

Loan Purchase Due Diligence Transaction Checklist (Commercial Real Estate)

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Status: **Maintained** | Jurisdiction: **United States**

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A Standard Document containing a checklist of actions and considerations for entities contemplating the purchase of an existing loan or loan portfolio from a real estate lender. This Standard Document is intended for a purchaser conducting due diligence of a loan file.

DRAFTING NOTE: READ THIS BEFORE USING DOCUMENT

Loan Purchase and Sale Transactions

Loan purchase and sale transactions tend to be more prevalent when real estate markets decline because lenders want to rid their portfolios of non-performing loans. Loans can be purchased at par value or, in the case of non-performing loans, at a substantial discount. A loan purchase can be in the form of a single loan or a group of loans together in a portfolio.

Because a loan purchaser is stepping into the shoes of the lender, it must evaluate risk and calculate the likelihood of realizing the projected return on its investment (see Loan Purchaser Due Diligence).

Loan Purchase and Sale Agreements

Once the parties agree on a purchase price for the loan or group of loans, they sign a loan purchase and sale agreement. Usually in a loan purchase, the parties do not sign a letter of intent.

The loan purchase and sale agreement resembles a typical real estate purchase and sale agreement. However, certain topics are handled differently.

Earnest Money Deposit

For institutional buyers, loan purchase and sale agreements do not typically require an earnest money or good faith deposit. For non-institutional buyers, whether earnest money is required is determined on a case-by-case basis. For a discussion on earnest money deposits generally, see [Standard Document, Purchase and Sale Agreement \(Commercial Real Estate\) \(Pro-Purchaser Long Form\): Drafting Note: Earnest Money Deposit](#).

Confidentiality

Given the sensitive information the purchaser is being permitted to review relative to the loan and the borrower, all loan purchase and sale agreements include confidentiality provisions which survive any termination of the agreement. Absent a loan purchase and sale agreement, the parties will sign a stand-alone confidentiality agreement (see Standard Documents, [Real Estate Confidentiality Agreement \(Pro-Disclosing Party\)](#) and [Real Estate Confidentiality Agreement \(Pro-Recipient\)](#)).

Limited Seller Representations, Warranties, and Covenants

The loan purchase and sale agreement typically has few seller representations, warranties, and covenants.



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A seller usually only covenants to:

- Make available a copy of the loan file.
- If the loan closes, deliver:
 - the assignment documents; and
 - the original loan file.

A purchaser might successfully negotiate a covenant from the seller to reasonably cooperate with the purchaser post-closing.

Furthermore, sellers usually limit their representations and warranties to statements that the seller:

- Owns the loan and holds the note.
- Has not previously transferred or encumbered its security interests.

A purchaser with negotiating leverage may persuade a seller to expand these representations and warranties to include one or more of the following:

- Confirmation of amounts for the current unpaid balance, accrued interest, and escrow or reserve accounts.
- A blanket statement about whether a default or event of default currently exists or is threatened.
- Confirmation on whether the seller has received notice from:
 - the borrower alleging default; or
 - the property tenants alleging a borrower default.
- Affirmation of completeness of the loan file.
- A statement that:
 - no mortgaged property has been released from the lien of the mortgage; and
 - neither borrower nor guarantor has been released from any of their respective obligations.
- Affirmation that no title claims, condemnation, or casualty event has occurred regarding the property.
- That the origination, servicing, and collection practices used by the seller are in all respects legal, prudent, and customary.

Because covenants, representations, and warranties are limited, it is critical for the loan purchaser to conduct detailed due diligence.

Purchaser's Due Diligence Rights

After the loan purchase agreement is signed, the seller delivers (sometimes electronically) a copy of its entire loan file to the purchaser. The purchaser should ensure that, in addition to traditional due diligence items such as title, survey, and property condition reports, including its environmental condition, the file includes items such as:

- Loan payment history.
- Information provided by the borrower or compiled by the seller about the property's:
 - income;
 - operations;
 - maintenance;
 - casualty history; and
 - management.

Purchaser has a period (typically 30 days) to decide whether it wants to proceed with the loan purchase. It conducts due diligence to evaluate any risks involved in purchasing the loan. The purchaser generally can terminate the purchase and sale agreement for any reason during the due diligence period.

Closing

If the purchaser decides to proceed, closing usually occurs immediately after the expiration of the due diligence period on a date certain. After due diligence expires, there are typically no further conditions to closing (as there might be in a real property purchase and sale transaction) and generally time is of the essence regarding the purchaser's obligation to close.

Loan Purchaser Due Diligence

Due diligence helps the loan purchaser to identify and evaluate risk. The extent of due diligence depends on several factors, such as:

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- The length of the due diligence period.
- The amount the purchaser is willing to spend on due diligence.
- The quality of the material provided by the seller.
- The age of the loan. The older the loan, the more likely that the loan file information is out of date.

Areas of Due Diligence Investigation

Counsel for the purchaser normally ask to review:

- The underlying loan documents (see Drafting Note, Loan Document Review).
- Information on any subordinate debt (see Drafting Note, Subordinate Loans, Mezzanine Loans, and Intercreditor Documents).
- Real estate-related reports, such as any:
 - inspection reports; and
 - environmental reports.

(See Drafting Note, Third Party Property Reports.)

- Property operations information, such as:
 - Insurance policies and whether coverage is adequate;
 - rent rolls;
 - operating statements;
 - tax notices;
 - lease agreements, estoppels, and tenant subordination agreements; and
 - ground lease documentation, if any.

(See Drafting Note, Property Contracts and Agreements.)

- Title policy, survey, and zoning information (see Drafting Note, Title Policy Review).
- Borrower entity information from closing (see Drafting Note, Borrower Party Information).
- The legal opinion issued at loan closing (see Drafting Note, Legal Opinion).
- Additional new information gathered including:
 - an updated title report;
 - updated property information;

- new information on the borrower and the guarantor.

(See Drafting Note, Additional Due Diligence.)

The role of the purchaser's counsel is to give the purchaser feedback on the materials reviewed. An important part of that review is identifying what may be missing from the files. It is common for the servicing files to be incomplete. The due diligence period is usually the purchaser's only opportunity to track down missing information and documentation.

The purchaser's counsel should have a well-organized and a straightforward method of communicating results of due diligence to its client. This Standard Document provides a comprehensive checklist of documents to review and issues to look for when reviewing a loan file as purchaser's counsel.

State and Local Laws

This Standard Document should be modified to reflect any supplemental items that may need to be reviewed based on applicable governing law. Consult with local counsel to determine whether local laws or customs require additional document review.

Assumptions

This Standard Document assumes:

- The purchaser is buying one or more permanent, fully funded loans.
- The parties have signed a loan purchase and sale agreement.
- The loan purchaser is unrelated to the loan seller.
- The transaction parties may be institutional or private equity lenders.
- The transaction is as is.
- The loan seller gives no representations and warranties about:
 - the condition of any loan collateral;
 - the completeness of the loan file; or
 - the enforceability or priority of the lien of the lender's security interests.

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- The loan seller may or may not agree to give limited representations and warranties about the seller's:
 - authority to enter the transaction; and
 - ownership of the loan.
- The loan purchase and sale agreement establishes a short due diligence period for loan file inspection and all other purchaser due diligence.
- The closing date is time is of the essence on the purchaser's part.
- The loan purchase and sale agreement is terminable by the purchaser for any reason.
- The purchasing entity is prohibited from being a borrower-related entity.
- The loan is not securitized or, if securitized, the special servicer has approved the sale.

Bracketed Items

Bracketed items in ALL CAPS should be completed with the facts of the transaction. Bracketed items in sentence case are either optional provisions or alternative language choices to be selected, added, or deleted at the drafting party's discretion.

Loan Purchase Due Diligence Checklist

[Pool ID: [POOL ID NUMBER]]

Loan Number: [LOAN NUMBER]

Borrower: [BORROWER NAME]

Property Type/State: [PROPERTY TYPE]/[STATE WHERE PROPERTY IS LOCATED]

Reviewer Name: [REVIEWER NAME]

A. Loan Documents

DRAFTING NOTE: LOAN DOCUMENTS

Due diligence begins with a review of the underlying loan documents to understand the loan's principal terms. The first steps of loan document due diligence are to:

- Confirm the loan files contain all documents, instruments, and reports delivered at loan closing.
- Review and summarize the terms of the loan documents.
- Identify any missing documents, pages, signatures, exhibits, or attachments.
- Identify any errors, omissions, or ambiguities in the terms and provisions of the loan documents.

Because loan purchase and sale agreements do not typically require the seller to remediate any

loan document deficiencies, serious errors or omissions may cause the purchaser to terminate the transaction.

The purpose of this section of the checklist is to identify and briefly summarize the key terms of the loan documents. All of the documents listed below may not exist for every loan, but every file must include a promissory note and a mortgage or deed of trust. If time permits and lender will pay for it, the purchaser's counsel may prepare a more detailed abstract of the loan documents, with legal analysis and recommendations. For a sample form of loan abstract, see [Standard Document, Commercial Real Estate Loan Abstract \(NY\)](#).

Loan Purchase Due Diligence Transaction Checklist (Commercial Real Estate)

Document	Status (Indicate any missing pages, signatures, blanks, exhibits, and other irregularities)	Summary
Promissory Note(s)		Date: _____ Amount: \$_____ Lender: _____ Borrower: _____ Maturity date: _____ Applicable interest rate: _____ Debt service payment date: _____ Prepayment permitted: Y/N Prepayment terms (if applicable): _____ Defeasance permitted: Y/N Late payment fees: _____ Default interest: _____
Allonge(s) to Note		Date: _____ Assignor: _____ Assignee: _____
Mortgage/Deed of Trust		Date: _____ Loan amount stated: Y/N If yes, does it match the Promissory Note: Y/N Lender name match Promissory Note: Y/N Borrower name match Promissory Note: Y/N Recording information: _____ Legal description match title policy: Y/N
Assignment and Assumption of Mortgage/Deed of Trust		Date: _____ Recording information: _____ Assignor: _____ Assignee: _____
Assignment of Leases and Rents		Date: _____ Recording information: _____ Assignor name match Borrower in Promissory Note: Y/N Assignee name match Lender in Promissory Note: Y/N

Loan Purchase Due Diligence Transaction Checklist (Commercial Real Estate)

Document	Status (Indicate any missing pages, signatures, blanks, exhibits, and other irregularities)	Summary
Loan Agreement and all amendments		Date: _____ Amount: \$_____ Lender name match Promissory Note: Y/N Borrower name match Promissory Note: Y/N Reserve requirements: (Summarize type, duration, and amount of required reserves) _____ _____ Financial and reporting requirements: (Summarize) _____ _____ Standard borrower covenants: Y/N Briefly describe any special covenants/provisions: _____ _____ Lender consent required for all transfers other than standard permitted transfers: Y/N Borrower required to cooperate with Lender's request for documents and information: Y/N Briefly describe any limits (time, expense, frequency) applicable to Borrower cooperation: _____ _____ Lender representations, warranties, or indemnities to Borrower: Y/N Lender required to respond to consent requests to avoid consent being deemed given: Y/N Lender unconditionally entitled to transfer the loan without the consent of any party: Y/N
Cash Management Agreement		Date: _____ Lender name match Promissory Note: Y/N Borrower name match Promissory Note: Y/N Type of lockbox: Hard/Soft/Springing
Deposit Account Agreement		Date: _____ Lender name match Promissory Note: Y/N Borrower name match Promissory Note: Y/N Depository bank: _____

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Document	Status (Indicate any missing pages, signatures, blanks, exhibits, and other irregularities)	Summary
Guaranty		Date: _____ Guarantor(s): _____ Beneficiary name match Lender in Promissory Note: Y/N Recourse liability: Full/Limited/Nonrecourse with carveouts Financial (net worth and liquidity) and reporting requirements, if any: _____ _____ Describe any burndown provisions or surviving liability: _____
Environmental Indemnity Agreement		Date: _____ Indemnitor(s): _____ Indemnitee name match Lender in Promissory Note: Y/N Cap on environmental liability? Y/N If yes, amount: \$ _____ Any limitations on survival of liability? Y/N If yes, describe: _____
Other Loan Documents		
UCC-1 Financing Statement		<p>State</p> Filing date: _____ Document number: _____ Where filed: _____ Secured Party name match Lender in Promissory Note: Y/N Debtor name match Borrower in Promissory Note: Y/N Older than 5 years: Y/N Continuance filed: Y/N Collateral description: Full/Generic <p>County</p> County of recordation: _____ Recording information: _____ Secured Party name match Lender in Promissory Note: Y/N

Loan Purchase Due Diligence Transaction Checklist (Commercial Real Estate)

Document	Status (Indicate any missing pages, signatures, blanks, exhibits, and other irregularities)	Summary
UCC-3 Financing Statement (Continuation)		Debtor name match Borrower in Promissory Note: Y/N Older than 5 years: Y/N Continuance filed: Y/N Collateral description: Full/Generic Date: _____ Secured Party name match Lender in Promissory Note: Y/N Debtor name match Borrower in Promissory Note: Y/N

DRAFTING NOTE: LOAN DOCUMENT REVIEW

Promissory Note

The promissory note evidences the loan. It is the document by which the borrower unconditionally promises to repay all sums borrowed on specified terms.

Delivery of the Original Promissory Note

The purchaser should require the seller to confirm it is in possession of the original promissory note. The loan purchase and sale agreement should require the lender to deliver the original promissory note to the purchaser on completion of the loan purchase. It is typical to require an in-person delivery of the original note immediately after closing, with the loan file to follow via insured delivery service. It is important for the purchaser to take possession of the original promissory note, not a copy. Many jurisdictions have disallowed lenders to exercise their right to foreclose because the lender could not produce an original promissory note or prove that they were the rightful note holder.

Chain of Title

The lender's name in the promissory note must be identical to the seller under the loan purchase and sale agreement. If not, look for transfer documents and establish a chain of title. Confirm borrower's name is the same in all loan documents and that all signature blocks are accurate.

In all cases, entity names should be precisely stated including punctuation and abbreviations. Entity names should be confirmed by a current (within 30 days) state-issued certificate of good standing or the equivalent from the jurisdiction in which the entity is formed or doing business (see Drafting Note, Borrower and Guarantor Due Diligence).

Allonge to Promissory Note

An allonge is an instrument that endorses a promissory note from one note holder to the next. The existence of one or more allonges indicates the loan has been previously transferred and that the loan seller is not the original lender. The loan purchaser should confirm the loan's chain of ownership is

unbroken and that the seller is the rightful owner and holder of the original promissory note. Any allonge being received by the purchaser should also be an original signature, not a copy.

Mortgage or Deed of Trust

These instruments create the lender's lien and security interest in the real estate which is the collateral securing the payment and performance of the borrower's loan obligations. Without a mortgage or deed of trust, the loan is unsecured, and the purchaser would have no right to the real estate collateral.

The purchaser must confirm that both the legal description attached to the mortgage and the recording information for the mortgage exactly match the seller's title policy (see Drafting Note, Title Policy Review). The purchaser should also confirm that any assignments of the mortgage (as reflected through any allonges in the file) have been properly recorded.

Loan Agreement

The loan agreement contains most of the information on covenants, representations, and warranties and the rights of the parties. If there is not a loan agreement, then look for the loan's key business terms in the provisions in the mortgage or deed of trust.

The information culled from the loan agreement and included in this checklist is a snapshot. Issues of permitted transfers, borrower cooperation, lender indemnities, and other important provisions are sometimes abstracted in more detail by the purchaser's counsel (see [Standard Document, Commercial Real Estate Loan Abstract \(NY\)](#)).

Cash Management Agreement

Not every loan has a cash management system in place, but if one exists, the purchaser must arrange to transfer control of the cash after closing. This

transition requires cooperation from the seller and third parties. Since not much cooperation is routinely required of the seller, this issue must be anticipated and addressed in the loan purchase and sale agreement. Cash management agreements typically have a separate notice requirement to the cash management bank to comply with when the loan is transferred. For more information on cash management agreements, see [Practice Note, Cash Management for Commercial Real Estate Loans](#).

Deposit Account Control Agreement

A deposit account control agreement is expected where:

- A hard cash management system is in place.
- There is a separate signed agreement with a depository bank.

It is important for the purchaser to know who is holding these funds and how the funds are to be disbursed. The deposit account agreement typically has a separate notice requirement to the depository bank to comply with when the loan is transferred. For more information, see [Standard Document, Deposit Account Control Agreement](#).

Guaranty

The purchaser must understand the recourse liability assumed by the loan guarantor. Knowing whether the guaranty is full recourse, limited recourse, or nonrecourse with carveouts is critical for a purchaser as it assesses if the loan is adequately secured.

Most commercial real estate borrowers and lenders structure their financing arrangements as nonrecourse loans. This means, in essence, that if the borrower defaults, the lender can exercise remedies against the collateral, but it cannot pursue the borrower, its constituent members and managers, or its guarantors and indemnitors personally.

Nonrecourse carveout guaranties allow the lender to have recourse beyond the collateral for certain negotiated matters that are expressly carved out from nonrecourse treatment. These are typically bad acts on the part of the borrower. For a non-performing loan, the purchaser wants to determine whether recourse has been triggered based on the borrower's conduct.

The purchaser should also confirm whether there are any other limitations on the guaranty, such as:

- A monetary cap on the guarantor's liability.
- A time-based limitation after which the guarantor's liability changes or terminates.

For more information on non-recourse carveout guaranties, see [Standard Clauses, Nonrecourse Carveout Provisions in Commercial Real Estate \(Mortgage Loans\) \(Pro-Lender\)](#) and [Standard Document, Guaranty of Nonrecourse Carveout Obligations \(Pro-Lender\)](#).

Environmental Indemnity

An environmental indemnity agreement is given by the borrower and by one or more creditworthy persons or entities, each typically an equity owner with the ability to control or manage the borrowing entity. The purpose of an environmental indemnity agreement is to limit a lender's exposure for environmental risks associated with real property ownership.

If there is a cap or limit on liability under the environmental indemnity agreement, ideally the purchaser wants updated environmental information. However, this is not always feasible given the timing for due diligence. If new environmental studies are not possible, the purchaser should at a minimum conduct a thorough public record search to see if there is anything of record demonstrating adverse environmental conditions.

If there is a known environmental problem with the property, this issue is best addressed in the loan purchase and sale agreement. The seller will not give an indemnity but might represent and warrant that no environmental issues have arisen since the loan was originated. For a more detailed discussion of potential environmental liabilities, see [Practice](#)

[Note, Commercial Real Estate Loans: Lender's Environmental Liability.](#)

Sunset Clauses

Indemnitors are often reluctant to carry the surviving liabilities of an environmental indemnity agreement on their books indefinitely. Therefore, some environmental indemnity agreements contain a sunset clause. A sunset clause provides that the indemnitors' obligations terminate on a date certain, usually one to five years following the repayment of the loan or lender's foreclosure on the real property, subject to certain exceptions. For more information on sunset clauses, see [Standard Document, Environmental Indemnity Agreement \(Pro-Lender\): Drafting Note: Survival.](#)

Other Loan Documents

There are some documents that a reviewer may find in a loan file that are not included in this list because they are not a part of what is standard in most loans. These documents might include:

- Security agreement or pledge of interests in the borrower entity.
- Loan modification agreement.
- Bond agreements.
- Interest rate cap agreement.
- Contribution agreement(s) (if multiple borrowers).

These types of documents should not be overlooked as they too provide important information about the loan.

UCC-1

Security interests in most types of personal property can be perfected by filing a properly completed UCC-1 financing statement (UCC-1) in the appropriate filing office (see [Practice Note, UCC Creation, Perfection, and Priority of Security Interests](#)). The purchaser wants to ensure that the lender has properly perfected its liens and that the personal property is part of the collateral securing the loan being purchased. If the interests in the borrower will serve as collateral for the lender, the purchaser should confirm a separate UCC-1 securing the pledge of those interests has been filed.

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B. Subordinate Loans, Mezzanine Loans, and Intercreditor Documents:

Intercreditor Agreement

Date: _____

Senior Lender: _____

Junior Lender: _____

Co-Lender/ Participation Agreement

Date: _____

Lender A: _____

Lender B: _____

Subordination Agreement

Date: _____

Subordinating party: _____

Party receiving subordination: _____

Subordinate Loan Documents

Mezzanine Loan Documents

DRAFTING NOTE: SUBORDINATE LOANS, MEZZANINE LOANS, AND INTERCREDITOR DOCUMENTS

The purchaser must understand what, if any, additional debt encumbers the property or the borrower, how that debt is structured, and if enforcement of the debt is subject to any agreements among multiple lenders.

Subordinate Loans

A subordinate mortgage can pose several risks to the first mortgage lender, such as:

- **Increased bankruptcy risk.** After an event of default under the second mortgage loan, the second mortgage lender may be more likely to file an involuntary bankruptcy action against the property owner.
- **Problems in bankruptcy.** If the mortgage borrower is embroiled in a voluntary or involuntary bankruptcy proceeding, the rights of the second mortgage lender can impede, delay, or adversely affect the enforcement actions of the first mortgage lender. In a borrower bankruptcy, the second mortgage lender:
 - is a secured creditor of the mortgage borrower, depriving the first mortgage lender of the

privileged position of being the sole member of its class;

- may assert, under various legal theories, that all or a portion of the second mortgage lien should take lien priority over the first mortgage loan; and
- may challenge the first mortgage lender's rights to rents and other income generated by the property (see [Practice Note, Postpetition Interest, Fees, Costs, and Charges in Bankruptcy](#)).
- **Drain on Funds Available.** A lender depends on property-generated income to satisfy the loan's debt service obligations. If there is also a subordinate loan, the property must generate enough income to pay debt service for both loans. This can pose a significant downside to the senior lender if the property is not performing well enough to fund both loans.

Although a first mortgage lender has the power to extinguish a second mortgage lien on foreclosure, until that time the purchaser will inherit the loan subject to whatever subordinated debt is in place, it must understand what this is and how it will impact the loan.

Mezzanine Loans

Mezzanine loans are loans made to the property owner principal who pledges its ownership interests as security for the loan. They are only indirectly secured by the real estate collateral in the mortgage loan. Mezzanine loans are subordinate to mortgage loans made to the property owner. Because the collateral for a mezzanine loan is ownership interests in a company as opposed to real property, the creation and perfection of a security interest in the collateral is governed by the UCC. Mezzanine loans enable financing of a property in an amount in excess of the maximum leverage ratio permitted under a mortgage loan.

To understand the loan borrower, the purchaser must understand any mezzanine financing affecting the borrower's equity owners.

Intercreditor Documents

Intercreditor agreements are used between two or more lenders having a security interest in the same collateral. Their purpose is to establish the priority of liens and to set out each lender's respective rights and obligations both before and after any potential borrower default.

The issues addressed in an intercreditor agreement depend on the type of subordinated debt in place. However, the purchaser wants to ensure that its rights are superior in all instances and to understand what rights a junior lender may have.

For more information on how intercreditor agreements work, see [Practice Note, Intercreditor Agreements Between Senior and Subordinate Mortgage Lenders](#).

Co-Lender and Participation Agreements

Co-lender and participation agreements are used between two or more lenders that may have a pari passu or senior to subordinate interest in the loan. The purpose is to establish the responsible parties for servicing, management of the loan, and distribution of loan payments.

The purchaser should ensure that it understands exactly what control rights it will have on the purchase of the loan and any payment subordination that may occur.

For more information on how participation agreements work, see [Practice Note, Intercreditor Issues in A/B Loan Structures \(Commercial Real Estate Loans\)](#).

C. Third Party Property Reports:

Phase I or II Report

Date: _____

Phase: _____

Conclusion: _____

Is any O&M plan implemented? Y/N

If yes, identify hazard (radon, asbestos, etc.):

Environmental insurance policy obtained: Y/N

Issues: _____

Property Condition Report

Date: _____

Issues: _____

Did Loan Agreement provide for remediation of immediate repairs: Y/N

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DRAFTING NOTE: THIRD-PARTY PROPERTY REPORTS

Due diligence of the real property is done to:

- Verify the property's condition.
- Estimate the value of the collateral to confirm it exceeds the purchase price of the loan.
- Determine whether there are any risks associated with owning the property (if the purchaser were to succeed to the property owner through foreclosure).

Additional property-related reports relate to title, survey, and zoning (see Drafting Note, Title, Survey, and Zoning Review).

Once any risks are identified, the purchaser can decide whether it is willing to accept those risks.

Note that an appraisal is not identified as a property-related report to be reviewed as part of the purchaser's due diligence. Lenders generally refuse to provide a copy of any appraisal as part of the loan file. Loan purchasers must generally rely on their own due diligence to determine the property's fair market value.

D. Property Contract and Agreements:

Management Agreement

Date: _____

Manager's Name: _____

Are the Owner and Manager related? Y/N

Is agreement terminable without cause on 30-60 days' notice? Y/N

Termination fee, if applicable: _____

Assignment and Subordination
of Management Agreement

Date: _____

Manager's name match Management Agreement: Y/N

Franchise Agreement

Date: _____

Franchisor: _____

Franchisee: _____

Assignment of Contracts

Insurance

Property damage coverage: Y/N

Policy number: _____

Commercial general liability coverage: Y/N

Policy number: _____

Flood insurance: Y/N

Policy number: _____

Other insurance: Y/N

Type: _____

Policy number: _____

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Operating Statements	Date: _____
Rent Roll	Date: _____
Lease Agreement(s)	List known tenants: _____ _____
Lease Estoppel	List known tenants: _____ _____
Subordination, Non-Disturbance Agreement	List known tenants: _____ _____
Ground Lease	Date: _____ Ground Lessee name match Borrower in Promissory Note: Y/N Memorandum recorded: Y/N
Ground Lease Estoppel	Date: _____ Ground Lessor name match Ground Lease: Y/N Issues: _____

DRAFTING NOTE: PROPERTY CONTRACTS AND AGREEMENTS

Property Management Agreement

The purchaser is interested in all property contracts, particularly the property management agreement if the manager is collecting rents. This due diligence must be conducted to avoid interfering with the seller's contracts. Without the permission of the loan seller it may be able to contact the property manager until the loan sale is complete. Often, loan sellers are not cooperative or willing to disrupt the status quo before the loan sale is closed.

Management Agreement Due Diligence

Steps that the purchaser can take during its due diligence relative to the property manager include:

- Confirming the contact information for the property manager.
- Having a notice ready to send to the property manager the day the loan sale closes.
- Confirming the agreement is in full force and effect. If the loan is in default and the manager is borrower related, the issue of management replacement is also under consideration.
- Confirming the property manager must cooperate on a loan transfer and attorn to the new lender.
- Confirming the management agreement does not prohibit transfers or require advance notice of loan transfer.
- Requesting that the seller acknowledge in the loan purchase and sale agreement that they have received no notice of default on the part of the borrower or the lender under the management agreement or any assignment and subordination of management agreement.
- Persuading the seller to agree (even if informally) to give the purchaser notice of any new leases submitted by the property manager during the purchaser's due diligence.
- Trying to get from the seller as much historical information as possible that has

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been provided to the seller by the property manager, such as:

- reports;
- budgets;
- rent rolls; and
- property statements.

Property Insurance

The purchaser generally asks its insurance consultant to review insurance policies to:

- Ensure:
 - adequate coverages are in place;
 - no policy has expired; and
 - all policies are transferrable to the purchaser.
- Compare coverages to required coverages under the loan documents.
- Assist in getting the policies amended to name the purchaser as additional insured or loss payee, as appropriate.

See [Standard Clauses, Insurance Covenants and Requirements \(Commercial Real Estate Loan Agreement\)](#).

Property Leasing Matters

Part of determining the value of the real property is determining how much income the property

generates. Property income is evidenced in certified rent rolls and operating statements. It should also be confirmed based on the leases and any tenant statements or certificates, such as tenant estoppels.

There is not enough room on a checklist to note the key information for each lease. If the seller makes leases available to the purchaser in due diligence, they are often abstracted in a separate form. For a form of lease abstract, see [Standard Document, Commercial Lease Summary Chart \(Short Form\)](#).

Tenant estoppels and SNDAs help the purchaser understand the status of the leases at a given time.

Ground Lease

If the mortgaged property is subject to a ground lease, the purchaser must review the ground lease and any estoppel entered into at the time of financing. The estoppel often provides key information on the status of the ground lease and may include additional lender friendly terms negotiated with the ground lessor to improve the financeability of the ground lease estate.

The ground lease may require that an assuming lender provide the ground lessor with notice so the assuming lender can benefit from any leasehold mortgage protection provisions included with the ground lease. For more information on ground lease lender protections, see [Practice Note, Financeable Ground Leases: Key Considerations](#).

E. Title, Survey, and Zoning:

Title Policy

Effective date: _____

Policy number: _____

Issuer: _____

Signed: Y/N

Insured estate: Fee/Leasehold

Insured loan amount: \$_____

Confirm named insured is same as Seller and includes successors and assigns? Y/N

Was survey exception removed? Y/N

Loan Purchase Due Diligence Transaction Checklist (Commercial Real Estate)

Deed of trust/mortgage recording information accurate: Y/N

Legal description match Deed of Trust/Mortgage: Y/N

Problematic existing encumbrances: Y/N

If yes, detail: _____

Endorsements to Title Policy	Identify each title policy endorsement by name and number: _____ _____ _____ _____
------------------------------	---

Survey

Date: _____

Survey signed and certified to Lender: Y/N

Surveyor name and license number: _____

Survey file number: _____

Zoning Compliance	Date: _____ Issuer: Zoning letter/zoning report/zoning opinion/refer to survey Zoning designation: _____ Property in compliance: Y/N Any building or fire code violations: Y/N If yes, explain: _____
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Certificates of Occupancy

Date: _____

If not available, does the absence of a Certificate of Occupancy rise to the level of a violation: Y/N

DRAFTING NOTE: TITLE, SURVEY, AND ZONING REVIEW

Title Policy Review

The existing title insurance policy should:

- Confirm that the borrower owns the property.
- Accurately describe the recorded mortgage.
- Include a legal description that exactly matches the legal description attached to the recorded mortgage.

Schedule B Exceptions

Counsel should also review the existing loan title insurance policy to determine what exceptions to coverage existed in that title policy to determine whether there are any associated risks. These Schedule B items are commonly referred to as permitted exceptions. The purchaser should confirm all permitted exceptions are acceptable.

Title Endorsements

The purchaser should further confirm that all appropriate endorsements have been included, including, to the extent available in the jurisdiction:

- Access endorsement.
- Comprehensive endorsement.
- Same as survey endorsement.

Schedule A

The purchaser also should ensure that the defined insured on Schedule A includes the seller's successors and assigns to affirm the purchaser can assume the seller's place under the title policy on recordation of the loan assignment. The rights of a lender's successor under a mortgagee policy is now memorialized in the jacket of the ALTA form policy. However, most lenders still want Schedule A to affirm coverage to successors and assigns. For more information on reviewing title policies and for basic title insurance principles, see Practice Notes, [Understanding Title Insurance: Policy Coverage and Exceptions](#) and [Title Insurance Policies and Surveys: Overview](#).

The loan purchaser should order an updated title report as soon as possible to determine if any title issues exist other than the permitted exceptions (see [Drafting Note, Additional Due Diligence](#)).

Survey

Surveys enable the parties to verify with certainty that the mortgage encumbers the correct property. They also provide a visual for the permitted exceptions reflected in the title policy. Review of the survey

includes comparing it to the exception documents. The survey may also provide information on:

- Zoning.
- Setbacks.
- Flood zones.
- Parking.

Surveys can often be missing from a loan file. The title policy typically incorporates survey information. If the title policy sets out the surveyor's name and survey number, then the purchaser's attorney is often able to contact the surveyor directly to obtain a copy of the survey (for a fee). Surveyors are generally readily able to locate and provide surveys (even old ones) on request. For information on survey review generally, see [Practice Note, Title Insurance Policies and Surveys: Overview](#).

Zoning

Loan purchasers, like originating lenders, are concerned with verifying that the mortgaged property complies with local zoning laws (see [Standard Clauses, Borrower Representations and Warranties \(Commercial Real Estate Loan Agreement\): Drafting Note, Confirming Zoning Compliance](#)). Zoning laws determine how a property can be legally used (see [Practice Note, Zoning and Land Use Law for Owners and Developers: Overview](#)).

Certificate of Occupancy

A certificate of occupancy confirms that the property is safe and suitable for occupancy. Certificates of occupancy can be obtained directly from the municipality but are often provided as part of the zoning letter, the zoning report, or the zoning opinion.

F. Borrower Party Information and Legal Opinion:

Borrowing Resolution

By-Laws/Partnership Agreement/
Operating Agreement

Articles of Incorporation/ Certificate of
Formation

Loan Purchase Due Diligence Transaction Checklist (Commercial Real Estate)

Attorney Opinion Letter

Date: _____

Law firm: _____

Documents missing: _____

Unusual terms: _____

DRAFTING NOTE: BORROWER PARTY INFORMATION

Review of the borrower and guarantor formation and operating documents confirm that:

- The borrower and its guarantor were properly formed and, at closing, were authorized to enter the loan transaction.
- The borrower's governing documents do not contradict the covenants and requirements under the loan documents (SPE covenants, transfer covenants, etc.).
- The correct entity name is included in:
 - the loan documents; and
 - the lender's title insurance policy.

the legal opinions can give the purchaser some comfort that the loan documents are enforceable and binding against the borrower parties (see Practice Note, [Legal Opinions: Commercial Real Estate Finance](#)).

Legal opinions list the documents that the lawyer reviewed in rendering its opinions. It is a good idea to review opinion qualifications and cross-check the documents in the loan file to the list in the opinion letter. If any loan documents are cited in the opinion letter but not provided by the loan seller, the purchaser should specifically request all missing documents.

Legal Opinion

Although the loan purchaser cannot rely on the legal opinions given to the seller at loan closing,

G. Additional Due Diligence:

Updated Title Search

Date: _____

Owner match Borrower name: Y/N

Receipt of encumbrance docs: Y/N

New encumbrances: _____

Problematic encumbrances: _____

Updated property reports, if any

Date: _____

Document name: _____

New property inspection report, if any

Date: _____

Problematic findings: _____

Loan Purchase Due Diligence Transaction Checklist (Commercial Real Estate)

Property tax search		Received: Y/N Date: _____ Problematic findings: _____
Borrower good standing certificate		Received: Y/N Date: _____
Borrower qualification to do business in the state		Received: Y/N Date: _____
Borrower UCC and judgment lien search		Received: Y/N Date: _____ Problematic findings: _____
Borrower litigation/bankruptcy search		Received: Y/N Date: _____ Problematic findings: _____
Borrower Patriot Act search		Received: Y/N Date: _____ Problematic findings: _____
Borrower tax search		Received: Y/N Date: _____ Problematic findings: _____
Guarantor good standing certificate		Received: Y/N Date: _____
Guarantor qualification to do business in the state		Received: Y/N Date: _____
Guarantor UCC and judgment lien search		Received: Y/N Date: _____ Problematic findings: _____
Guarantor litigation/bankruptcy search		Received: Y/N Date: _____ Problematic findings: _____
Guarantor Patriot Act search		Received: Y/N Date: _____ Problematic findings: _____
Guarantor tax search		Received: Y/N Date: _____ Problematic findings: _____

Loan Purchase Due Diligence Transaction Checklist (Commercial Real Estate)

Missing documents to request from the seller

List: _____

Missing documents to request from third parties

List: _____

DRAFTING NOTE: ADDITIONAL DUE DILIGENCE

Updated Title

Loan purchaser should order an updated title report, together with all Schedule B exception documents, as soon as possible. The title report does not need to be completed by the same title company that issued the lender's title policy (but this can expedite the process).

The title update should:

- Be dated within 30 days of closing.
- Confirm that the borrower still owns the property.
- Reflect any title matters since the loan originated and the title policy was issued.

A seller typically has no duty to address title problems so if any new material matters affecting title arise, the purchaser must take that information under advisement and weigh any associated risk. Although additional easements or minor violations generally will not cause a purchaser to terminate the transaction, unpermitted transfers or new liens or encumbrances might.

Borrower and Guarantor Due Diligence

Due diligence on the borrower parties is done to confirm that:

- The borrower and its guarantor:
 - remain in good standing in their respective state(s) of formation;
 - remain authorized to do business in the state where the property is located;
 - are not prohibited parties under the Patriot Act;
 - are not in litigation or bankruptcy or subject to the protection of any debtor relief laws.
- No unauthorized transfers or encumbrances on the interests of the borrower parties have occurred since loan closing.

Documents to Request

Purchaser's counsel should keep track of any documents missing or material deficiencies in the documents from its review of the due diligence materials. Most missing information may be forthcoming from the seller but some missing information (such as a survey) might be requested from third parties.

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