

Debt Transfer

Loan assumptions provide a funding source during challenging economic times.

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While new money is difficult to find in the current economic climate, loan assumptions may provide the prospective debt commercial real estate buyers need to close deals. A loan assumption is exactly that: A property buyer assumes a mortgage loan by stepping into the shoes of the seller/borrower and assuming its loan obligations. Although many types of loans contain assumption provisions, they are most common in securitized loans, which typically range between \$9 million and \$75 million or more.

Understanding Loan Assumption

Pools of securitized loans are serviced pursuant to pooling and servicing agreements, with day-to-day loan issues managed by one or more servicers. The common division of loan servicing responsibilities is often between a master servicer and a special servicer. Master servicers generally service loans that are not in default, while special servicers handle loans in default.

In transactions that involve loan assumptions, buyers should request copies of all property-related loan documents from the seller immediately after signing a purchase agreement. Buyers should carefully review the terms and conditions, particularly the requirements for the loan assumption, before contacting

the master servicer. After the buyer makes contact, the master servicer will send an information request package that typically includes a timeline for the assumption process and a list of requisite deliverables and fees.

After the master servicer receives the completed application package, the assumption process generally takes about eight to 10 weeks, presuming the package is complete and there are no unusual or undisclosed issues. It is especially important for buyers to plan ahead if there are specific time constraints, such as a 1031 exchange deadline.

The assumption application requires the buyer to make deposits and also may contain indemnities in favor of the servicer in order to proceed. The buyer may be asked to identify its authorized representatives and to indicate whether the assumption involves a 1031 exchange or other time-sensitive aspects. The servicer also requires a number of other documents, including formation documents, biographical information on principals and guarantors, the purchase agreement, tax returns, financial statements, and comparable sales, among others. The master servicer completes due diligence to ensure the buyer is financially sound and has the requisite real estate experience.

Typically, the master servicer must obtain the special servicer's consent before authorizing an

assumption. After the special servicer approves the deal, the master servicer issues an approval letter to the seller and buyer setting forth closing conditions.

From the lender's and servicers' perspectives, the original loan terms must remain final in every respect. However, there are two areas where servicers are willing to consider modifications. First, modifications may be allowed when loan documents contain obvious errors or require conforming to new ownership, such as the name of a new property manager. The buyer and its counsel should highlight any errors or conforming changes for the master servicer. Second, master servicers may consider modifications to equity transfer provisions. If transfer restrictions exist that will not work with the buyer's structure or business model, the buyer should notify the master servicer early and be specific about the necessary modifications.

Organizational Documents

The single-purpose entity is a hallmark of securitized lending, and conduit loan documents usually contain detailed requirements for the borrower's structure. These provisions specify which entity or entities must be SPEs and what provisions must be contained in their organizational documents. Before the buyer contacts the master servicer, it should carefully review the SPE provisions in the loan documents.

The buyer typically cannot use an existing entity as the new borrower. Accordingly, if the loan documents require an SPE, that entity must be newly formed. While the buyer or its counsel may prefer different SPE provisions than those in the loan documents, the lender's strong preference — if not requirement — is that the provisions match the loan documents verbatim.

The buyer also may want to use an existing entity to take advantage of a 1031 exchange because the Internal

