THE MORTGAGE OBSERVER

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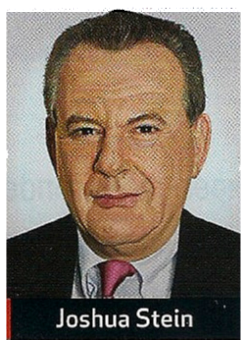
Stein's Law

Quicker And Cheaper Loan Closings?

Why does it cost so much in legal fees to close a commercial real estate loan? How can a borrower control legal fees for one of these transactions? What's the magic answer?

Any set of loan documents typically goes into tremendous detail on a tremendous range of issues. A complete and perfect negotiation of the documents may require full exploration of all those issues, which can take a lot of time and cost a lot of money. But every one of those issues could, in some circumstance, make a difference. As the starting point for discussion, then, borrowers and their counsel should at least consider working their way through and negotiating everything.



Joshua Stein

A borrower may want to direct counsel to take a different approach, by telling them to focus on only three things in reviewing and negotiating the documents.

First, make sure the loan documents get the deal right—the dumb stuff staring everyone in the face—such as the maturity date, the interest rate, who will sign which guaranties and anything that relates directly to how much the borrower will pay for the lender's money. Given the complexity of modern legal documents, the fundamentals of a deal often can become overwhelmed by details, alternatives, hypotheticals and side issues.

For example, have you ever tried to figure out the loan amount, interest rate and maturity date just by reading a syndicated loan agreement? You can do it, of course, but it's typically an ordeal that can involve dozens of interacting defined terms. Important points can slip between the cracks in all that complexity. Borrower's counsel must make sure that doesn't happen.

Second, try to trim back the verbiage of the loan documents at least enough so the borrower isn't automatically in default at the moment of closing or when proceeding with his or her basic business plan for the property. Don't worry so much about hypothetical eventualities, provisions unlikely to become relevant in the ordinary course of events. Focus on the parts of the documents that relate to the borrower's real daily life in operating (and, where relevant, developing or improving) the property. And make sure the financial reporting and insurance requirements match what the borrower really expects to do.

Third, and most important, focus on the

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guaranties. If someone agreed to guaranty something in connection with the loan, confirm that the guaranties cover only what they should cover and nothing more. No one should face personal liability as a guarantor for anything more than the business deal contemplated. Understand all possible circumstances that could trigger the guaranty. Recent litigation has shown that surprises lurk in "standard" carveout guaranties, including in the "boilerplate." Counsel should identify and prevent those surprises.

If a borrower tells counsel to focus on the three areas just described—and it is the borrower's decision, not the lawyer's—this means some verbiage in the loan documents will escape close legal attention. Arcane requirements for lender approval to various unlikely matters may just survive, and the lender won't have to be "reasonable." Ordinary obligations to preserve the property may not have the benefit of complicated exceptions and limitations that lawyers could have created. If the borrower goes into default, the documents will give the lender the ability to take various unpleasant actions, which would have, for the most part, also been true even if the borrower had tried to negotiate those unpleasant actions.

In short, the loan documents won't be as "good" as they could have been if the lawyers had worked harder. But, for three reasons, the borrower might conclude they will be "good" enough.

First, if the borrower makes the required loan payments when due, the lender probably will give the borrower a wide berth and mostly leave him or her alone. And if the borrower doesn't pay the loan, everything will change.

Second, if the borrower takes care to build and maintain a good relationship with the lender, the lender will probably work cooperatively with the borrower as possible issues arise.

Third, lenders usually don't want to have a loan in default, and they don't want the collateral. Once the borrower has the lender's money and the lender just has the loan documents, much of the practical leverage switches to the borrower.

Of course, much will depend on the type of lender involved. Today's "nice" lender may sell the loan to tomorrow's "mean" lender.

It ultimately amounts to a business decision and a judgment call. A borrower may decide it makes sense to save money and time today in exchange for the possible risk of less-favorable loan documents later, particularly if the borrower has some comfort that any problems will probably arise only in secondary or tertiary areas of the loan documents.

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