1. Definition of Secured Indebtedness 34
2. Description of Mortgaged Property for the Deed of Trust 35
3. Granting Language 37
4. Security Agreement 38

D. Third Party Consents and Acknowledgments 38

E. Limitation of Liability/Non-recourse Provisions 38

A PRACTICAL GUIDE TO DOCUMENTING AND CLOSING A CONSTRUCTION LOAN

I. SCOPE OF DISCUSSION. This paper is intended as a practical guide to assist you in documenting and closing a commercial real estate construction loan. First and foremost, a construction loan is a real estate loan, and all issues applicable to real estate lending generally are applicable to construction loans. A construction lender faces additional risks associated with the construction process and, for that reason, a construction loan is usually more expensive to document and close than other real estate loans and is less frequently non-recourse (at least with respect to construction risks). A construction loan requires that lender's counsel conduct additional due diligence, and additional loan documents and third-party assurances will be required.

This article is written from the perspective of the lender's attorney because the lender's attorney is generally responsible for and directs the due diligence, loan documentation and closing process. This paper begins with a discussion of the special issues faced by construction lenders and their attorneys, and then addresses the loan commitment/term sheet process, the due diligence process and the loan document drafting process. This paper is a general guide to the process of documenting and closing a construction loan and does not include a detailed discussion of regulatory or bankruptcy issues), or attempt to provide an in-depth discussion of the current state of case law on the many areas of real estate law open to discussion today. Counsel should note that virtually all legal principles applicable to real estate generally are relevant to the lender's counsel because these issues may affect the viability of the project, the likelihood that the loans will be successfully repaid and, ultimately, the value or marketability of the project to the lender in the event a foreclosure occurs. The lender's counsel must have some understanding of the legal and business issues associated with the acquisition, development, ownership, operation, leasing, financing, refinancing and sale of the type of real estate project under construction in order to adequately advise his or her lender client and prepare appropriate documentation allocating the risks associated with such matters, consistent with the agreement of the parties. By approaching the transaction in an organized and efficient manner, lender's counsel can streamline the process and, hopefully, cause the loan to be closed in a more timely and economically efficient manner. To assist you in this effort, I have included with these materials a sample form of Due Diligence Checklist and Loan Document Checklist.

II. SPECIAL RISKS, RIGHTS AND REMEDIES ASSOCIATED WITH CONSTRUCTION LENDING. The additional risks facing construction lenders can be categorized as follows: the construction risk, the leasing/market risk and the take-out risk. Additionally, because of state law governing the "inception" and priority of mechanics liens, lender's counsel must fund the loan in a manner consistent with local law and practices, and require additional title insurance protection, documentation, affidavits and representations regarding funding, commencement of construction and lien subordinations and waivers. The lender will also want to negotiate extensive remedies allowing the lender to enforce the agreements with the architect, engineer and contractor, and complete construction following a default.

A. ***The Construction Risk***. Essentially, the lender must satisfy itself that the contemplated improvements can be built in accordance with the plans and specifications, for the budgeted amount, and within the time period anticipated. Upon completion, the development must comply with all applicable governmental requirements (including zoning) and restrictive covenants, and the requirements of all applicable tenants, purchasers and permanent lenders. A construction loan is generally based on a budget prepared by the borrower. This budget should include all costs - hard and soft - the borrower anticipates it will incur in buying the land and planning, developing, financing, and if applicable, leasing, refinancing and disposing of the project. The borrower will advise the lender of the anticipated construction period, and the lender will generally make provision in the loan budget to advance funds to pay interest on the construction loan during the construction period. A construction lender is usually unwilling to advance one hundred percent of the budgeted costs, and will require that the borrower contribute its equity before the lender advances any loan proceeds (or at least any loan proceeds beyond the nominal amount needed to allow the lender to perfect its liens and security interests). The lender will also usually require that the borrower has the obligation to pay for any cost overruns, before the lender advances any further loan proceeds.

The lender's collateral value is dependent upon completion of construction. If the lender advances all or a portion of the loan proceeds and the building is not completed, the value of the collateral will be grossly disproportional to the amount advanced. For example, if a construction project is estimated to cost $100,000,000, and the lender advances $75,000,000, but the construction is only 50% complete, the collateral value will be substantially less that $75,000,000 - and potentially substantially less than $50,000,000. In order to avoid this situation, the lender's attorney should consider the following:

1. Failure to Comply with Zoning, Other Governmental Requirements, and Restrictive Covenants. The lender's attorney should review applicable zoning ordinances, governmental requirements and restrictive covenants, and be sure the lender's construction review team is also furnished a copy of these materials prior to their review of the project. A building permit, zoning compliance letter from the applicable municipality, certificates of compliance from the architect and engineer, and written approval from the architectural review board under the restrictive covenants are useful in this regard. It is very difficult to determine compliance of the contemplated improvements until the plans and specifications are finalized. Frequently the borrower will "fast track", and will not have finalized plans and specifications at the time of the loan closing. A fast track approach usually speeds up the entire construction process because the contractor begins work before the architect has completed the plans. The risk with this approach is that the preliminary plans used by the contractor are not adequate or that the final building contemplated by the architect turns out to be unacceptable to applicable governmental authorities or the architectural review board, or costs more than budgeted. Obviously, the lender will not want to advance funds for construction until the necessary building permits and municipal approvals are obtained, but the collateral value of even the land and the soft costs advanced from loan proceeds may be adversely affected if the municipality subsequently requires substantial alterations to the contemplated improvements. Proceeding without final plans is a business risk which is acceptable to many lenders in today's marketplace, and sometimes the only comfort available is the experience of the borrower, architect and engineer in related projects in the area. Unless directed otherwise by the lender, lender's counsel should review applicable governmental requirements and restrictive covenants, and furnish copies to the lender and the lender's construction review team. The loan documents should prohibit the borrower (as well as the architect, engineer and general contractor) from changing the

plans after the lender and its construction review professionals have approved the plans and specifications. Frequently, the lender will allow changes without its consent, or will agree not to withhold or delay its consent, if the changes, individually and in the aggregate, do not impair the compliance, structural integrity, value or cost of the building in any material way. The borrower should be required to furnish lender a set of final, certified as-built plans and specifications upon completion. If the lender ever has to foreclose or market the project in the future, these "as-built" plans will be very valuable, and the borrower may not be inclined to deliver them at that time.

2. Budget. In order to assure that the development can be completed with the proceeds of the loan and the borrower's required equity, the borrower must prepare and submit to the lender a detailed budget covering all costs anticipated to be incurred in the development process. The lender should carefully review the borrower's construction budget. The construction budget is broken down first into hard and soft construction costs, and these general categories are further broken down into very specific categories - such as architectural and engineering fees, steel, electrical, etc. The budget will include a contingency item in an amount acceptable to the lender, and will give the borrower's best estimate of the timing of advances, so that the borrower and lender can estimate the size of the "interest reserve" in the construction loan. Since a construction loan is advanced as work proceeds and costs are incurred, the total amount of interest which will accrue will depend on the advance schedule. If the loan will not be repaid immediately upon completion, the lender may also require delivery of an operational budget which includes the estimated costs to lease, manage, operate and refinance or dispose of the project following completion, and the projected cash flow of the project for the same period. The lender will usually require that the borrower has sufficient money available to fund projected operating deficits, and to maintain, manage and lease the project in accordance with prudent ownership practices until the loan is repaid. The construction loan documents should (a) not obligate the lender to advance loan proceeds except in accordance with the approved budget or as the lender may otherwise see fit, (b) require that the borrower pay its required equity and any construction or operating deficits before loan proceeds are advanced, and (c) prohibit the borrower from making any changes in any line items in the approved budget without the lender's consent, if the change order would result in a cost increase. The lender may agree to allow the borrower to make changes below some agreed upon threshold (such as 5% or 10% of any line item), so long as sufficient funds remain available in the contingency item or equivalent cost savings are achieved in another budget category.

3. Approval of Contractor and the Construction Contract. The lender will generally want to approve the general contractor and major subcontractors, as well as the form of the construction contracts. If the borrower's contractor choices are not acceptable to the lender, the lender may require performance and payment bonds to protect itself against the possibility that the contractor will not complete the project or will fail to pay subcontractors with the money advanced, and may also require that the borrower pay for the lender to hire (or increase the scope of work for) lender's inspecting architect. The lender will want the construction contract to be written as a fixed price or "not to exceed" contract, but the borrower may want to use a "cost plus" contract, thereby introducing uncertainty as to the actual hard cost of construction. The construction contract should (a) provide that the contractor perform its duties in a manner consistent with the construction loan and take-out documents, (b) permit the lender to step into the borrower's shoes upon default, (c) require the contractor to sign a lien subordination and waivers in a form acceptable to the lender, and (d) require that payments be made to the contractor in a manner consistent with the loan advance provisions in the construction loan documents (including retainage, if applicable).

4. Integrity of Construction. The loan documents should provide reasonable assurances that the project will be built in a good and workmanlike manner, consistent with the approved plans and specifications. The borrower, contractor and architect are generally required to submit affidavits with each construction advance certifying that construction is proceeding in such manner, and the lender generally requires that the borrower pay for lender's inspecting architect to monitor the construction process. If a third party lender, purchaser and/or tenant has the right to approve or accept construction, a prudent lender may also require that the third party approve construction performed to date with each construction advance.

5. Location of the Improvements and Encroachments. The lender should confirm that the improvements as shown on the plans and specifications do not encroach into any building setback requirements or easements, and that the building is built within the boundaries of the land covered by the lender's deed of trust. The lender may require delivery of a foundation survey after completion of the foundation of the building to verify the building location before additional funds are spent on construction. If the project will be built in phases, the lender may require that the foundation surveys be furnished for each phase as completed.

6. Construction Schedule. The loan documents should require that the borrower commence construction by a date certain, prosecute construction diligently and cause construction to be completed by a date certain. Most construction loan agreements also provide that if construction ceases for a period in excess of a set number of days (and sometimes giving a longer period for weather delays), the loan will be in default. Timing of completion is important because a delay may cause additional interest which is not covered in the loan budget (and which the lender is not obligated to advance), jeopardize a market advantage or cause a default under significant take-out or credit commitments, such as loan commitments, purchase agreements and leases.

7. Availability of Roads and Utilities. The lender must assure itself that upon completion, the project will have unrestricted access to one or more publicly dedicated roads, and that utility service will be available at the project in sufficient capacities. Frequently, in order to obtain a building permit or zoning variances, the borrower will be required to submit a traffic study to the municipal authorities. The lender may want to review this study to confirm that sufficient funds are available in the budget to pay for on and off-site roadway improvements contemplated in the traffic study. The borrower should be required to deliver letters from local utilities (such as water, sewer, electricity, gas and telephone) confirming that the utility will supply sufficient capacity to the edge of the property, and the lender should confirm that the plans and specifications and budget include necessary on-site and off-site infrastructure to bring the utilities in sufficient capacity to the project. The lender's inspecting construction professionals may also request further assurances that any technical requirements necessary for the buildings' users will be available.

8. Use of Loan Proceeds/Funding Risks. The construction loan documents should require that as a condition to advancing funds, the borrower, contractor and architect certify that the money being requested is due and owing for work actually performed on the project. The documents should also require that the borrower use the loan proceeds for the purpose for which they were advanced, and may allow the lender to pay third parties directly, or make checks payable jointly to the borrower and contractor. A borrower will usually resist allowing the lender to make advances directly to third parties, and a prudent lender will generally make direct advances only if a problem has arisen with the borrower or the construction process. The lender should also require

that as a condition to each interim advance, the borrower must deliver an interim lien waiver from each contractor and subcontractor to be paid with the requested advance, confirming the funds paid to date and the funds remaining to be paid under the contractor or subcontractor's contract, and including a lien waiver for funds already paid. The lender should verify that the statements in the interim lien waiver are consistent with the lender's funding records. Upon payment in full of any contractor or subcontractor, the lender should require delivery of a final, complete lien waiver from that contractor or subcontractor.

B. ***The Leasing or Market Risk.*** Since the construction lender advances funds at a time when the building has no operating history, the lender must depend upon market studies and its understanding of the marketplace to predict the operating success of the contemplated project. In many cases, the first building completed in a market segment has an advantage over other projects coming on the market shortly thereafter, and the borrower and lender will want to assure that the project is completed as quickly as possible to preserve any market advantage. If the project is pre-leased, the lender will want to assure that construction is completed in the time periods (and in the manner) required by the lease. The lender will require that the borrower employ a marketing or leasing team and keep in place a marketing or leasing program acceptable to the lender, and require that the economic terms and lease forms for each lease of the project be approved by the lender. Lender's counsel may assist the lender in confirming that the lease contains satisfactory lender protections and requires the tenant to execute a subordination, non-disturbance and attornment agreement satisfactory to lender. The lender should carefully review any expansion, extension or purchase options, casualty and condemnation provisions and any exclusive use provisions contained in the leases.

C. ***The Take-Out-Risk.***

The "take-out" is the source of repayment for the construction loan. The borrower may provide a take-out by delivering a permanent loan commitment, a commitment to contribute equity (or "partner" the project), a commitment to purchase the project upon completion, or a lease with a creditworthy tenant which provides sufficient funds to service and amortize the loan in a manner acceptable to the lender. Lender's counsel should consider the following issues when reviewing any take-out agreement:

1. The Amount of the Take-Out. The lender should first confirm that the cash proceeds of any loan or equity commitment or purchase agreement will be sufficient to repay the construction loan in full, even if any gap, hold-back or lease-up requirements are not met. The lender should consider any free rent or tenant self-help remedies under any lease and confirm that these provisions will not affect the anticipated income stream in a manner unacceptable to the lender.

2. Tri-Party Agreements. Lender's counsel should require execution and delivery of a tri-party agreement between the lender, the borrower and the take-out party. If the take-out is in the form of a lease, this agreement is usually the subordination, non-disturbance and attornment agreement. The purpose of this agreement is to (a) establish contractual privity between the take-out party and the lender, (b) confirm that upon the borrower's default, the lender may enforce the take-out on behalf of the borrower or foreclose and succeed to the borrower's rights under the take-out, (c) provide for notice to the lender if any party defaults under the take-out, and an opportunity for the lender to cure any borrower default under the take-out, and (d) memorialize

the take-out party's approval of conditions to its funding obligation under the take-out agreement. The tri-party agreement should also provide that the take-out agreement cannot be assigned (except to the construction lender), amended or terminated without the lender's prior written consent.

3. **Approval of Conditions.** The take-out agreement generally conditions its closing and funding obligation upon satisfaction of certain conditions. The lender should require that all, or as many as possible, of these conditions are pre-approved in the tri-party agreement. If the lender cannot convince the take-out party to waive a condition precedent to its funding obligation, the lender should at a minimum attempt to have the take-out party narrow and clarify the condition, removing any discretion on the part of the take-out party. Lender's counsel should outline the conditions precedent contained in the take-out agreement, and draft the tri-party agreement to acknowledge the take-out party's consent to each condition. These conditions usually include the following:

a. Title and Survey. The take-out party should acknowledge its receipt and approval of the title commitment and survey furnished for the construction loan. If additional easements will be required to accommodate development of the property or the tenants' utility needs, the take-out party should also approve those title matters in advance. If the take-out party will not approve these additional title matters in advance, the borrower should agree not to grant any such easements without the prior written consent of the lender and the take-out party. The take-out party should agree not to object to any item shown on the completion survey which is shown on the survey delivered at the closing of the land loan, or to improvements shown in the plans and specifications. If the property is on a ground lease, the take-out party should pre-approve the estoppel letter it will require from the ground lessor, and the construction lender should obtain the agreement of the ground lessor to execute an estoppel letter in the required form for the closing with the take-out lender.

b. Appraisal. The take-out party should approve the appraisal delivered for the closing of the construction loan and waive its right to require a new or updated appraisal following completion.

c. Plans and Specifications. The take-out party should approve the plans and specifications, and pre-approve any amendments to the plans the borrower is authorized to make under the loan documents without the lender's approval. If the take-out party is not willing to pre-approve any changes, the borrower, contractor and architect must all agree not to make any changes without the consent of the lender and the take-out party.

d. Completion of Construction. The take-out party should agree that the completion of construction condition will be satisfied if the contemplated improvements are completed substantially in accordance with the approved plans and specifications (including approved changes), and should specify the evidence of completion which will be required. The lender's attorney should try to include an objective standard for completion, such as delivery of a certificate of completion by the borrower's architect or the lender's inspecting architect, and may also require that a certificate of occupancy (or a shell certificate of occupancy if additional tenant finishout will be required) be delivered as a condition to funding. The lender may also want to require that the take-out party conduct periodic inspections of construction progress, and upon completion of its inspection sign off on all work done to the date of such inspection. If the take-out

agreement requires delivery of an engineering study, the tri-party agreement should clarify that so long as the improvements are completed substantially in accordance with the approved plans, no item shown in the engineering study will be a basis for the take-out party's refusal to fund. Any time periods for commencement and completion of construction set forth in the take-out agreement should be conformed to the construction schedule prepared by the borrower and approved by the lender, plus adequate periods after the deadlines contained in the construction loan documents to allow the lender to cure any construction schedule problems.

e. Insurance. The take-out party should pre-approve the forms of evidence of insurance, certificates of insurance and insurance policies which will be required.

f. Architect, Engineer and Contractors. The take-out party should pre-approve the architect, engineer, general contractor and any subcontractors required by the take-out agreement as well as the terms of the agreement between the borrower and such parties, and forms of completion certificates which will be required from such parties at closing.

g. Environmental Matters. The take-out party should acknowledge its receipt and approval of the environmental assessment of the property delivered for the construction loan, and waive its right to require a new or updated report for closing. If the take-out party is unwilling to waive such right, it should at a minimum agree not to object to any matters disclosed in the environmental assessment furnished for the construction loan, or to any construction materials specified in the approved plans and specifications.

h. Evidence of Compliance with Laws. The take-out lender should specify precisely the evidence of compliance with laws it will require for closing, and the lender's attorney should confirm that such evidence will be available. For example, many take-out lenders require that the local government issue a zoning compliance letter, that the title company issue a zoning endorsement to the title insurance policy, and that the borrower's attorney issue a zoning compliance opinion. Many municipalities will not issue any written statement of zoning compliance, zoning endorsements for title insurance policies are not available in a few states, and attorneys in some states do not issue legal opinions on zoning. Any requirements of the take-out party for a certificate of occupancy should be carefully scrutinized if the lender intends the take-out party to fund prior to final completion of all tenant finishout. The final certificate of occupancy will usually not be issued until all finishout is complete; frequently, the borrower will be able to obtain only a shell certificate of occupancy for the building shell and a partial certificate of occupancy for completed tenant space. If the contemplated tenant finishout includes life safety systems, the borrower may not be able to obtain the shell certificate of occupancy until all of the life safety systems for the entire building are installed.

i. Evidence of Existence and Authority. The take-out party should acknowledge its receipt and approval of the organizational documents and good standing certificates for the borrower and the direct and indirect owners of the borrower and any other parties to the transaction, and should approve the forms of authorizations, consents, resolutions and incumbency certificates which will be required for closing of the take-out transaction.

j. Leasing. The take-out party should pre-approve a leasing schedule for the project, which should include standards of tenant creditworthiness, minimum economic terms for

leases and a standard lease form, and agree that all leases complying with those guidelines will be deemed approved by the take-out party. Alternatively, the lender must require that the take-out party and the lender approve each lease for the project. If the take-out party will require estoppel letters or subordination, non-disturbance and attornment agreements for closing, the leases should require the tenant to deliver such documents in the prescribed form upon the landlord's request.

k. Closing Documents. Ideally, the take-out lender and the borrower will negotiate and finalize the documentation to evidence their transaction before the construction loan is closed, and will execute the documents and hold them in escrow until closing. If the take-out agreement is a lease, the lender should require execution and delivery of the lease as a condition to closing the construction loan. If the take-out agreement is a purchase agreement or an equity commitment, the parties should agree on the form of closing documents to be executed, and either execute them and hold them in escrow until closing, or agree in the take-out agreement to execute the agreed form of documents at closing. Similarly, the lender may require that the take-out lender and borrower agree on the form of take-out loan documents, and execute the take-out loan documents and hold them in escrow until closing. If the take-out commitment is a standby loan commitment that the borrower and take-out party intend will be used only if better financing is not available, it will be more difficult to force the borrower to spend the money to negotiate and finalize those documents. If legal opinions will be required by the take-out party for closing, the form of those opinions should be negotiated and agreed upon at the closing of the construction loan.

4. The Nature of a Take-Out Loan Commitment. A take-out loan commitment is not a guaranty and it is not a note purchase agreement. If the construction lender is unwilling to assume the risk that the borrower (and any necessary guarantors) will refuse to execute the documents necessary to evidence the take-out loan, the construction lender should negotiate for a loan guaranty and/or a note purchase agreement from the take-out party. A take-out loan commitment does not generally obligate the take-out lender to refinance the construction loan if the borrower and guarantors are unwilling to execute or deliver the loan documents. The construction lender should negotiate for the right to foreclose the project and execute the take-out loan documents as the borrower/owner/assignee under the take-out loan commitment, but take-out lenders are sometimes unwilling to allow a special purpose subsidiary or affiliate of the construction lender to execute the take-out loan documents as borrower. Also, if the take-out loan includes a recourse component or a prohibition on sale, the construction lender may not be willing to accept the loan.

D. *Lender's Remedies Upon Default*. In addition to the standard remedies available to a lender upon a borrower's default, the construction lender should have the right to self-help remedies to complete construction of the project, both before and after foreclosure. The lender should have the right to cause the construction to be completed in accordance with the approved plans and specifications, governmental requirements and restrictive covenants, and the requirements of any take-out party. The lender should obtain written confirmation from the architect, engineer and contractor that the lender has the right to accept an assignment (or foreclose) the borrower's rights under the architectural and engineering contracts and the construction contract, and that the architect, engineer and contractor will continue to perform on lender's behalf. The lender will generally want the right to cause the architect, engineer and contractor to continue performance for lender even if the borrower previously defaulted under the contract, and without the lender being obligated to cure any borrower default. The contractor is unlikely to agree to this and will usually require that the lender must assume the construction contract and assume all of the borrower's obligations thereunder (especially the payment obligation). The construction lender may also require a completion guaranty from a solvent third party. Before drafting the completion guaranty, lender's counsel should discuss with the lender exactly what the lender expects the guarantor to do if the borrower defaults, and cause the lender to consider the following questions: (1) Does the lender want to require that the construction guarantor complete construction? (Note that the construction guarantor is usually affiliated with the borrower and in a default situation, the lender may not want anyone associated with the borrower to control construction) (2) If the guarantor will be required to complete construction, will the lender make the unadvanced loan proceeds available to the guarantor to pay construction costs? (3) Will the guarantor be required to assume the construction loan and become liable for the construction loan? and (4) Does the lender want the right to complete construction itself, and require the guarantor to reimburse the lender for construction costs? Or only the construction costs which exceed the unadvanced loan proceeds?

E. *Lien Priority Issues*. State laws vary in determining the priority of a mechanic's lien over a perfected construction loan mortgage. A few states provide that a mechanic's lien has priority over the lien of a prior perfected construction lender if the inception of the mechanic's lien occurred prior to the date the construction lender recorded its deed of trust. In some states, the time of inception of a mechanic's lien is the first to occur of commencement of construction and delivery of materials to the project. Other states provide that priority may be achieved by the construction lender by using some combination of special funding procedures, compliance with statutory retainage requirements and lien waivers and subordinations. Some states also provide that a lien waiver is unenforceable-and void-if the contractor has not been paid for the work the subject of the waiver. Lender's counsel for any construction loan for a project in another state should work closely with counsel in that state to assure that the construction lender will have complete priority over mechanic's liens, to the extent such protection is available. Often the best and simplest way to guaranty a construction lender lien priority over mechanic's liens is to obtain title insurance protection against mechanic's liens. This title insurance coverage is not available in every jurisdiction.

III. ESTABLISHING THE TERMS OF THE REAL ESTATE LOAN. Generally, the real estate loan process begins when a prospective borrower (or its broker or agent) approaches one or more lenders seeking financing for a real estate project. The prospective borrower (or its broker or agent) will negotiate with these lenders regarding the general loan terms that may be required - amount, interest rate, fees, payment terms, maturity, collateral, personal liability and any additional credit support (such as guarantors, letters of credit, etc.). At some point, usually before a lender obtains its necessary internal approvals to commit to the loan, the prospective borrower and lender will formally or informally agree on a schedule of key terms for the proposed loan. After the parties have agreed on this preliminary statement of terms, the prospective lender(s) will seek necessary internal approvals to commit to the loan. At that point, the parties may enter into a more detailed and formal written loan commitment, or may simply request that the lawyers begin preparation of the closing documents based upon the preliminary term sheet or the lender's internal loan approvals.

A. Legal Issues Affecting Commitment Letters and Term Sheets. A lender may be deemed to have committed to lend funds because of the oral statements of its lending officers. "Commitment letters" may become binding if third parties rely on the commitment letter or if a commitment fee is collected. A breach of a binding commitment to lend gives rise to a cause of action by the borrower.

1. Reliance by Third Parties. Even a term sheet which by its terms provides that the term sheet is not binding on the proposed borrower or lender can, in certain circumstances, create third party liability issues for a lender. A third party acting in reliance upon such a "commitment" may attempt to enforce the term sheet if the lender knew or had reason to know that its term sheet or commitment letter was utilized to induce a third party (such as a tenant, contractor or investor) to become involved in the project. Obviously, the third party will have a more difficult case proving it justifiably relied on the term sheet if the term sheet or commitment letter clearly and unequivocally states that it is not a commitment and should not be deemed to constitute a commitment of the lender.

2. Effect of Commitment Fee. Even if the term sheet states that the lender has not committed to make the proposed loan, the lender's receipt of a fee for issuing the term sheet may be sufficient evidence to convince a court to conclude that the lender made a binding commitment to lend, or at least imposes a greater obligation on the lender to act in good faith to attempt to close the loan. Lender's counsel should also be aware of current case law which may, in some circumstances, re-characterize a commitment fee as interest and necessitate a usury analysis.

3. Remedies for Breach. If a court finds that a lender committed to make a loan to a borrower, and the lender refused to honor its commitment, damages for such breach may, in appropriate circumstances, include (a) financing costs incurred by the borrower in borrowing the money from a third party, to the extent such costs exceed the terms for the originally committed loan, (b) lost profits and consequential damages, and (c) punitive and other exemplary damages.

4. Regulatory Issues. Although beyond the scope of this presentation, other limits may be imposed on an insured or otherwise regulated lender's ability to enter into a lending transaction, including "loans to one borrower" limits, restrictions on loan terms applicable to real estate lending generally (imposed by statute or regulation, or institutional lending guidelines adopted pursuant to statute or regulation), and capital adequacy issues.

B. ***Internal Loan Approvals***. Many institutional lenders furnish their attorney a copy of their internal loan approval memoranda (and the supporting narrative), and, as a part of the attorney's loan closing duties, require that counsel confirm in writing that the loan documentation conforms with the terms approved by lender. Even if lender's counsel is not required to confirm to its client that the loan, as closed, conforms to lender's internal approvals, the loan approval memo (and the narrative attached to that memo) can assist lender's counsel in the drafting and negotiation process by clarifying the assumptions and projections which were most important to the lender in committing to the loan. Reference is also made to relevant ethical principles and disclosure requirements generally applicable to an attorney's dealings with an employee or representative of a client acting outside the scope of his or her authority, or otherwise in a manner not in the best interest of the client.

C. ***Term Sheets***. A term sheet is generally intended to be a non-binding expression of intent with respect to the key terms upon which the loan will be made or considered, although there is always some risk that a prospective borrower will be able to construct an argument that the non-binding term sheet was actually a commitment to make a loan or an "agreement to agree" or negotiate in good faith with respect to the proposed loan. A non-binding term sheet may include: (i) a "discussion draft" term sheet, which the lender prepares as a working paper for further negotiations prior to the issuance of a binding commitment or loan documentation; or (ii) a letter of intent or expression of interest which reflects the parties' present intentions regarding a possible loan, but which is not intended to create a binding legal commitment.

When a non-binding letter of intent is used, the parties have not reached agreement on the essential loan terms, but believe that the "term sheet" will serve as a basis for further negotiations and eventual loan documentation - if and when an agreement is reached. Whenever a lender signs any document with respect to its willingness to extend credit, it is essential that the document clearly express the parties' agreement with respect to the binding nature of the proposed loan and any conditions to further discussions. If the lender does not intend to commit to be bound by or committed to the proposed loan, that must be clearly and unequivocally stated in the written commitment letter or term sheet. Similarly, to the extent the lender is aware of specific conditions which must be met (such as legal and business diligence and loan committee approval) before the lender is willing to commit to the loan, those should be clearly stated.

Sample language which may be included in a non-binding term sheet or commitment letter might include one of the following:

> "This term sheet is submitted for discussion purposes only, and is not intended to evidence or create a commitment of the lender."
>
> "This letter is not intended to create a legal commitment of the lender, and the lender shall have no obligation to lend funds unless and until comprehensive loan and collateral documents are negotiated and executed by the lender and the borrower."

D. ***Binding Commitment Letters***. A binding loan commitment should set forth in reasonable detail all of the material terms of the loan. It may provide for the payment of an up-front commitment fee that may or may not be refundable if the loan does not close. If the commitment is a "takeout commitment", it may expressly contemplate that in addition to the borrower's right of enforcement, designated third parties may rely upon and enforce the provisions of the commitment as third party beneficiaries. These third party beneficiaries may include the construction lender, seller, purchaser, or tenant. If the lender does not intend that a third party may enforce the commitment, the commitment should expressly so state. Generally, most commitments provide that they may be enforced only by the borrower and the lender. If appropriate to the circumstances, the borrower, lender and contemplated third party beneficiary may enter into a separate agreement which clearly sets forth the third party beneficiary's rights and remedies with respect to the proposed loan. Most lenders prefer that third party rights with respect to the loan commitment be set forth (and defined and limited) in a separate agreement, and that the commitment itself be enforceable only by the proposed borrower and lender.

The commitment letter should contain the key business (and perhaps legal) points with respect to the proposed loan, including the following: loan amount, type of loan (multiple advance, term, revolver, etc), purpose/ use of proceeds, interest rate, payment terms, maturity, collateral, guaranty requirements, limitations on liability, commitment fees (up-front or during the loan term, based on the unadvanced portion), environmental indemnities, hedging/interest rate protection requirements, conditions precedent, covenants, defaults, due on sale/change in control, syndication and assignment. These terms are generally set forth in a somewhat "short-hand" manner. The commitment letter will also generally include a reference to one of the following: (1) such other documents, covenants or defaults as lender customarily requires in loans of this nature, (2) such other documents, covenants or defaults as lender shall, in its sole discretion, require, or (3) such other documents, covenants and defaults which are mutually satisfactory to the borrower and lender. Obviously, this "mutual agreement" limitation does not provide a great deal of help to the lender in assuring that the definitive loan documents will conform with the lender's policies and practices or the lender's underwriting criteria, and a lender is generally unwilling to enter into a commitment letter that gives the borrower this degree of control over the final loan terms. The lender should in any event endeavor to include any special, unusual or particularly restrictive conditions, covenants and defaults, such as additional collateral or credit support, income, leasing or pre-sale requirements or benchmarks, lock box requirements for property revenues, limitations on or approvals required for leasing, prohibitions on other indebtedness and liens, due on sale and prohibitions against transfer of ownership or management rights, mandatory repairs and renovations, financial or performance covenants, reserves or escrows required to be funded or maintained with the lender or otherwise, material adverse change defaults, etc.

If the lender intends to syndicate the loan, the lender should clarify that it intends to be the sole agent, and clearly identify its maximum total commitment and the maximum total commitment for the entire bank group. The commitment letter should state the efforts the lender/agent will pursue to bring in additional lenders, clarify the borrower's rights, if any, to consent to lenders (or subsequent assignees or participants), and clarify the allocation of costs associated with the syndication efforts.

The loan commitment should specify (in the commitment itself or by reference to side letters) the commitment or other loan fees which are payable upon execution of the commitment, delivery of

drafts of the loan documents, and closing of the loan, and clarify when these fees are deemed to be "earned" and become non-refundable. If the agent lender intends to syndicate the loan, it may wish to include all commitment and agency fees in one or more separate letters to avoid disclosure of agency fees to the bank group and disclosure of initial fees to future bank group members. If the borrower's obligation to pay fees is set forth in one or more side letters instead of the commitment letter and loan agreement, care must be taken to include these obligations, by reference, in the loan documents, and to include these fees within the indebtedness secured by the security documents.

The loan commitment may include the borrower's promise (and sometimes the promise of the borrower's principals or prospective guarantors) to indemnify the lender for its costs and expenses (including attorneys and consultants fees) whether or not the proposed loan actually closes, and may also require that the borrower pay to the lender a "deposit" to cover these amounts. If the lender intends to contract with third party consultants with regard to appraisals, surveys, engineering reports, insurance audits, etc., it is particularly important that the borrower agree to indemnify the lender for these amounts whether or not the loan closes, and the commitment may require that the borrower pay these charges or a portion of these charges prior to closing. In some cases the lender may also require a general indemnity with respect to claims of any third parties arising from the commitment letter (and including third party beneficiaries and claimants under applicable securities laws or in connection with pending or anticipated litigation), whether or not the loan actually closes. If these indemnities are intended to survive termination of the commitment (and even if the loan does not close), the commitment should expressly so state.

IV. INITIAL DRAFTING CONSIDERATIONS. Before lender's counsel begins drafting the loan closing documents, there are certain preliminary issues lender's counsel should resolve.

A. *Length and Sophistication of Documents*. Before beginning preparation of any loan documents, lender's counsel should discuss with the lender the strengths and weaknesses of various approaches to preparation of the loan documents. For example, does the lender want a separate loan agreement, or should the provisions generally found in the loan agreement be spread out among the note, security documents, guaranty, etc.? Counsel should also check to see if the lender has form documents it would prefer to use, and determine the methodology to be used to adapt the lender's form documents to the proposed transaction. Some lenders require that all changes to their standard form documents be made by interlineation or supplement so that the lender's loan administration and servicing representatives can easily identify the negotiated changes to the lender's form documents. A lender may also require that any modifications to the lender's forms be approved by lender's in-house counsel or another designated employee. Counsel should also ask whether the lender and borrower have entered into a similar transaction in the past, or if the lender has promised the borrower to conform its loan documents, to the extent feasible, to the borrower's existing documentation with another lender. If lender's counsel is instructed to conform the closing documents to the lender's forms or an earlier transaction, delivery of the documents on diskette or by e-mail can substantially improve counsel's turn-around time and efficiency if his or her software is compatible or if counsel has (or has access to) the expertise necessary to electronically convert (if necessary) and copy the documents to his or her word processing system.

B. ***Distribution of Documents and Methodology for Redrafts***. As soon as possible, lender's counsel should prepare or obtain from the lender a distribution list containing the name, address, telephone, fax number and e-mail address for each party to the transaction, including the borrower's attorney. If the time line for closing is tight, lender's counsel may also want to request home addresses and telephone numbers for night and weekend deliveries and calls. If borrower's attorney requests that all distributions from lender's counsel to borrower's counsel be simultaneously sent directly to the borrower, lender's counsel may furnish the borrower copies of all documents sent to borrower's counsel simultaneously with delivery to borrower's counsel. Many lenders expect that documents will be delivered directly to the borrower. Therefore, lender's counsel must explain to the lender that absent direction or consent from borrower's counsel, lender's counsel is not allowed to furnish any documents directly to the borrower. It is also helpful at this point to determine if the parties want to provide for e-mail distribution of documents, test the compatibility of the software and determine the best methods for e-mail deliveries to all the parties on the distribution list. All of the parties should be advised that expenses for the transaction will be noticeably higher if hard copy distributions, especially faxes, hand deliveries and massive overnight mailings, are required. Counsel should also make certain that all parties are aware of potential confidentiality problems with the use of e-mail.

If the loan will be secured by real estate in multiple jurisdictions, requiring use of local counsel in addition to the borrower's and/or lender's primary counsel, lender's counsel should determine when the parties would like documents to be distributed to these additional parties. Although it is frequently helpful to have input of local counsel at an early stage, the parties may decide to defer delivery of the documents to local counsel until the documents have been substantially negotiated and approved by the borrower and lender and their respective primary counsel in order to save legal fees and expenses which will be incurred if local counsel is involved in the negotiation process with respect to issues which are not "local counsel" issues. Similarly, if the documents will be distributed to bank group members, tenants or a construction or take-out lender, or their respective counsel, the parties may want to wait and distribute documents after they have been substantially negotiated and are in a form generally acceptable to borrower and lender and their respective primary counsel. However, counsel should remember that these third-party participants may not have the economic incentive to turn the documents around immediately upon receipt, and primary counsel should plan ahead to try to avoid imposing unreasonable deadlines on these other parties.

C. ***Choice of Law***. Because of the location of one or more parties to the transaction, the collateral for the transaction or other loan terms, the parties may wish to choose the substantive laws of another state to govern the transaction. A lender may wish to choose the laws of another state to govern a transaction because the lender is more familiar with the laws of the other state, because the laws of the other state offer more predictability or because one or more loan terms run afoul of the state's legal requirements. Before lender's counsel chooses another state's laws to govern the transaction, lender should confirm with counsel in the chosen jurisdiction that the chosen jurisdiction will recognize the choice of law and that the chosen jurisdiction will provide lender the benefits it is seeking to achieve by choosing that jurisdiction to govern the transaction. Of course, no attorney may draft loan documents to be governed by the laws of a jurisdiction in which the attorney is not licensed, without advice of council licensed in the other chosen jurisdiction.

D. ***The Move to Institute Bankruptcy-Proofing Requirements***. Because of the influence of the capital markets on real estate lending, most lenders for securitized loans and many other lenders are now including in their loan commitments and loan documents protections and inducements to prevent the borrower from becoming the subject of a bankruptcy proceeding. This is done generally by prohibiting the entity from acquiring other assets or incurring additional indebtedness, by controlling the project revenues to prevent the borrower from building a "war chest" from project revenues to finance a bankruptcy, and by requiring outside approval by independent third party directors of a bankruptcy filing. These requirements may reduce, but certainly do not eliminate, the risk of borrower bankruptcy. These provisions are often highly negotiated, particularly those provisions which will interfere with the borrower's daily operations or conflict with the agreements between the principals of the borrower and their equity investors.

1. **Bankruptcy Remote Borrowers**. Many lenders require that the borrower be a "bankruptcy remote" (sometimes referred to as a "special purpose") entity to reduce the risk to the lender that the borrower may become the subject of bankruptcy or insolvency proceedings. The rating agencies (such as Standard and Poor and Moodys) have issued detailed guidelines setting forth their requirements for bankruptcy remote entities, but most lenders require terms substantially similar to the following:

a. at least one outside (or independent) director;

b. the organizational documents of the entity must require unanimous consent of the directors to commence an insolvency proceeding or to acquire additional assets or incur additional indebtedness;

c. the organizational documents of the entity must restrict the entity's activities and powers, and impose limitations on indebtedness and additional liens;

d. the organizational documents of the entity must prohibit amendments to the key provisions of the organizational documents of the entity;

e. impose requirements with respect to the practices and procedures and the books and records of the entity to assure that the entity will not be consolidated with another entity; and

f. obtain a legal opinion regarding "substantive consolidation" issues.

Inclusion of these requirements and restrictions is fairly new and there is often some room for negotiation, particularly with respect to the independent director requirement and the legal opinion. It is frequently difficult for a borrower to find an outside director willing to accept the responsibilities imposed on the outside director under this structure. The lender may not be able to successfully impose the bankruptcy-remote entity requirements on the borrowers if the loan is being made to a group of affiliated borrowers, each of which owns one or more of the projects serving as collateral for the loan, if the borrowers have liability for the entire debt or the projects are cross-collateralized to secure the entire loan, simply because of the assumption or guarantee and cross-collateralization requirements of the loan structure. Other structures may be requested by the lender to protect the lender from insolvency risk, many of which allow the lender to control certain key decisions regarding bankruptcy proceedings and additional assets and indebtedness. To the extent

these requirements allow the lender or its affiliate to control key decisions regarding the borrower, the lender should be aware of the lender liability risks and the possible claims of third party creditors if bankruptcy proceedings are successfully instituted with respect to the borrower.

2. Restriction on Other Assets and Other Indebtedness. In addition to requiring that the borrower's organizational documents restrict the borrower's acquisition of other assets and the borrower's ability to incur additional debts and grant additional liens on the collateral, the lender will generally include covenants in its loan documents prohibiting the acquisition of other assets, incurrence of other indebtedness and granting of other liens without the prior written consent of the lender. Since contributions of shareholders and members to corporations and limited liability companies are sometimes structured as loans instead of capital contributions to avoid certain tax liabilities, the inclusion of these provisions may run afoul of the borrower's internal structure. Lenders may consent to these insider loans if the shareholder/member creditors are willing to execute a subordination agreement subordinating payment of the insider loan to the third party real estate loan. Rating agencies will generally furnish the form of subordination agreement which they require to be executed to evidence this subordination. These subordination agreements will usually require a full lien subordination and at least a partial payment subordination.

3. Controlling the Cash. A lender may limit the borrower's ability to build a "war chest" to finance a bankruptcy proceeding, and if a bankruptcy proceeding is filed, limit the borrower's ability to use project revenues to reorganize, by requiring that all rents and revenues from the date of the loan closing forward be paid to the lender, and restricting the borrower's access to such funds. Lender may require that all project rents and revenues be paid directly to the lender or to a designated lock box account, with revenues to be distributed to the borrower only upon satisfaction of agreed-upon conditions and for agreed-upon purposes. The lender may also require that reserves and escrows be established and held by the lender (or in an account assigned to the lender) to pay taxes, insurance, ground lease payments, tenant finish, leasing commissions, and other contemplated renovations and repairs. The lender should, of course, take care to properly perfect its assignment of these reserve and escrow accounts as a preventive measure in the event a bankruptcy proceeding is instituted or a third party claims a prior interest with respect to these funds.

4. Personal Liability Inducements. Many lenders require that, notwithstanding certain limitations on liability set forth in the loan documents, the borrower, guarantors and other financially solvent principals will have full personal, partnership and corporate liability for the repayment of the debt in the event the borrower becomes the subject of a bankruptcy proceeding or any of the covenants of the loans documents pertaining to the "bankruptcy remote" requirements are violated. Although most authorities believe these "springing liability" provisions will probably not be effective with respect to the borrower if the borrower becomes the subject of a bankruptcy proceeding, they should be effective with respect to solvent third party guarantors and, to the extent those guarantors have control over the activities of the borrower, may be a substantial inducement to the borrower to avoid violating these provisions. A guarantor may try to negotiate provisions to provide that its liability will not "spring" unless that guarantor is responsible for the triggering act (*i.e.*, that guarantor caused or consented to the bankruptcy filing or to the covenant violation). If the lender includes the "springing liability" provisions to punish the guarantor for a violation of the loan requirements, the lender may agree to limit the guarantor's liability to situations caused by that guarantor. However, many lenders include the "springing liability" provisions because the lender's agreement to enter into a non-recourse or limited recourse loan is based upon the assumption that if a

default occurs, the lender will be able to foreclose the project swiftly and without a contest. If the lender's remedies are contested or delayed due to a bankruptcy filing, regardless of the reason for the bankruptcy, the lender is not getting one of the principal benefits of the bargain it negotiated, and the lender may require credit support from each guarantor without reference to the fault of each guarantor or the guarantor's involvement in the bankruptcy filing.

V. <u>DUE DILIGENCE</u>. Before lender's counsel begins preparation of his or her own due diligence checklist for a specific transaction, lender's counsel should check with the lender to see if the lender has any internal checklists or other document submission requirements that its lending policies or loan administration procedures require be submitted. This is especially important if, in conjunction with the closing, lender's counsel will be asked to sign a certificate stating that he or she obtained and reviewed a specified list of documents and information. In any event, counsel should have his or her own "generic" due diligence checklist prepared, and customize that checklist to fit the transaction as outlined in the loan commitment, term sheet, committee approval, and other information furnished by the lender. I have attached to this article a generic Due Diligence Checklist which you may find helpful. It is important that lender's counsel prepare the Due Diligence Checklist immediately and furnish a copy to the lender for its review. The lender will then determine which items on the Checklist the lender wishes its counsel to request and review. If the lender determines that it does not want its counsel to request and review some of the documents shown on this Checklist, counsel can complete the applicable Checklist items with the word "waived" in the applicable lines to indicate that the lender instructed counsel not to review same. Additionally, if any of the items on the checklist are not applicable to the transaction, counsel can insert "N/A" in the applicable blocks to the right of the document/information description to indicate the information was considered and deemed to be unnecessary for the transaction. Including a time and date stamped "header" on the Checklist is helpful so that over the course of the transaction, counsel can periodically update the Checklist for distribution to all the transaction parties. After receiving the lender's input with respect to the Checklist, counsel should furnish a copy to the borrower's attorney as quickly as possible so that the borrower and the borrower's attorney can begin assembling the required documentation while lender's counsel is preparing the initial drafts of the loan documents. The attached form of Checklist is also helpful because it indicates responsibility for providing the requested information and documentation, and should insure that the responsible party does not fail to order critical information in a timely manner because of confusion over responsibility for obtaining the information. By preparing and distributing the Checklist in this form, lender's counsel will also be able to re-create why certain due diligence documents and information were not required for closing, avoid missing due diligence information because of confusion concerning the lender's requirements or responsibility for obtaining certain information, and easily distribute current status reports with respect to the due diligence matters.

A. ***<u>Organizational Documents</u>***. Items 1 through 5 on the Due Diligence Checklist list the organizational documents lender's counsel may request for its review during the due diligence process. Note that the Checklist lists the required documents for corporations, limited partnerships, general partnerships, limited liability companies and trusts. Unless otherwise instructed by the lender, lender's counsel should obtain organizational documents for each direct or indirect signatory of any loan document which is affiliated with the borrower. With respect to third party signatories unaffiliated with the borrower, the lender may want to rely upon a legal opinion regarding existence, authority and (perhaps) enforceability, or the lender may direct lender's counsel to depend upon the apparent authority of the individual executing the document on behalf of an unaffiliated third party.

The term "principal" in items 1-5 of the Checklist refers to each direct and indirect signatory of each entity signing any of the loan documents which is the borrower or affiliated with the borrower. For example, if the borrower is a limited partnership, whose sole general partner is a limited partnership, whose sole general partner is another limited partnership, whose sole general partner is a limited liability company, whose sole managing member is a corporation, lender's counsel should request organizational documents for the borrower, the first and second tier limited partnerships which are general partners, the limited liability company and the corporation. As discussed above, the lender may request that its counsel depend upon legal opinions from third parties or representations from the borrower or other signatories with respect to these matters in order to reduce legal fees and accelerate the due diligence process.

B. ***Title Review***. Item 6 on the Checklist lists the information which should be obtained in order to review the current state of title of the property. Obviously, lender's attorney should review not just the title commitment, but the underlying documents giving rise to each exception to title shown in the title commitment, including all exceptions listed on Schedule B and Schedule C of that title commitment. If the title commitment shows that memoranda have been recorded which reference unrecorded documents, lender's counsel must obtain copies of and review those unrecorded documents. The lender's counsel may also want to require that the unrecorded documents be certified to confirm that the document furnished is a true, correct and complete copy of the document referenced in the recorded memoranda. Because of the change in the UCC, UCC searches should be obtained for the borrower and prior owners in the county in which the property is located, the central UCC filing office for the state in which the property is located, and in the state in which the borrower's chief executive office or principal place of business is located, or its state of incorporation/registration.

C. ***Survey***. Lender's counsel should furnish to borrower's counsel, as soon as possible, the form of surveyor's certification the lender will require, and request that the form of certification be furnished to the surveyor immediately. The borrower will then be responsible for delivering the survey with a certification which conforms to the lender's survey requirements, without delay or additional expense. In ALTA jurisdictions, minimum survey requirements generally include preparation of a survey in accordance with the "Minimum Standard Detail Requirements for ALTA/ACSM Land Title Surveys," jointly established and adopted by ALTA, ACSM, and NSPS in 1999 and meeting the "Minimum Angle, Distance and Closure Requirements for Survey Measurements Which Control Land Boundaries for ALTA-ACSM Land Title Surveys." As an additional measure, prudent lenders will require that the survey contain items 1, 2, 3, 4, 6, 7(a), 7(b), 8, 9, 10, 11, 13, 14, 15, and 16 of Table A to those standards.

Counsel should locate on the survey each exception to title listed on the title commitment, confirm that each item shown on the survey appears in the title commitment, and confirm that the survey contains an appropriate flood plain certification and clearly indicates appropriate access to dedicated and accepted public streets.

D. ***Flood Certification***. In addition to the standard certification usually included in this surveyor's certificate with respect to flood hazard designations, national banks and certain other lenders are required to obtain flood certification forms for real estate loans. See the National Flood Insurance Act of 1968 and the Flood Disaster Protection Act of 1973, as amended, and codified at 42 U.S.C. 4001-4129.

E. ***Tax Information***. The title company should obtain the tax information with respect to the real estate collateral, which tax information should include the current taxes (if assessed), the payment status of taxes for prior years, and any exemptions applicable to the property. If the state in which the land is located provides for "agricultural valuations," the parties should confirm that the property was not taxed for the current or prior years based upon an agricultural valuation, or the borrower and lender should be advised of the economic implications of that designation.

F. ***Permits and Licenses***. Lender's counsel should discuss with the lender the permits and licenses, if any, the lender wants its counsel to review in connection with the due diligence process. Item 10 on the attached Checklist lists only a few of the more important permits that lender may want to review in connection with its due diligence activities, although many more permits are required for an owner/operator of an operating property, particularly hotels. If project operations involve the sale of alcoholic beverages and lender's counsel is not familiar with the unique issues associated with liquor licenses, further review of those issues would be appropriate. Because a liquor license is not assignable in many states, the lender must understand the risks it will face upon foreclosure, and be prepared to take appropriate steps to obtain the required liquor licenses if the lender becomes the owner of the project.

If the proposed loan is a construction loan, the lender should require delivery of a copy of applicable permits for grading and site work and the building permit. If the borrower fails to deliver these permits at closing, there is some risk that the contemplated structure will not be able to be built because the necessary governmental approvals of the plans and specifications cannot be obtained.

If the proposed loan is not a construction loan, the lender should require delivery of a copy of the final certificate of occupancy for the building as a whole and any separately completed tenant spaces. If the tenant does not have a copy of these certificates of occupancy in its files, they can be difficult (or impossible) to obtain from the applicable governmental authorities, particularly for older buildings. The borrower can, for a fee, require that the city re-inspect the property and issue a current compliance certification, but most borrowers and lenders are unwilling to open these issues with the governmental authorities in connection with the loan process. If city verification of compliance cannot be obtained, the lender may have to depend upon a certificate from an architect or engineer and/or a representation from the borrower.

G. ***Availability of Utilities***. If the loan is a construction loan or substantial renovations are contemplated which will increase the utility needs for the project, the lender should require delivery of a letter from each utility whereby the utility agrees to furnish service in a capacity sufficient to meet the anticipated needs of the project. If the borrower will be responsible for any of the costs associated with extending service to the project, the letter should also confirm those costs.

H. ***Zoning***. There are three (3) major issues with respect to the zoning of a project: the applicable zoning designation, what the zoning designation means, and whether the project complies with the applicable zoning requirements (including applicable "grand-fathering"). The borrower's counsel should obtain from the City a letter designating the applicable zoning for the property, and also furnish lender's counsel a copy of the applicable zoning ordinances so that lender's counsel can understand the zoning designation. In some states, a zoning endorsement is available from the title company which insures (with certain limitations) that the project as currently constructed and operated, complies with applicable zoning requirements. Additionally, borrower's counsel may be willing to issue a zoning compliance opinion or to include zoning compliance assurances in its opinion letter, although attorneys in some states are not generally willing to give zoning opinions. Until fairly recently, many cities were willing to issue zoning compliance letters, although they frequently stated on their face that they were not binding on the city. More recently, cities are unwilling to issue these non-binding compliance letters. Lenders are sometimes required to depend upon zoning compliance letters issued by the architect or engineer for the project (if the project is fairly recently constructed). If the project is an older project, and the borrower was not involved in the construction of the project, the lender may have to satisfy itself with a review of the current "open and obvious" zoning criteria (such as number of parking spaces, floor area ratio, use, etc.), and depend upon the certificate of occupancy and the historical operation of the project for evidence of compliance with zoning.

I. ***Confirmation of Compliance With Laws***. In addition to a certification regarding zoning compliance, the lender should receive appropriate third party assurances that the project complies with applicable laws, including zoning requirements, restrictive covenants, the Americans With Disabilities Act, the Fair Housing Act and similar state law requirements. With respect to federal laws, the lender will probably have to depend upon the borrower's representations, and may also require that the borrower obtain a certification from a knowledgeable third party architect or engineer regarding compliance with other laws (including the Americans With Disabilities Act and, to the extent applicable, the Fair Housing Act).

J. ***Plans and Specifications***. If the proposed loan is a construction loan, the lender should require delivery of the preliminary and final plans and specifications so that the lender's representatives can verify compliance with laws and budgetary assumptions, and otherwise verify compliance with the construction requirements of the lender and relevant third parties (such as a purchaser, tenant or take-out lender). Of course, this review is not a substitute for independent verification of compliance from such third parties. Many times the final plans and specifications will not be ready at the closing of the construction loan. In that situation, the lender must understand and assume the risk that the building may not be able to be built in the manner, at the cost, or in accordance with the contemplated schedule. Even if the project is not newly constructed, the lender should obtain copies of the plans and specifications for the initial construction and all renovations for the project. These plans and specifications will be invaluable if the lender becomes the owner of the project and, at that time, the borrower may not be willing to furnish this loan information.

K. ***Architectural Approval/Subdivision Restriction Compliance Confirmation***. If the project is subject to any restrictive covenants or other deed restrictions which require that all improvements be constructed in accordance with standards set forth in such restrictions, or that the plans and/or finished project be approved by the architectural review committee set up by such restrictions, lender's counsel should obtain written confirmation of compliance.

L. ***Waiver of Repurchase Rights***. If any restrictive covenants or deed restrictions affecting the property provide that the seller or another person or entity may repurchase the property if construction is not commenced by a certain date or if the improvements fail to comply with the stated requirements, lender's counsel may be instructed to obtain a written waiver of such repurchase rights and cause the written waiver to be filed in the real property records of the county in which the property is located. In any event, if the repurchase right are not waived, upon satisfaction of the condition, the holder of the repurchase rights should confirm such satisfaction in an instrument filed in the real estate records.

M. ***Waiver of Right of First Refusal***. If the seller or any other person or entity has a right of first refusal with respect to the property, lender's counsel should obtain a waiver of such right of first refusal, in recordable form, if the right of first refusal itself is of record. If the party holding the right of first refusal is not willing to completely waive this right of first refusal, lender may decide to accept a waiver or confirmation that the right of first refusal will not be applicable to any foreclosure sale or deed in lieu of foreclosure. Although options to purchase are not mentioned in the checklist, if the lender's counsel due diligence review discloses any such option to purchase in favor of a third party, that information should be disclosed to the lender and the economic impact of that option assessed. If the option is unacceptable to the lender, it, too, must be waived in a similar manner.

N. ***Appraisal***. As a general rule, an insured financial institution will be required to obtain an appraisal of the real estate for a traditional real estate loan. A more detailed discussion of the circumstances in which an appraisal is required is beyond the scope of this article. If the cost of this audit is to be paid by the borrower, the commitment and the loan documents should expressly so state. If the costs are to be paid by the borrower even if the loan does not close, the commitment should expressly state that borrower's payment obligations survive termination of the commitment, whether or not the loan closes. Even if the borrower is unwilling to agree to pay for subsequent appraisals, the borrower should agree to give lender's appraiser access to the project and relevant documents and information for lender's appraiser to complete the appraisal.

O. ***Insurance***. Generally, the lender will require property insurance (all risk, after completion, and builder's risk, during construction), liability insurance and, in appropriate cases, "operational" types of insurance, such as worker's compensation, etc. Lender's counsel should note that delivery of a certificate of insurance to evidence compliance with insurance requirements almost certainly provides inadequate information for the lender to evaluate compliance with its insurance requirements. The lender may also want to obtain an "insurance audit" from its internal risk management department or an outside insurance professional to review and analyze the policies, certificates and other evidence of insurance submitted by the borrower. If the cost of the third party insurance audit is to be paid by the borrower, the commitment and the loan documents should expressly so state. If the costs are to be paid by the borrower even if the loan does not close, the commitment should expressly state that borrower's payment obligations survive termination of the commitment, whether or not the loan closes.

P. ***Environmental Assessment***. A current environmental assessment of the real estate is a standard closing requirement. Lender's counsel should discuss with the lender whether the lender intends to review the environmental assessment internally, or whether counsel should be responsible for such review. If the lender commissions the environmental assessment, it should request submission of the report in draft form before it is finalized, and the lender should consult with the borrower and lender's counsel before commissioning a Phase 2 or other more "intrusive" environmental investigation. If the cost of this audit is to be paid by the borrower, the commitment and the loan documents should expressly so state. If the costs are to be paid by the borrower even if the loan does not close, the commitment should expressly state that borrower's payment obligations survive termination of the commitment, whether or not the loan closes. Lender's counsel should also determine whether the environmental assessment will be required to include wetlands and endangered species information (and sometimes an air quality and/or mold and fungus investigation), and advise the borrower accordingly.

Q. ***Architect/Engineer's Audit***. For a construction loan and for a loan made on property which is already improved, the lender may want an independent architect or engineer to inspect the property and give a report as to the current condition of the property. The lender may also want its architect or engineer to independently verify or confirm compliance of the plans and specifications with applicable laws and zoning requirements and any other applicable requirements of the lender. If the cost of this audit is to be paid by the borrower, the commitment and the loan documents should expressly so state. If the costs are to be paid by the borrower even if the loan does not close, the commitment should expressly state that borrower's payment obligations survive termination of the commitment, whether or not the loan closes.

R. ***Ground Lease***. Lender's counsel should obtain a copy of any ground lease affecting the property and all amendments and assignments thereto, copies of all recorded documents concerning the ground lease (which should be furnished by the title company in connection with the title commitment), and copies of any prior estoppel letters and agreements signed by the ground lessor. These prior estoppels and agreements may assist the lender's counsel in preparing an estoppel and agreement for the subject transaction in a form which may be more easily signed by the ground lessor.

S. ***Space Leases***. The lender should determine whether the space leases will be reviewed internally by the lender to determine compliance with the lender's underwriting criteria, or if the lender wishes lender's counsel to be involved in this process. If lender's counsel will be involved, lender's counsel should reach a clear understanding with the lender with respect to its scope of review. In any event, borrower and its attorney should be required to submit full and complete copies of all space leases affecting the property, along with a summary of the material legal and business terms found in such leases. The lender may also want to require copies of any material correspondence with respect to the space leases.

T. ***Equipment Leases and Conditional Sales Agreements***. The lender should determine if it wants to require that these documents be furnished and, if it does, whether lender's counsel should be involved in the review process. The borrower should in any event be required to deliver a summary of these contractual arrangements because they will affect the value and operational ability of the project following foreclosure if the foreclosure will not result in the lender becoming the owner of the equipment necessary for the operation of the project.

U. ***Operating/Service Agreements***. The lender should determine if it wants to require that these contracts be delivered and, if it does, whether lender's counsel should be involved in the review process. In many cases, and particularly in larger transactions, the lender may want to require delivery of only "material" agreements, which can be defined by the purpose or term of the agreement, or the aggregate annual payments under the agreement, and may in any event include service agreements with respect to significant operational functions of the project.

V. ***Management and Franchise/License Agreements***. Lender and its counsel should review all management and franchise or license agreements affecting the project. Material terms of these agreements generally include the length of the agreement, payment and lien priorities, operational standards and performance requirements imposed on the parties, the payments required under the agreement, lender's rights to property rents and revenues following default, any lien and purchase rights in favor of third parties, and the lender's right following foreclosure or deed in lieu of foreclosure to assume or terminate these agreements.

W. ***Purchase and Sale Agreements***. If the loan proceeds will be used to acquire the property, lender's counsel should review the Purchase and Sale Agreement pursuant to which the borrower will acquire the property. Significant terms may include verification of price, restrictive covenants, repurchase options, architectural approval, and liens and assessments which may be placed upon the property at closing. Additionally, the lender's counsel should investigate any material post-closing obligations of the seller and any escrow arrangements which will be set up to secure or fund such performance.

X. ***Existing Loan Documents***. If, in connection with the subject transaction, the existing lender will assign its loan to the new lender, the new lender and its counsel will need to obtain and review the existing loan documents. However, this review is not a substitute for appropriate waivers in the documents with respect to defenses, claims, etc., arising under these prior loan documents. In most states, the prior loan documents are generally assigned to the lender only when the lender needs to establish lien priority. In other states, the assignment may be used to avoid additional mortgage or stamp taxes.

Y. ***Other Loan Documents***. If subordinate or superior liens will exist on the property, the lender and its counsel must review all of these documents (both recorded and unrecorded) and analyze the respective positions of the lender with respect to the collateral, payment terms, rights and remedies, in order to prepare appropriate tri-party and intercreditor/subordination agreements for closing. Additionally, if the borrower's balance sheet discloses any "insider debt", the lender and its counsel should also review copies of any documentation which evidences that loan.

Z. ***Take Out Loan Commitment***. If the borrower is delivering a take-out loan commitment or other third party commitment from a third-party lender, the lender and its attorney should review that document prior to closing to evaluate its enforceability, and in order to prepare an appropriate tri-party agreement for closing.

AA. ***Budget***. Prior to closing, the borrower should submit for lender's approval a construction budget, if construction or significant renovations or repairs will be required after closing, and an operating budget with respect to the project for the current year or following completion of the project. Some lenders also require a three or five-year pro forma budget for the project.

BB. ***Project and Financial Information***. Prior to closing, the borrower should submit for the lender's review a current rent roll, copies of current marketing materials, a summary of pending marketing efforts, financial information on the project and financial information with respect to the borrower and each guarantor. This information may be submitted directly by the borrower to the lender, although the lender may want its counsel to prepare appropriate certifications with respect to financial information delivered. These certifications may also be included as representations in the applicable loan documents.

CC. ***Pledges of Ownerships Interests***. If the lender is going to require a pledge of an ownership interest or stock to additionally secure the loan, the lender's counsel should review copies of all applicable organizational documents, and all amendments thereto, with respect to the pledged interest or stock. If counsel's review discloses that any stock is restricted (contractually or by application of securities laws), lender and its counsel should evaluate the effect of such restrictions on the transferability and resulting value of the pledged stock, and determine whether further documentation, waivers or registrations will be required.

VI. DRAFTING THE LOAN DOCUMENTS. After the Due Diligence Checklist has been circulated to all parties, lender's counsel should begin preparation of the Loan Document Checklist. I have attached to this article a generic form of Loan Document Checklist which can be revised to fit the transaction after counsel's review of the loan terms and the initial drafting considerations outlined in this article. This Checklist should also include a time and date-stamped "header" so it can be easily circulated among the parties to update the status of negotiations and used as a closing checklist to confirm that all required documents have been executed and delivered at closing. Lender's counsel should attempt to obtain all information necessary to complete the loan documents prior to closing, so that the final documents require only execution. If blanks or other information must be supplied at closing, it is helpful to list the outstanding items on the Loan Document Checklist so the parties do not forget to complete these items, which are frequently administrative and deemed to be less important than the actual execution and delivery of the documents. Before closing and funding the loan, lender's counsel should verify that each document has been executed and delivered, and that every line of every column in the Checklist has been checked off.

A. ***General Drafting Considerations***. In the rush to finalize the substantive (and more difficult) aspects of the transaction, the parties frequently fail to supply or otherwise agree upon the more mundane issues associated with the loan closing documents. Early consideration and resolution of these issues can assist in counsel's efforts to provide a quick and efficient closing. Lender's counsel should address the following issues early in the loan preparation and negotiation process, and incorporate them into the document drafts:

1. **Notice Information**. The borrower and lender should determine where and to whom official notices should be sent, the manner of delivery which will be allowed (such as personal delivery, overnight courier, certified mail, fax, etc.) and when (and if) notices will be "deemed"

received for purposes of the documents. Conflicting notice provisions (and the resulting uncertainty which will arise when the parties attempt to give notices under the documents) can be avoided by setting forth the notice provisions in only one of the loan documents (usually the loan agreement), and referencing or incorporating those notice provisions by reference in the other documents.

2. **Format for Recorded Documents**. Counsel should confirm that all documents to be recorded comply in form and in substance with all applicable state and local law requirements.

3. **Execution**. Lender's counsel should determine if the documents will be circulated for execution prior to closing or if the parties will actually attend the closing. If multiple counterparts or faxed signatures will be used, appropriate provisions should be inserted in the loan documents to confirm the validity of such signatures. If faxed signatures will be allowed for closing, but follow-up of original signatures will be required, lender's counsel may also want to incorporate these post-closing delivery obligations in the loan documents. If the parties know the names and applicable titles of the individuals who will be signing the documents on behalf of the transaction parties, that information should be inserted in the signature blocks prior to closing, and all acknowledgments should be completed. Completing the signature blocks and acknowledgments prior to closing can save substantial time at the closing. Some states require that certain documents be signed, witnessed or otherwise verified or confirmed by an additional officer or representative of the signing entity if the document will be recorded in the real property records, and lender's counsel should confirm that the final signature blocks will comply with all local requirements. Multiple signatories may also be required by the organizational documents of a signatory.

4. **Post-Closing Requirements**. If the lender agrees that certain items on the Due Diligence Checklist or the Loan Document Checklist can be delivered after closing as a post-closing matter, the borrower's obligation to deliver these specific items should be incorporated into the loan documents to be enforceable. If the parties prefer to memorialize their agreement with respect to these post-closing items in a side letter, lender's counsel should confirm that the default language in the loan documents is sufficiently broad to include borrower's failure to perform as required by the side letter.

5. **Tax Identification Number and Organizational Number**. The borrower should furnish its tax identification number and its organizational number. Not all states issue organizational numbers. However, if the state issues such number it should appear on the articles (or certificate) of incorporation certified by the applicable Secretary of State.The lender will need the borrower's tax identification number for the loan administration process, to comply with tax and other governmental reporting requirements and to set up any bank accounts required by the loan documents. The tax identification number and the organizational number are frequently incorporated into the documents (usually the representation section of the loan agreement) for the lender's convenience. Additionally, some states and the multistate UCC form require that UCC financing statements include the organizational number for the debtor. A call to the UCC Division of the applicable state filing authorities is recommended to clarify the filing requirements.

6. **Corporate Seals**. Some states require that a corporate signature be "sealed" by stamping the corporation's seal on the document. A few states even require that the seal be embossed, and that a "stamp" seal is insufficient. If corporate seals will be required, counsel should

notify the parties well in advance so the parties have time to locate or adopt a corporate seal for closing. Failure to include the seal may affect the enforceability of the documents and the ability to have the documents recorded in these jurisdictions.

7. **Multiple Execution Copies**. Lender's counsel should determine in advance the number of copies or original counterparts of each closing document the parties will require, and prepare (or circulate) a sufficient number of execution counterparts so that each party can leave the closing with the requested number of original counterparts of each closing document. The closing will proceed more quickly and the post-closing delivery burdens on the lender's counsel will be lightened if full sets of original, signed documents can be distributed at the closing table, without delays for copying. Lender's counsel should also prepare an additional original counterpart of each document to be recorded for the title company. Of course, the borrower should only sign one (1) original note, which should be delivered to the lender, and all other transaction parties should receive only a copy of that note.

8. **Out of State Filings**. If any documents need to be filed in any office or jurisdiction outside of the state of closing, lender's counsel may want to provide to the title company the place of filing (including the address), the name of the records in which the documents should be filed, and any filing fees or other stamp or mortgage taxes that will be required. Primary lender counsel should consult with local counsel to confirm that the form and substance of the documents comply with local requirements. If a jurisdiction requires payment of a mortgage or stamp tax, these amounts should be paid to the title company, and all necessary affidavits or certifications required in connection with such taxes should be prepared, executed and delivered. Primarily lender counsel may also confirm that local restrictions do not prohibit the borrower from paying such taxes.

B. ***The Loan Agreement***. A loan agreement is a written agreement governing the central elements of the lending relationship. Some lenders prefer not to have a loan agreement and, instead, spread the provisions normally found in the loan agreement among the note, deed of trust, etc. The loan agreement generally includes the following provisions:

1. **The Lender's Commitment to Lend**. The loan agreement should set forth (a) the details regarding the lender's commitment to lend (including the borrower's ability to repay and reborrow, *i.e.*, a "revolving loan", if applicable) and the conditions precedent to the lender's obligation to make any advance, (b) the maximum amount and duration of the lender's commitment to advance funds, including any circumstances or events pursuant to which the maximum loan amount may be increased or decreased, and (c) the right of lender to terminate its commitment to lend if an event of default, or an event which would, with the giving of notice or passage of time, or both, constitute an event of default occurs.

2. **The Purpose the Loan**. If the lender wishes to restrict the manner in which the borrower may use the loan proceeds, the loan agreement should expressly so state.

3. **Repayment Terms**. This section of the loan agreement describes the interest rate and the default interest rate, any late payment fees, and principal and interest payment requirements. This section should also state whether prepayments will be allowed, and any limitations on the right to prepay, including prepayment penalties. If the borrower will have options to select interest rates during the loan term, specific procedures should be included for the borrower

to select LIBOR, CD rate, T-Bill rate, prime or other pricing options. Most lenders require that notice of LIBOR pricing be delivered three (3) eurodollar business days prior to the first date of the applicable eurodollar interest period, and that the rate will be set two (2) eurodollar business days prior to such first date. Shorter notices are generally allowed for other types of pricing. If the borrower will have the option to extend the term of the loan upon satisfaction of certain conditions, the borrower's extension options and any conditions thereto should be expressly set forth in this part of the loan agreement. Many of these provisions may be contained in the promissory note but, for ease of reference and because many of the pricing and prepayment penalty provisions are lengthy, these provisions are frequently contained in the loan agreement. Additionally, yield maintenance, capital adequacy, pricing availability, taxing and withholding protections and breakage costs (with respect to LIBOR and other appropriate types of pricing options) should also be clearly set forth in this section of the loan agreement.

4. Representations and Warranties. Representations and warranties in a loan agreement generally include the following issues:

a. The existence, good standing, and qualification of the borrower in all requisite jurisdictions.

b. The status of significant or burdensome contracts and material litigation.

c. Compliance with applicable laws and regulations, the organizational documents of the borrower, and all agreements and arrangements to which the borrower is subject.

d. Accuracy of documents and information submitted by or on behalf of the borrower.

e. Certification of financial statements and statements as to no material change since the date of such financial statements.

f. Confirmation of any conditions precedent to the loan closing required by the lender (such as equity contributions, preleasing or leasing requirements, net worth, revenue, net income and cash available for debt service requirements, etc.).

g. Confirmation with respect to the ownership, title, condition, construction, development, operation, leasing and use of the project.

h. Confirmation of owned, leased and financed tangible personal property at the project.

i. Rent roll certification and other representations with respect to the leases.

j. Enforceability of the loan documents.

k. Non-existence of any default or event which, with the giving of notice or passage of time, or both, would constitute a default.

l. Bankruptcy remote/special purpose entity requirements.

m. Payment of taxes and claims.

n. Full disclosure ("there is no fact known to borrower that borrower has not disclosed to lender which would have a material adverse effect on the borrower or the project").

The representations and warranties should be made, and should be true and correct, as of the date of closing and initial funding of the loan. If the loan is a multiple advance loan, the lender should determine whether the representations and warranties should be remade effective as of the date of each subsequent advance under the loan. If the lender so intends, the loan agreement should clearly state that each request for advance will constitute (and the advance request should expressly include) a restatement of such representations and warranties effective as of the date of each subsequent advance.

5. Reserves and Accounts. The loan agreement should set forth borrower's obligations to establish and maintain any reserve or collateral accounts, set forth the limitations on the borrower's right to request, and the lender's obligation to authorize, withdrawals from such accounts, and the lender's rights and remedies with respect to such funds upon the occurrence of a default. The loan agreement should also set forth the obligation of the borrower to pay and cause to be paid all project rents and revenues to a lock box and otherwise comply with lender's cash management requirements, if applicable.

6. Covenants. The loan agreement should contain the ongoing obligations and agreements of the borrower during the loan term, and which may include the following:

a. It is helpful if all of the borrower's post-closing obligations to furnish financial and other information and reports are set forth in one place in the loan documents. These obligations are generally referred to as the "reporting requirements", and may include the following:

(1) monthly or periodic financial information, including unaudited financial statements (for the period in question and year to date), a reconciliation of actual revenues and expenses to the budget, a current rent roll and, if applicable, calculation of accounting information necessary to verify compliance with financial covenants.

(2) Annual [*audited*] financial statements and, if applicable, calculation of accounting information necessary to verify compliance with financial covenants.

(3) Periodic (or annual) officer's compliance certificates, wherein the officer states that a review of the activities of the borrower and the project has been made under his or her supervision and, to the best of his or her knowledge after reasonable and due investigation, no default has occurred under the loan documents or any other material agreement, and there is no material pending litigation or claims for such litigation.

(4) Material notices from or to governmental authorities.

(5) Annual operating budgets.

(6) Tax returns (if applicable, and as limited by legal requirements).

(7) Notices with respect to material agreements.

(8) Material determinations in material litigation and proceedings affecting borrower, any other obligor or the project.

(9) Material changes in any representation or warranty.

(10) The occurrence of a default under any other indebtedness of the borrower or any other obligor.

(11) The borrower or any other obligor becomes liable with respect to additional indebtedness.

(12) Additional liens on the collateral.

(13) Any distribution, dividend or insider loan repayment.

(14) Any name change with respect to the borrower or any obligor.

(15) Any amendment of the organizational documents of borrower or any obligor.

(16) The occurrence of any event which constitutes or would, with the giving of notice or passage of time, or both, constitute an event of default under the loan documents.

(17) Notice (and a copy) of each post-closing material operating agreement, equipment lease or purchase money financing for personal property with respect to any of the mortgaged property.

(18) Financial information with respect to other parties (such as other obligors and pledgors, tenants, purchasers, etc.).

(19) Such other information concerning the business, properties or financial condition of the borrower or any other obligor or pledgor as lender may from time to time [*reasonably*] require.

b. Covenants with respect to leases (including limitations on the borrower's ability to enter into leases without the lender's consent, to modify any lease, to declare a default under or terminate any lease, to collect rents for more than one month in advance, to pledge or otherwise transfer any leases or rents, etc.)

c. Standard covenants regarding the construction, management, maintenance, repair and alteration of the project.

d. Standard covenants regarding the use of the project.

e. Borrower's agreement to maintain appropriate interest rate hedging arrangements with respect to the debt, consistent with the terms of the loan.

f. Lender's inspection rights with respect to the project and its books and records.

g. Compliance with governmental requirements, leases and material agreements.

h. Post-closing appraisal provisions (even if the borrower is not obligated to pay for post-closing appraisals, the lender should include provisions whereby the borrower agrees to cooperate with lender's appraiser if lender from time to time determines that such an appraisal is necessary).

i. General insurance requirements of the lender and the borrower's obligation to maintain such insurance.

j. Payment of (and the right to contest) taxes and claims with respect to the project (and including the terms and conditions upon which lender will allow liens to attach the property).

k. Payment of lender's costs and expenses (including legal fees) incurred in connection with the loan closing and the subsequent administration and enforcement of the loan. Additionally, if the borrower has agreed to pay for any post-closing syndication costs of the lender, the documents should expressly so state.

l. General indemnity of the lender, and its officers, employees, agents and affiliates. Issues for negotiation will generally include the scope (generally, all claims arising out of the project and the lending transaction, and which may include a "tax gross-up" for payments made under the agreement other than principal and interest payments), exclusions for lender's (gross) negligence or willful misconduct, and lender's right to choose and retain separate counsel. The parties must also negotiate consents required for settlement of claims.

m. Further assurances (essentially, borrower's agreement to execute and deliver or cause to be executed and delivered such additional documents as lender may from time to time require to evidence the agreement of the parties with respect to the loan).

n. Limitations on name change and accounting terms, as well as consolidation, merger or conveyances of all or substantially all of the borrower's or any other obligor's assets.

o. Limitations on transactions with affiliates (either a complete limitation or a requirement that the terms of any arrangements with affiliates be no less favorable than are generally available in the marketplace).

p. Limitations on equipment leases and financed purchases of personal property necessary for the operation of the project.

q. Limitation on easements, changes in zoning and new construction without the lender's consent.

r. Limitation on additional indebtedness.

s. Limitation on dividends, distributions and insider loan repayments from project revenues.

t. Subordination of payments to affiliates and other cash flow management requirements.

u. Financial or operating benchmarks or covenants.

v. Limitations on the borrower's right to amend, terminate or enter into any material agreement without the lender's consent.

7. **Events of Default**. The loan agreement generally sets out all of the events of default and, to avoid confusion and conflicting provisions, each other loan document should refer to the events of default set forth in the loan agreement, without restatement of such defaults. Events of default may include the following:

a. Payment defaults (including any applicable notice and/or cure rights applicable to specific payment defaults).

b. Breach of any covenant, agreement, obligation or condition set forth in any loan document (including any notice and/or cure rights specifically applicable to covenant defaults).

c. Breach of any representation or warranty in any loan document.

d. The occurrence of any default or event of default under any other loan document.

e. With respect to borrower and each other obligor and pledgor: bankruptcy or insolvency, receivership, default under other material indebtedness, failure to pay material judgment, liquidation, dissolution or termination, death or disability.

f. Material adverse change with respect to the project or the financial condition of the borrower or any other obligor or pledgor.

g. Any of the loan documents shall for any reason cease to be in full force and effect, or be declared null and void or unenforceable in whole or in part, or the validity or enforceability of any loan document is challenged or denied by any party other than lender.

h. Material condemnation or casualty with respect to the project (with appropriate exclusions if the parties agree the project will be repaired with the insurance proceeds).

i. Any transfer, sale, lease, mortgage, pledge, etc., of all or any portion of, or any interest in, the property, or any direct or indirect ownership interest in (or management of) the borrower.

j. The liens created or purported to be created by the loan documents become unenforceable or cease to be first priority liens.

k. Amendment, termination or default with respect to specified material agreements without the prior consent of lender.

Drafting Tip: Any cure rights negotiated by the borrower should be inserted only with respect to (and applicable to) a specified default, and should not be applicable to all defaults generally. Lenders are not generally willing to give the borrower a cure period if the default is not susceptible of being cured or if the circumstances giving rise to the default were knowingly caused by the borrower. The defined term "Event of Default" or "Default" in the loan agreement should refer only to the occurrence of a specified event, and only after the applicable notice and cure periods have run with respect to that event. By so defining an "Event of Default" or "Default", lender's counsel can clearly delineate the remedies, if any, available to the lender if the event occurs and before the applicable cure period has run, and those remedies which are available only after the cure period has run and the default remains uncured. For example, many lenders will not make loan advances or allow withdrawals from reserve or collateral accounts during a cure period.

8. **Rights and Remedies of Lender**. The loan agreement should generally describe the rights and remedies available to the lender under the loan documents, and may include the following:

a. Lender's right to take possession of the property.

b. Lender's right to make protective advances.

c. Lender's right to accelerate the loan. [The loan agreement should clearly state that upon the occurrence of an "Event of Default" or "Default", the lender may accelerate the loan. Some lenders also provide for an automatic acceleration if the borrower becomes the subject of a bankruptcy or insolvency proceeding.]

d. A provision clarifying that any funds advanced by the lender to cure any default or to exercise its remedies will (i) constitute a portion of the loan, (ii) bear interest from the date advanced at the default rate, (iii) be secured by all collateral and security for the loan, and (iv) be due and payable immediately upon demand.

e. Lender's right to terminate its commitment to make further advances of the loan.

f. Lender's rights with respect to reserve and other collateral accounts.

g. Lender's rights to control disbursements of project revenues, if applicable, including payments to insiders and affiliates of the borrower.

h. Confirmation of the right of offset.

i. Confirmation of other rights and remedies under the loan documents or which are otherwise available to lender at law or in equity.

9. **Application of Casualty and Condemnation Proceeds**. The loan agreement should clearly set forth the lender's right to negotiate casualty and condemnation settlements, the

borrower's obligation to pay such awards or cause such awards to be paid directly to the lender, and the lender's rights to apply such funds to the loan or allow the borrower to use such funds to repair or rebuild.

10. Co-Lender Provisions. If the loan is a syndicated loan, the loan agreement should appoint the agent for the bank group, set forth the obligations of each lender and the agent, provide for the appointment of successor agents, authorize the agent to act on behalf of the lenders with respect to the loan, and provide for intercreditor rights with respect to loan amendments, waivers, administration and enforcement. These provisions are generally not enforceable by the borrower, and are set forth solely for the benefit of the agent and the lenders.

11. Miscellaneous. This section may include the general/miscellaneous provisions found in other real estate documents, but generally include the following:

a. Notice provisions.

b. Limitation on amendments.

c. Third party beneficiaries.

d. Availability of records; confidentiality (if applicable).

e. Limitations on the lender's right to assign or grant participations with respect to all or any portion of the loan, and confirmation that the borrower may not assign the loan without the prior written consent of lender.

f. Time of the essence.

g. Governing law, choice of forum, consent to service of process and jurisdiction and (if appropriate given the choice of law determination) waiver of trial by jury.

h. Waivers generally.

i. Severability.

j. Multiple counterpart language.

k. Usury/spreading limitation.

l. Limitations on liability or exculpation. [The loan agreement should clearly set forth any limitations on the personal, partnership or corporate liability of the borrower or any direct or indirect general partner of the borrower or any other obligor, but should confirm that such limitation of liability shall not in any event impair lender's rights with respect to the project and other collateral. Reference can be made in each other loan document to the limitations on liability set forth in the loan agreement.]

m. Partial release provisions.

n. Controlling documents/entire agreement.

C. ***General Considerations Regarding Security Documents***. The most important issue in preparing the security documents is to confirm that the documents are sufficient to create and perfect a lien, security interest or assignment with respect to the applicable collateral. The following issues are also important when drafting security documents:

1. ***Definition of Secured Indebtedness***. The indebtedness secured by each security document should be precisely the same and should clearly cover the existing loan, as it may from time to time be renewed, amended, increased, restated or supplemented, all obligations of the borrower and third-party pledgors under the other loan documents, and any additional extensions of credit to the borrower (which may be limited to advances made in connection with the loan and collateral securing the loan). The following language may be used in each security document to describe the indebtedness intended to be secured thereby:

> "Secured Indebtedness" means: (a) all indebtedness, liabilities and obligations arising under that certain promissory note dated ________________, executed by borrower and payable to the order of lender, in the original principal amount of $___________, bearing interest as therein specified, and providing that the balance of such note shall be due and payable on ____________________, and all principal, interest, fees, expenses, obligations and liabilities of borrower to lender arising pursuant to or represented by such note, as it may, at any time and from time to time, be renewed, extended, modified and/or increased (collectively, the "Note"), or this [name security document]; (b) all loans and advances which lender may hereafter make to borrower [*in connection with the Loan or the Mortgaged Property*]; (c) all other and additional indebtedness, liabilities and obligations of every kind and character of borrower now or hereafter existing in favor of lender [*in connection with the Loan or the Mortgaged Property*], regardless of whether they are direct, indirect, primary, secondary, joint, several, joint and several, liquidated, unliquidated, fixed or contingent, and regardless of whether the same may, prior to their acquisition by lender, be or have been payable to some other person or entity, it being the intention and contemplation of borrower and lender that future advances may be made to borrower for a variety of purposes, that borrower may guarantee (or otherwise become directly or contingently obligated with respect to), the obligations of others to lender [*in connection with the Loan or the Mortgaged Property*], and that lender may, from time to time, acquire from others obligations of borrower to such others, or that borrower may otherwise hereafter be, or become further indebted to lender, and that payment and repayment of all of the foregoing are intended to and shall be part of the Secured Indebtedness secured hereby; (d) the payment and performance by borrower of all of its obligations under (i) any loan agreement now or hereafter executed by and between borrower and lender [*in connection with the Loan or the Mortgaged Property*], together with all amendments, modifications, renewals, restatements, rearrangements, or extensions thereof, (ii) [*describe any net profits or equity sharing agreement*], and (iii) any and all other security agreements, mortgages, deeds of trust, collateral pledge agreements, assignments or contracts of any kind now or hereafter existing as evidence of, security for, or otherwise executed in connection with any indebtedness, obligation or liability of borrower to lender [*in connection with the Loan or the Mortgaged Property*]; and (e) any and all renewals, increases, extensions, modifications, rearrangements, or restatements of, and supplements to, all or any part of the loans, advances, indebtednesses, liabilities and obligations described or referred to in

subparagraphs (a) through (d), above, together with all costs, expenses and attorneys' fees incurred in connection with the enforcement, administration or collection thereof."

2. ***Description of Mortgaged Property for the Deed of Trust***. Care should be taken to include in the description of mortgaged property the land, any appurtenances thereto, all improvements, fixtures and tangible personal property now or hereafter located thereon, and all applicable contractual arrangements, deposits, accounts and intangibles arising under or in connection with the property. Sample language may include the following:

"Mortgaged Property" means the Real Estate and the Collateral, collectively.

"Real Estate" means the Land, the Improvements, the Personal Property, the Leases, the Rental, and all other estates, easements, licenses, interests, rights, titles, powers and privileges of every kind and character which Grantor now has or at any time hereafter acquires, in and to the Land, the Improvements, the Personal Property, and all property which is used or useful in connection with the Land, the Improvements, and the Personal Property, and the proceeds of any and all insurance covering the Land, the Improvements, the Leases, the Rental and the Personal Property. [Note: some attorneys do not include Rental in the definition of "Mortgaged Property", and choose instead to depend upon the absolute assignment of Rental]

"Land" means all of that certain tract of real property located in ____County, Texas, more particularly described upon Exhibit A attached hereto, together with all strips or gores appurtenant to such property, underlying roadways or public rights-of-way or otherwise, in which Grantor now or hereafter possesses an interest.

"Improvements" means all buildings and improvements now or hereafter situated upon the Land.

"Personal Property" means all fixtures, building materials, machinery, equipment, furniture, furnishings, and personal property in which Grantor now has, or at any time hereafter acquires, an interest, and which now, or at any time hereafter, are situated in, on or about the Land.

"Lease" means any ground lease, space lease, sublease or other agreement (oral or written) under the terms of which any person other than Grantor has or acquires any right to occupy, use, or manage the Mortgaged Property, or any part thereof, or interest therein.

"Rental" means rents, issues, profits, royalties, bonuses, revenue, income and other benefits derived from the Mortgaged Property or arising from the use or enjoyment of any portion thereof or from any Lease and liquidated damages following defaults under any Lease, and all proceeds payable under any policy of insurance covering loss of rents, together with any and all rights which Grantor may have against any tenant under any Lease.

"Collateral" means all of Grantor's right, title, and interest, now owned or hereafter acquired, in and to the following described properties and interests and all replacements or substitutes therefor and all products and proceeds thereof, and accessions thereto:

(1) All portions of the Personal Property which are either fixtures or personal property, tangible or intangible; and

(2) All building materials and equipment, machinery and other items of personal property of any kind or character now or hereafter related to, situated upon or used, or acquired for use, upon or in connection with any part of the Real Estate; and

(3) All accounts, inventory, instruments, chattel paper, documents, consumer goods, insurance proceeds, leases, contract rights, and general intangibles now, or hereafter related to, any of the Real Estate, including, without limitation, the following:

(A) All contracts now or hereafter entered into by and between Grantor, as owner, and any contract or subcontract for the construction (original, restorative or otherwise) of any of the Improvements, and of any other buildings, structures or improvements to, or on, the Real Estate (or any part thereof), or the furnishing of any materials, supplies, equipment, or labor in connection with any such construction;

(B) All of the plans, specifications, and drawings (including, without limitation, plot plans, foundation plans, utility facilities plans, floor plans, elevations plans, framing plans, cross-sections of walls plans, mechanical plans, electrical plans, architectural and engineering plans and specifications, and architectural and engineering studies and analyses) heretofore or hereafter prepared by any architect or engineer with respect to any of the Real Estate;

(C) All agreements now or hereafter entered into with any party with respect to architectural, engineering, management, licensing, brokerage, operation, promotion, marketing, or consulting services rendered or to be rendered, with respect to the construction, development, management, marketing, promotion, leasing, operation, or sale of any of the Real Estate;

(D) All commitments (and the proceeds therefrom) issued by any lenders or investors to finance or invest in any of the Mortgaged Property, or in Grantor;

(E) Any completion bonds, performance bonds, labor and material payment bonds, and any other bonds (and the proceeds therefrom) relating to any of the Real Estate or to any contract providing for construction of any of the Improvements or any other buildings, structures, or improvements to, or on, any of the Real Estate;

(F) All rights or awards due to Grantor arising out of any eminent domain proceedings for the taking or for loss of value of any of the Real Estate;

(G) All rents, issues, profits, and deposits due to Grantor, as lessor, under any lease covering any of the Real Estate;

(H) All trademarks, trade names, or symbols under which any of the Real Estate is operated or the business of Grantor at the Real Estate is conducted;

(I) All accounts receivable arising out of the leasing and operation of, or the business conducted at or in relation to, any of the Real Estate;

(J) All monetary deposits which Grantor has been, or may be, required to give to any public or private utility with respect to utility services furnished, or to be furnished, to the Real Estate;

(K) All contracts of sale and options relating to the disposition of any of the Real Estate;

(L) All products and proceeds arising by virtue of any transaction related to the disposition of any of the Mortgaged Property;

(M) All deposits of cash, securities, or other property which may be held at any time, and from time to time, by Grantor to secure the performance by each Lessee of such Lessee's covenants, agreements, and obligations under any Lease;

(N) All permits, licenses, franchises, certificates, and other rights and privileges obtained by Grantor in connection with the Mortgaged Property;

(O) The balance of every deposit account (now or hereafter existing) of Grantor with Beneficiary (or any agent, affiliate, or subsidiary of Beneficiary) and any other claim of Grantor against Beneficiary (now or hereafter existing) and all money, instruments, securities, documents, chattel paper, credits, demands, and any other property, rights, or interests of Grantor which at any time shall come into the possession, custody, or control of Beneficiary (or any agent, affiliate, or subsidiary of Beneficiary);

(P) All proceeds payable or to be payable under each policy of insurance relating to the Real Estate and/or the Personal Property; and

(Q) All books, records and computer software concerning the Real Estate, the Personal Property, and the property described in clauses (A) through (P) above.

3. **Granting Language**. The granting language in the deed of trust should include all rights, hereditaments and appurtenances appertaining or belonging to the Mortgaged Property, and should clarify that (a) with respect to personal property, the deed of trust constitutes a

security agreement in favor of lender, and (b) with respect to non-UCC personal property, the deed of trust constitutes a common law assignment of the non-UCC personal property collateral.

4. <u>**Security Agreement**</u>. The deed of trust should be drafted to include a deed of trust, mortgage, assignment of leases and rents, financing statement and security agreement. A separate, additional security agreement is generally used only if the collateral includes substantial equipment, inventory, receivables or other intangibles.

D. <u>***Third Party Consents and Acknowledgments***</u>. To the extent the loan documents assign or purport to assign to the lender any rights or benefits of the borrower under third party agreements (such as the management contract, franchise/license agreements, equipment leases, etc.), the lender should obtain the written consent and acknowledgment of the third party to the assignment to lender. The third party consent may also confirm the existence of the third party agreement, confirm lender's right to assume or reject the third party agreement upon foreclosure and, following foreclosure and assumption, provide that lender has no liability for pre-existing defaults or liability other than lender's interest in the property. If these third party agreements are material to the operation of the project and its value, lender may also want each third party to consent to the assignment of the third party agreement to any purchaser at foreclosure or its assignee.

E. <u>***Limitation of Liability/Non-recourse Provisions***</u>. Many lenders agree to limit the liability of the borrower and/or the guarantors, except that (a) if certain events occur, the limitation of liability will be rescinded and the borrower and/or guarantors will have unlimited joint and several liability for the loan, and (b) the borrower and/or guarantors will in any event be liable for certain amounts, separate and apart from any other limitation of liability in the loan documents. Most lenders provide that notwithstanding any limitation of liability or nonrecourse language in the loan documents, the borrower and each guarantor will at all times be jointly and severally liable for the following:

a. Fraud, waste and any criminal act;

b. Breaches of representations and warranties (sometimes limited to knowing, material breaches);

c. Environmental and ADA indemnities and compliance with other laws;

d. Ad valorem and personal property taxes and insurance premiums and deductibles;

e. Misapplication of project revenues (sometimes limited to misapplication after default), casualty or condemnation proceeds, loan proceeds, or escrow or reserve accounts;

f. Violations of prohibitions on distributions, dividends, payments on insider debts and payment to affiliates; and

g. Collection costs.

In addition, the loan documents frequently provide that the limitation of liability or nonrecourse provisions are contingent upon the non-occurrence of certain events, such as the following:

a. Any conveyance or encumbrance of the property or any direct or indirect ownership interest in the borrower in violation of the loan documents;

b. Any violation of bankruptcy remote entity/ special purpose entity requirements;

c. A bankruptcy of the borrower (or other property owner); and

d. Any failure to cooperate with, obstruct, challenge or assert a defense to any of lender's rights or remedies under the loan documents.

In any event, lender's counsel should draft the limitation of liability/non-recourse provisions very carefully to confirm that such provisions will not in any event affect or impair lender's rights and remedies with respect to the collateral.

Due Diligence Checklist

L = Lender
LA = Lender's Attorney
B = Borrower

BA = Borrower's Attorney
TC = Title Company
Principals = Each direct and indirect signatory for borrowerand each guarantor [and any affiliated manager]

	Document Title	Responsibility	Received /Prepared	Approved	Executed
1.	Organizational Documents for Corporate Principals				
	a. Certificate of Incorporation - State of Incorporation	BA			
	b. Certificate of Good Standing - State of Incorporation	BA			
	c. Certificate of Qualification to Conduct Business - Texas	BA			
	d. Articles of Incorporation, certified by the State of Incorporation	BA			
	e. Bylaws	BA			
	f. Corporate Resolutions	BA			
	g. Certificate of Incumbency	BA			
2.	Organizational Documents for Limited Partnership Principals				
	a. Limited Partnership Agreement and all amendments	BA			
	b. Certificate of Limited Partnership and all amendments, certified by the State of Registration	BA			
	c. Certificate of Existence - State of Registration	BA			
	d. Certificate of Good Standing - State of Registration	BA			
	e. Certificate of Qualification to Conduct Business - Texas	BA			

	Document Title	Responsibility	Received /Prepared	Approved	Executed
	f. Partnership Authorization and Consent signed by all [general] partners	BA			
3.	Organizational Documents for General Partnership Principals				
	a. Partnership Agreement and all amendments	BA			
	b. Partnership Authorization and Consent signed by all partners	BA			
4.	Organizational Documents for Limited Liability Company Principals				
	a. Articles of Organization, certified by State of Registration	BA			
	b. Certificate of Existence - State of Registration	BA			
	c. Certificate of Good Standing - State of Registration	BA			
	d. Certificate of Qualification to Conduct Business - Texas	BA			
	e. Resolutions of the [managing] members	BA			
5.	Organizational Documents for Trust Principals				
	a. Trust Agreement	BA			
	b. Authorization and Consent signed by beneficiaries	BA			
	c. Certification of the trustee	BA			
6.	Title Information				
	a. Title Commitment	BA/TC			
	b. Two legible copies of each exception to title shown in Title Commitment	BA/TC			
	c. UCC Searches - Borrower				
	(i) local (county) filing	BA			
	(ii) central filing	BA			
	(iii) other??	BA			
	d. UCC Searches - Prior Owners (5 years)				

	Document Title	Responsibility	Received /Prepared	Approved	Executed
	(i)	BA			
	(ii)	BA			
	(iii)	BA			
7.	Survey				
	a. Form of certification	LA			
	b. Survey	BA			
8.	Flood Certification	BA			
9.	Tax Information	BA/TC			
10.	Permits and Licenses				
	a. Underground Storage Tank	BA			
	b. Building Permit (construction loan)	BA			
	c. Final Certificate(s) of Occupancy	BA			
	d. Elevator Permits	BA			
	e. Liquor License	BA			
	f. State ADA Certification	BA			
	g. Other?	BA			
11.	Evidence of Availability of Utilities				
	a. Electricity	B/BA			
	b. Gas	B/BA			
	c. Sewer	B/BA			
	d. Water	B/BA			
	e. Telephone	B/BA			
	f. Other?	B/BA			
12.	Zoning				
	a. Zoning Designation Letter (City)	BA			
	b. Zoning Compliance Letter [City/Architect/Engineer/Attorney]	BA			
	c. Copy of applicable zoning ordinances	BA			

	Document Title	Responsibility	Received /Prepared	Approved	Executed
13.	Architect/Engineer's Letter Regarding Compliance With Laws (including ADA)	BA			
14.	Plans and Specifications	B			
15.	Agreement Between Owner and Architect	BA			
16.	Agreement Between Owner and Engineer	BA			
17.	Agreement Between Owner and General Contractor	BA			
18.	Major Subcontracts				
	a.	BA			
	b.	BA			
	c.	BA			
19.	Architectural approval/subdivision restriction compliance confirmation	BA			
20.	Waiver of Repurchase Rights, if applicable	BA			
21.	Waiver of Right of First Refusal, if applicable	BA			
22.	Appraisal	L			
23.	Insurance				
	a. Digest Summaries/Policies	BA			
	b. Evidence/Certificates of Insurance	BA			
24.	Insurance Audit	L			
25.	Environmental Assessment	L			
26.	Architect/Engineer's Audit	L			
27.	Ground Lease				
	a. Ground Lease and all amendments	BA			
	b. All recorded memoranda, amendments, assignments, etc.	BA			
	c. Prior Estoppels and Agreements signed by the lessor	BA			
28.	Space Leases (and all amendments)				
	a. Summary	BA/B			

	Document Title	Responsibility	Received /Prepared	Approved	Executed
	b. [Tenant Name]	BA			
	c. [Tenant Name]	BA			
	d. [Tenant Name]	BA			
29.	Equipment Leases and Conditional Sales Agreements				
	a. Summary	BA/B			
	b.	BA			
	c.	BA			
	d.	BA			
	e.	BA			
30.	Operating/Service Agreements				
	a. Summary	BA/B			
	b.	BA			
	c.	BA			
	d.	BA			
31.	Management/Leasing Agreements	BA			
32.	Franchise or License Agreement	BA			
33.	Purchase and Sale Agreement				
	a. Purchase and Sale Agreement and all amendments and assignments	BA			
	b.Escrow Agreements, if any	BA			
34.	Existing loan documents (only if they will be assigned to Lender)	BA			
35.	Mezzanine/subordinate loan documents with third party lender	BA			
36.	First/superior lien loan documents with third party lender	BA			
37.	Documents evidencing existing insider debt	BA			
38.	Takeout Loan Commitment	BA			
39.	Budget				

	Document Title	Responsibility	Received /Prepared	Approved	Executed
	a. Construction	B			
	b. Operating	B			
40.	Project Information				
	a. Rent Roll	B			
	b. Marketing Proposals and Reports	B			
41.	Financial Information				
	a. Project Financial Statements				
	(i)________________ - audited	B			
	(ii)________________ - audited	B			
	(iii)________________ - unaudited	B			
	b. Borrower Financial Information				
	(i)________________ - audited	B			
	(ii)________________ - audited	B			
	(iii)________________ - unaudited	B			
	c. Guarantor Financial Information				
	(i)________________ - audited	B			
	(ii)________________ - audited	B			
	(iii)________________ - audited	B			
42.	Partnership Interest/Stock Pledge Information				
	a. Copies of all Partnership Agreements and all Amendments	BA			
	b. Copies of all Stock Certificates to be Pledged	BA			
	c. Copies of all applicable Shareholders Agreements	BA			
	d. Analysis of Securities Law Issues for Restricted Stock	BA/LA			

Loan Document Checklist

L = Lender
LA = Lender's Attorney

B = Borrower's Attorney
BA = Borrower's Attorney
TC = Title Company

	Document Title	Responsibility	Received/ Prepared	Approved	Executed
1.	Loan Agreement	LA			
2.	Note	LA			
3.	Deed of Trust, Security Agreement, Financing Statement and Assignment of Rents	LA			
4.	Assignment of Leases and Rents	LA			
5.	Security Agreement (and Assignment of Rights)	LA			
6.	Environmental Indemnity Agreement	LA			
7.	ADA Indemnity	LA			
8.	Guaranty	LA			
9.	Statutory Notice of Final Agreement (Texas only)	LA			
10.	Flood Hazard Determination (if required for the applicable lender)				
11.	Assignment/Pledge of Stock/Partnership Interests and Consents	LA			
12.	Delivery of Original Stock Certificates	BA			
13.	Blank Stock Power				
14.	Assignment of Purchase Agreement Escrow and Consent	LA			
15.	Assignment of Management Agreement and Consent	LA			
16.	Manager's Estoppel Letter and Agreement	LA			
17.	Assignment of Franchise/License Agreement and Consent	LA			
18.	Franchisor/Licensor Estoppel Letter and Agreement	LA			
19.	Financing Statements				

	Document Title	Responsibility	Received/ Prepared	Approved	Executed
	a. Project				
	(i) Texas - central	LA			
	(ii) Texas - local	LA			
	(iii) Other?	LA			
	b. Other Collateral?				
	(i)	LA			
	(ii)	LA			
	(iii)	LA			
20.	Subordination Agreement (with respect to insider debt)	LA			
21.	Tri-Party Agreement (with takeout lender/purchaser)	LA			
22.	Intercreditor/Subordination Agreement (with subordinate/prior lienholder)	LA			
23.	Prior/Subordinate Lien Documents executed contemporaneously	BA			
24.	Interest Rate Protection Agreement(s)	B			
25.	Assignment of Interest Rate Protection Agreement(s)	LA			
26.	Consent to Assignment of Interest Rate Protection Agreements	LA			
27.	Letter(s) of Credit	BA			
28.	Confirmation(s) of Letter(s) of Credit	BA			
29.	Tax Abatement Agreement - City	B			
30.	Tax Abatement Agreement - County	B			
31.	Tax Abatement Agreement - Other	B			
32.	Assignment of Tax Abatements and Consents, if applicable	LA			
33.	Assignment of Reserve Accounts and Consents	LA			
34.	Reserve Account Signature Cards	L			

	Document Title	Responsibility	Received/ Prepared	Approved	Executed
35.	Assignment of Escrow Accounts and Consents	LA			
36.	Escrow Account Signature Cards	L			
37.	Architect’s Affidavit, Consent and Subordination	LA			
38.	Engineer’s Affidavit, Consent and Subordination	LA			
39.	Contractor’s Affidavit, Consent and Subordination	LA			
40.	Subcontractors’ Affidavit, Consent and Subordination	LA			
41.	Ground Lease and all amendments and assignments	BA			
42.	Ground Lessor Estoppel and Agreement	LA			
43.	Subordination, Non-Disturbance and Attornment Agreements				
	a. Form	LA			
	b. [Name of Tenant]	BA/B			
	c. [Name of Tenant]	BA/B			
	d. [Name of Tenant]	BA/B			
44.	Tenant Estoppel Letters				
	a. Form	LA			
	b. [Name of Tenant]	BA/B			
	c. [Name of Tenant]	BA/B			
	d. [Name of Tenant]	BA/B			
45.	Estoppel Agreements - equipment leases and conditional sales agreements [**??**]				
	a. Form	LA			
	b. [lessor/seller]	BA			
	c. [lessor/seller]	BA			
	d. [lessor/seller]	BA			

	Document Title	Responsibility	Received/ Prepared	Approved	Executed
46.	Estoppel Agreements - operating/service agreements [**??**]				
	a. Form	LA			
	b. [vendor]	BA			
	c. [vendor]	BA			
	d. [vendor]	BA			
47.	Assignment of Existing Loan, if applicable	LA			
48.	Delivery of existing loan documents to Lender, if assigned	Assignor			
49.	Legal Opinions				
	a. Form(s)	LA			
	b. Texas	BA			
	c. State of Incorporation/Registration (if applicable)	BA			
	d. Other applicable law?	BA			
50.	Commitment Letter	L/LA			
51.	Agent Fee Letter	L/LA			
52.	Bank Group Fee Letter	L/LA			
53.	Closing Statement	BA/TC			
54.	Closing Instruction Letter/Marked up Title Commitment	LA/TC			
55.	Insured Closing Letter	TC			
56.	Reinsurance/Coinsurance Agreements	TC			
57.	Lien and UCC Releases for Existing Debt				
	a.	BA/TC			
	b.	BA/TC			
	c.	BA/TC			