

Fast-Moving Deals

Competition speeds up transactions' due diligence process.

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Traditionally, commercial property buyers have had 30 to 60 days to perform due diligence on potential property purchases before putting down sizeable deposits. But in today's competitive climate, diligence periods are shrinking to as few as five to 15 days. To avoid being caught off guard when bidding for properties, commercial real estate professionals and their clients should understand the motives behind the movement to shorter periods of investigation.

Increasing Competition

In the past few years institutional investors with significant sources of discretionary funds have competed to acquire investment properties at a record-setting pace, especially in office and retail markets. The rising number of aggressive buyers has caused many sellers to offer properties on a competitive-bid basis. This process not only requires buyers to submit the prices they are willing to pay for properties, but also their definitive comments to sellers' purchase and sale agreements. In addition, when a buyer is selected, it must be willing to execute the deal as revised.

To win bids, buyers must offer increasingly higher purchase prices and make the purchase and sale agreements favorable to sellers. To make their agreements as attractive as possible, buyers often significantly shorten the due diligence period to convince sellers they are committed to the sale faster than their competitors.

Is Shorter Better?

Many buyers have realized they can shorten the due diligence period significantly without incurring risks for several reasons. First, the high purchase prices involved allow buyers to be less concerned about minor financial underwriting discrepancies discovered during the diligence period.

Second, in the current environment, buyers are less likely to receive price reductions based on information discovered during the due diligence, so this time period has less strategic significance during transactions.

Third, sellers typically include prepackaged due diligence as part of their bid-offer packages. This gives potential purchasers a better understanding of a property's condition prior to submitting their bids and purchase agreement comments.

Fourth, many institutional buyers have the means to complete all-cash deals. With no lender requirements, buyers don't need long diligence periods to obtain financing.

Fifth, because of marketplace competition, buyers are more willing to commit funds and resources to investigate properties before they are in an exclusive position to purchase them. Therefore, significant due diligence is completed before the bidding process even begins.

Lastly, the pace at which diligence is completed has increased dramatically due to large volume buyers who assemble

teams of internal and external consultants that are ready to perform their investigations quickly.

Streamlining the Process

To compete effectively in today's marketplace of shrinking diligence periods, buyers should consider outsourcing due diligence as much as possible. Professional consultants have the experience and expertise necessary to complete the diligence quickly and thoroughly, including the knowledge of issues that need more-detailed investigation as well as those that are unlikely to affect the purchase price. Many non-technical functions that traditionally have been completed internally, such as reviewing leases, rent rolls, operating expense budgets, contracts, and litigation, can be performed by external consultants to save time.

In addition, buyers should have a combined internal/external acquisition team assembled and standing by to conduct environmental, seismic, and physical condition inspections. The team should comprise dedicated and experienced personnel ready to act before and immediately after purchase and sale agreements are signed.

In today's super-heated real estate market, buyers are agreeing to shorter diligence periods than ever before to gain a competitive advantage. But it is likely that shorter due diligence soon will become a prerequisite for buyers to even be considered in a competitive-bid process.

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