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The Riddle Report

Professional Management Of Residential Condos

Whether the condos are converted from apartments or built from the ground up, the builder-developer, the project lender and even the unit purchaser in a condominium project should all be concerned with the proper management of the project. Without good management, a project can quickly lose its value and begin a downturn.

The owners in a condo project are free of the day-to-day maintenance cares that beset homeowners. They can best enjoy that freedom when the project is operated and managed by trained and capable people. The fact is that condominium management requires the expertise of a sophisticated professional manager. The manager’s skills can be profitably employed during the project design stage, while the building is being completed, and for the ongoing daily operation of the condominium development.

The Design Stage

Skilled professional property managers contribute a good deal to the success of the project by focusing their attention on building into the project low maintenance requirements and durable materials and facilities. They will be concerned with creating trouble free housing accommodations. Their skills complement those of the builder and architect, and their knowledge and experience can be very useful

in achieving a set-up that makes for efficiency and economy.

Start-Up Functions

Among the first things a professional property manager will do upon taking over the management of a project is to learn about the buildings and how they work. He or she will determine the stage of completion and when the remaining work will be completed.

Management functions should, as a rule, be separate from construction and maintenance functions. The construction superintendent should not double as the property manager or vice versa. Regular maintenance service should be completely separate from subcontractor follow-up service. In this way, construction costs won’t become interwoven with maintenance expenses, and customer services won’t become confused.

- **Handling Move-In Problems:**

The property manager must schedule move-ins so that everyone can get through this difficult period with the least amount of friction and with the greatest economy. If the property is a high-rise structure, the problems are multiplied.

Most buildings can’t accommodate many move-ins in one day. Physical



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This publication is not a solicitation but is an information service from this office.

In This Issue

- Professional Management Of Residential Condos
- The Corporate Negotiation Team
- The Value of The Master Lease
- Real Estate Investment Guidance
- A Land Development Agreement

When ideas in tax and other legal areas in this publication seem to fit your situation, it is recommended that you discuss them with your professional advisor before taking action.

(continued)

limitations of truck parking and loading areas, corridors and lobbies, elevators, etc., all impose very definite limits on the number of move-ins that can be handled at one time. In most situations, management will try to handle move-ins on a phase-by-phase basis or even a floor-by-floor basis in large buildings.

- **Parking Problems:** Parking spaces have to be assigned before move-ins are scheduled. Generally parking spaces are assigned on a first-come first-served basis.

If garage parking is insufficient, the property manager might want to provide valet parking so that the aisles can be used. The property manager might set up a parking space priority list. As condominium units are resold, the unit owners that have top priorities are entitled to the newly available spaces.

- **Perfecting Plan for Ongoing Operations:** As the buildings near completion, the property manager will have to negotiate building-service contracts, buy janitor supplies, and perfect and complete pro-forma operating budget. The manager will also help the homeowners'

association devise rules and regulations for the orderly operation of the common areas before the condominium-unit owners move in.

In Operation

Once the buildings of a condominium development are completed, occupied, and in operation, a full-time property manager will be responsible for overseeing the operation of the entire development. He or she will be involved, for example, with bookkeeping, housekeeping, planning for the future, keeping peace among unit owners, everyday service problems, move ins and move-outs and much more.

The Managers

The services of skilled, resident, professional property managers are a must for condominium developments of 200 or more units, and are recommended for developments with 35 or more units. Developments with fewer units, say 20 to 30, can also benefit from the services of professional property managers. With 20 units or fewer, the part-time services of a professional property manager might be available for a reasonable expenditure. □

The Corporate Negotiation Team

A corporate negotiating team is now part of the major decision making process in the acquisition of real estate and lease negotiations. This team may consist of legal counsel, finance department representatives, outside specialists such as real estate brokers or tenant representatives, design and engineering consultants, and others.

In today's market, corporate tenants with high credit ratings, who are willing to make long-term lease commitments negotiate from a strong position. Therefore, corporations that formerly treated real estate transactions in a matter-of-fact way have now developed detailed real estate negotiating strategies. The corporate tenant sees these negotiations as a way to cut costs within the company (whether upsizing or downsizing).

Landlords, developers, and brokers must be aware of this new style of negotiation. While the real estate executive plays a key role in developing the strategy, the other parties must be ready to respond quickly to requests for information and be prepared to discuss issues that rarely if ever arose in the past.

Request For Proposal

The document that best illustrates the new negotiating process is the Request For Proposal (RFP), sent to property owners. The RFP incorporates the specification for rental rates, free rent, up fitting, operating expenses, options, cash incentives and other "money clauses" that the corporation intends to negotiate. A short list of prospective sites or buildings is then prepared based on the

initial responses to the RFP. The corporate real estate executive (often with the aid of a real estate broker) will negotiate to obtain the best deal with the prospective landlords.

The RFP usually contains a number of items that are nonnegotiable—for example, amount of usable square feet, geographic area, lease term, expansion option, parking facilities, and security. On the other hand, many items remain negotiable, such as rent rate, concessions, rent escalations, cash inducements, and amenities. The parties should understand from the outset that failure to obtain a non-negotiable term could kill the deal for the tenant. Other items may be "throwaways" that could be modified or omitted from the lease.

Example: A corporate tenant may lack the capital funds to improve the leased premises, and so may be willing to pay a higher rental rate or extend the lease term in exchange for a larger allowance for improvements. Alternatively, the tenant may be willing to fund all or part of the improvement costs in exchange for a lower rental.

Bargaining position in Negotiations

Although it is obvious that any negotiating process involves give and take by both sides, corporate real estate executives have learned the importance of understanding the strengths and weaknesses of their bargaining position as well as that of the landlord. Within reason, these tenants are assured of getting whatever is needed if the bargaining team is aware of the options and takes carefully calculated risks based on solid information. □

The Value of The Master Lease

Business leaders are optimistic about the long-term future of corporate development. When new development is occurring in a market and developers are anxious to sell when the construction is complete, use of a master lease may facilitate a sale before the lease-up period is ended. A master lease is a form of seller guarantee that has several specific goals:

- It enables the seller to negotiate a price that reflects a stabilized occupancy and the long-term potential of the property.
- It assures the purchaser of a guaranteed level of income over an initial period and so assures for payment of debt service and equity dividends.
- When an appraisal is a necessary prerequisite for the purchase, the master lease enables an appraiser to value the property without regard to the initial vacancy rate (although certain adjustments may be required).

When a seller agrees to become a master tenant (and so be responsible for the agreed rental regardless of the actual occupancy level), the seller usually insists on having the management contract for the property for the duration of the master lease to assure an

aggressive leasing effort. This also enables the seller to earn leasing commissions and usually is agreeable to the purchaser, which also is interested in achieving full occupancy as soon as possible.

The Terms That Protect Buyer And Seller

The essential purpose of a master lease is to assure the buyer that it will receive a specific amount of cash flow throughout the master lease term. The obligation on the seller can be structured in one of several ways. The seller may guarantee that a certain occupancy level will be maintained or that gross rents will not decline below a specified amount. The lease should contain protective provisions for the buyer; for example, the seller (as manager) should not be able to reduce rents below market merely to achieve a higher occupancy rate. Similarly, the seller-manager should not be able to offer additional and costly amenities in order to increase gross rental revenue. The term of the master lease usually will approximate the estimated time for the property to attain stabilized occupancy. Finally, the obligation of the seller should be secured through an escrow account, letter of credit or other form of guarantee. □

Real Estate Investment Guidance

Which way is the right way in real estate investments in 2020? What is the future in these investments? An answer to these questions can be an interview with an interested professional real estate broker who can act as a real estate investment counselor. Each prospective investor can be interviewed in depth to find out specific needs in an income property. At the same time their needs are being evaluated, the broker will also communicate what benefits are available in various properties and how to identify them.

Some considerations should be given to the risk of loss for each age bracket of investor. Should an older investor purchase a property with the smallest down payment and highest leverage position? This will limit cash flow and may cause the property to have a “negative” cash flow. Is this what they want—or do they want cash flow from the property?

How about the younger investors? Are their objectives for long-range estate building or for current cash flow? Would they be more willing to take chances with a marginal investment that might

bring big returns later?

Each investor must decide these answers for himself or herself. But, only after enough information has been furnished so that an intelligent decision can be made.

When a new investor has a better idea of the type of property that will do the right job for him/her, or them, then and only then should they be exposed to the market place and shown specific properties. Now the investor or investors can evaluate the various benefits and risks for the information shown on each property and apply the information to their own situation.

What is right for you? A new rental unit? A strip center? A one hundred-unit apartment property? Perhaps you should have five or six apartments or commercial properties in scattered locations. Real estate counseling can show you that you can choose which is right for you and know the reasons why it is right! □

A Land Development Agreement

The acquisition and improvement of land is a large-scale operation and requires large amounts of capital. This has created methods of land acquisition that gives the developer access to and control over a large enough tract to make development economical without requiring an initial outlay of all of the capital necessary to acquire such a tract. From the point of view of the landowner, the disposal of a large tract at a good price may require a formula that will encourage the developer to commit improvement and development money for part of the tract that will build future value into the entire tract.

This may be accomplished by the following:

- The developer sets up a master plan that sets forth the general scheme of development and submits it for the approval of the owner.
- The developer and owner enter into an agreement setting forth the acreage prices for the entire property.
- Owner and developer agree on the number of years over which the full development is to be completed.
- To protect the owner against freezing of his property, the developer firmly commits to buy a predetermined number of acres each year.
- If the developer fails to meet this schedule, the owner is released from his commitment.

A Development Agreement

Another way of handling the problem is for the developer to share the net profits from the land development with the landowner. This can be done

by a “land development agreement” in which the developer agrees to perform the platting, the laying out, the installation of lot improvements, and the promotion of the subdivision. The landowner agrees to accept a percentage of the sales price of each lot, with a fixed minimum guaranteed. For example, the developer agrees to pay net to the landowner 25% of the sales price of each lot sold, with a minimum of \$50,000 per lot.

With this kind of arrangement, it is important to protect the landowner from finding his land cluttered up with liens left by a subdivider who went broke. The landowner should consider confining the developer or subdivider to a small tract of land at a time and give him “rolling options” to acquire additional parcels at intervals over a period of time. Failure to keep up with this purchase program results in loss of future options. The land that has been optioned but not purchased is not subject to liens against the developer.

A Liability for Not Proceeding With Development.

In one case, a jury found that a village breached its contract with a real estate developer calling for the village to acquire property and convey it to the developer for construction of apartment houses and a shopping center, all conditioned on obtaining financing from HUD. The village repudiated its explicit undertakings, to acquire and convey property to the developers. HUD had granted the main application and was in the process of considering the other grants involved, so the village could not back out of its promise. [Heritage Commons Partners v. Village of Summit, 730 FSupp 821, (ND Ill. 1990)] □



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A CCIM is a professional real estate practitioner with proven technical expertise in commercial property. A CCIM is a person truly committed to the fundamentals of effective commercial-investment brokerage. The CCIM has completed a full schedule of Post Graduate Level Courses in investments, taxation, development and marketing all types of commercial-investment properties. The designation of Certified Commercial-Investment Member is unquestionably the highest degree awarded in the commercial-investment real estate practice.