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Due Diligence When Buying and Selling New York Real Estate

1 credit hour

Offered by: RE CREDITS, LLC

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DUE DILIGENCE WHEN BUYING & SELLING NEW YORK REAL ESTATE
1 CREDIT HOUR

I. Coop Due Diligence (15 MINUTES)

- Financial Statements
 - Attorney must conduct due diligence on the financial condition of the Coop or Condo
 - Attorney's Opinion Letter
 - "We conducted our audit in accordance with auditing standards generally accepted in the United States."
 - "In our opinion, the financial statements present fairly, in all material respects, the assets and members' equity and its revenues, expenses and retained earnings."
 - Audited vs. Unaudited Financial Statements
 - Many smaller buildings do not have audited financials, however, loans are still available
 - Ask the lender or mortgage broker if their institution grants loans to buildings with unaudited financials
 - Watch out for:
 - Shares are not publicly traded
 - Building income before depreciation and amortization
 - The goal is not to maximize profit but to meet operating expense (Building can run at a loss)
 - Identify Amount of Reserve Fund
 - Compare latest accounting period with period immediately prior (three years)
 - Comparison of one year to the next will reflect noteworthy variations
 - The variations tell a story
 - Substantial maintenance arrears or substantial accounts payable increases
 - When Representing a Coop Buyer, the attorney and client must be satisfied that the building is easily handling its obligations to pay the underlying mortgage and real estate taxes
 - The smaller these obligations are as percentage of maintenance income, the more likely it is that the building will not have difficulty in refinancing
 - Encourage clients to seek a second opinion on the financials
- Board Minutes
 - It is critical that minutes are reviewed for both Coop and Condo purchases
 - Minutes may reflect:
 - Financial concerns
 - Building maintenance issues
 - Various problems (other unit owners)
 - Changes in building policy
 - Not all buildings permit inspection of minutes
- Coop Offering Plan
 - Review of the Offering Plan is especially important if there are still unsold shares
 - Provided sponsor complies with Article 23-A of the General Business Law, the Offering Plan will include up to date financial disclosures by the holder of unsold shares, including how many

- If disclosures are not current or show financial weakness, purchase may be more speculative than the usual home purchase, and purchaser should be advised
- The number of sponsor-owned unsold shares allocated to apartments as a percentage of the building should be determined and a judgment made as to whether or not the purchaser is actually buying into a cooperative
- If a large percentage of units are held by the sponsor as rentals, it may be hard to run the building in the best interest of the owner occupants or for potential purchasers to obtain financing.
- A large number of sublets can suggest an inability to resell at an acceptable price, which discourages share lenders and potential underlying mortgagees
- Coop Proprietary Lease
 - Lease term must exceed the term of the proposed financing, or the purchaser will have difficulty obtaining the financing.
 - Risk of unsold shares - Will lease be renewed?
 - Unusual conditions with respect to assignment or sublease?
 - Consent required for transfers
 - Flip tax/fees on assignment and sublet
- Coop House Rules
 - Classification of directors (is current management entrenched through term system)
 - Unusual provisions and fees associated with respect to assignment and sublet
- Coop Underlying Building Mortgage
 - What is the due date of any balloon payment?
 - What are the terms of the building financing?
 - Were terms competitive when taken?
 - Are terms very uncompetitive today?
- Coop Tax Abatements
 - When do they expire?
 - How are they credited to unit owners?
 - Portion of deductible maintenance
 - History of maintenance increases or assessments
 - Anticipated increases in maintenance or assessments
 - Limitations of financing
- Miscellaneous Coop Issues
 - Subletting policies
 - Number of Shares allocated to the unit
 - Number of units in the building and the building-wide mortgage amount
 - Pet policy
 - Guest policy
 - Are utilities paid by shareholder or building
- Special Issues
 - Roof rights
 - Proposed alterations
 - Home business
 - Combining apartments (certificate of occupancy issues, generally results in disproportionately high maintenance).
- Physical Inspection
 - Not usually obtained for an apartment in a multiple dwelling, but may be advisable if:

- small building
- ground floor unit (vermin and water damage)
- top floor unit (water damage)
- Confirm contract terms (seller is owner of record, # of shares, % common elements, monthly charges, social security # of clients)

II. Condominium Due Diligence (10 MINUTES)

- Declaration & By-Laws
 - Verify current dates of declaration, by-laws rules and regulations, and amendments thereto.
 - Review declaration, bylaws and rules and regulations for unusual provisions and procedures governing sales of unit.
- Budgets
 - Determine if budget includes all proposed renovations and changes in services
 - Aging building – determine how or proposed alterations will be financed.
 - Many condominiums cannot borrow money for repairs; some may follow RPL §339-jj, which permits borrowing under certain circumstances; 5 years of operation, for repairs or replacement, approval of majority in common interest of association.
- Miscellaneous
 - Obtain a copy of power of attorney form used by the condominium and explain to client along with right of first refusal.
 - Check contract description against seller's title report.
 - Special issues
 - Roof rights
 - Proposed alterations
- Information to Confirm:
 - Common area charges
 - No claims or litigation pending
 - Payment of utilities
 - Special assessments (current, past, contemplated and pending)
 - Unit's common interest

III. Contract of Sale (35 MINUTES)

- NYSBA Real Estate Forms
- Variations Clearly Identified
- A Rider Amends the Form Contract to Address Unique Issues & Protections
- Form Contract and Seller's Rider Drafted By Seller Counsel
- Purchaser Should Submit Purchaser's Rider
- Delivery Date
 - The date when fully executed contract has been delivered.
 - The date contract is in full force and is the date from when time periods are measured.
 - Upon the delivery date:
 - Seller's counsel should seek payoff existing mortgage or share loan.
 - Purchaser's counsel should confirm timely loan application with client and order title/lien search.
- Mortgage Contingency

- Allows for the return of purchaser's contract deposit (typically 10% of sales price) if the purchaser is unable to obtain financing.
- Net effect of the escrow provision is to tie up the down payment and require agreement of the parties or a judgment before the funds are released.
- Most litigation between buyers and sellers of real estate arises out of buyer's attempts to obtain financing
 - Two to One Courts Favor Buyers
- Clause is conditioned upon the issuance of a commitment not upon closing of the loan.
- Seller and Purchaser have right to cancel if loan commitment not obtained by specified date.
- Loss of the commitment is on the purchaser – but courts have failed to act accordingly by allowing a purchaser to rescind where mortgage commitment has been cancelled after issuance (and expiration of the contract condition) due to loss of the purchaser's employment.
- Purchaser should be wary of making representations about ability to obtain loan unless she has fully completed a pre-qualification process with the lender.
- Two elements to issuance of a loan:
 - Does borrower have sufficient income and assets to repay loan?
 - Is the value of the property is sufficient to adequately secure repayment?
- Purchaser's attorney may want to ask for the addition of the loan closing condition.
- Seller's attorney should add "unless failure to close the loan is due to the fault of the purchaser does not protect seller from a failure to close that is not due to the fault of the purchaser."
- Seller's attorney should add a representation by purchaser that the purchaser has sufficient income and assets to qualify for the loan and does not know of any judgments, claims or other matters that would impair his ability to obtain the loan.
- Seller's attorney should add a representation by purchaser that contract is not contingent on sale of property, rental income or refinancing of property.
 - Friend v. McGarry, Purchaser allowed to cancel pursuant to mortgage contingency, when lender conditioned loan on sale of property and purchaser was unable to sell
- Seller's attorney should add a representation by purchaser that purchaser has not, within the past two years, been denied consent by an apartment corporation or condominium association with respect to any proposed purchase by Purchaser of any other cooperative apartment or condominium unit. In addition, Purchaser has not been rejected in an application for a loan within the past five (5) years.
- Four Contracts of Sale
 - Condo – 1998 & 2000
 - Co-op – 1989 & 2001
- Institutional Lender & Mortgage Broker
- Earlier contracts – required application to institutional lenders
- Requirement satisfied if mortgage broker submits to an institutional lender
- Purchaser's and Seller's Riders
 - Purchaser's Rider: Caveat Emptor
- Specific Performance: Purchaser's Default and Seller's Remedy
 - Absent a clause specifying or limiting the seller's remedy in the event the purchaser wrongfully refuses to take title, or otherwise defaults, the seller may always retain the purchaser's down payment as liquidated damages.

- Purchaser is not entitled to a return of the down payment even if the seller resells the property to a third party for an amount equal to or in excess of the original contract price.
- Deposits and Default
 - Misrepresentation as to occupants exposed at board interview causing the Coop Board to reject a purchaser is material breach.
 - Glanzer v. Altman, Purchaser's failure to submit application within 10 days per contract was breach entitling seller to liquidated damages; purchaser's misrepresentation of bankruptcy status was material breach.
 - Rosenbloom v. Estate of Zuckerman, Purchaser who stated in contract that the amount to be financed was "none" could not cancel when co-op approved application as all-cash purchase.
- Risk of Loss
- Closing Adjournments and Time of the Essence
 - New York form contracts do not make time of the essence
 - If the contract does not explicitly state that time is of the essence, it is not, and either party will be allowed a reasonable adjournment
 - If either party refuses without good reason to cooperate in scheduling the closing, the other party may make time of the essence after the contract is signed demanding performance by the other within a reasonable time by giving clear, distinct, and unequivocal notice of the demand
- NY law requires Seller's to disclose whether the property sits in a flood hazard area and if any flood insurance claims have been filed.