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Opportunities, challenges abound in 'broken' RE developments

With a modest economic recovery seemingly in sight, many real estate developers have been sifting carefully through the wreckage of the last several years with the hope of finding promising land development and redevelopment projects that had become victims of the Great Recession and never got above ground. Many of those projects were conceived, underwritten and possibly even entitled with what we now know was an overly optimistic outlook. With the proper review, assessment and restructuring, some of those broken developments will constitute the best opportunities currently available in the market, provided that developers are aware of the unique obstacles that must be negotiated when attempting to restart projects. Following is a brief discussion of three major phases that developers should consider before attempting to restart or restructure a broken development.

■ **Current condition/due diligence.** It is essential to comprehensively review and understand the current state of the broken development. Once an opportunity is identified, an interested developer should secure access to the property and information related to it, as well as some measure of control over potential negotiations for the property, by entering into a letter of intent or similar preliminary agreement with the current owner or other controlling party, including a commitment to take the property off the market during an agreed-upon review period. After securing access to

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the property, related information and the right to negotiate with the current owner or controlling party, the developer should undertake a full investigation and evaluation of the property: its title, existing and potential liens, public approvals and entitlements, permits, committed undertakings, neighborhood support or opposition, financial status, physical and environmental conditions, existing contracts and any litigation and regulatory proceedings, to name a few of the likely matters that will impact the feasibility of the opportunity.

To be sure, many broken developments were brought down by some manner of financial distress, so the developer's diligence will necessarily include identification of all of the development's creditors, including their ability to control the property and its transfer, as well as any governmental, quasigovernmental and private entities such as metro districts, urban renewal authorities and community associations that may be owed monetary or nonmonetary obligations with respect to the property. Of course, market distress may have contributed to the development's failure, so understanding the current nature of the property's zoning,

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platting, entitlements and related commitments is surely necessary and critical to the developer's assessment of the development's feasibility.

The goal of the developer's diligence is to understand what options are available to the developer if it attempts to repair the development and the challenges associated with each option. With that understanding, the developer can then either abandon the opportunity or attempt to enter into an agreement with the development's current owner or controlling party that will give the developer time to further assess and pursue any necessary re-entitlement of its desired development alternatives with the right to purchase the property if that re-entitlement proceeds favorably.

■ **Revision and restructuring.** Once the proper diligence has been performed and the developer has an exclusive right to pursue re-entitlement, the developer should then analyze, in the context of what went wrong with the original plans, revised plans for the development, incorporating the input of stakeholders, current market intelligence and future market forecasts, the current market requirements of intended equity and debt capital providers – lessons learned from the last development cycle and any other changes that are necessary to position the project for success in the current market. Few real estate projects, let alone broken developments, will be truly successful without taking into account the input of stakeholders and partners such as the approving governmental and quasi-governmental authorities, investors and lenders, neighboring landowners and neighborhood organizations, intended end-users and the developer's team. Of critical importance today is a realistic understanding of the current-day requirements of the public and private financing sources and the challenges associated with securing their commitments to the new plan. Without important end-user commitments in hand, the ability to secure adequate financing (debt or equity) is unlikely. While it is beyond the scope of this article to summarize the myriad mishaps that led to today's broken developments, it can be said that tomorrow's successful real estate projects will undoubtedly be based more on current rather than projected market conditions.

■ **Implementation.** With a thorough understanding of where a development has been and where it needs to go, developers should then focus their attention on implementation. Implementation will include securing final approval of the developer's plan by the stakeholders mentioned above, equity and debt capital commitments, premarketing to any anchor users.