



ICSC+LAW SYMPOSIUM OH/KY/IN/MI/PA
Hilton Columbus/Polaris, Columbus, OH
February 29 - March 1, 2024

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Hilton Columbus/Polaris
Columbus, OH
Friday, March 1, 2024
1:40 - 2:40 pm

**Session 3B: To Insure or Not Insure, That is the Question: Hot Issues in Insuring
Commercial Real Estate**

Moderator

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Panelists

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OUTLINE

To Insure or Not Insure, That is the Question: Hot Issues in Insuring Commercial Real Estate

This discussion will explore the latest title insurance coverage and underwriting issues in commercial real estate transactions with a comprehensive discussion among experienced practitioners from all sides of the transactions – national underwriter, buyer/borrower counsel, and commercial title agent – on what coverages to ask for and how to get them in the current environment.

- I. Hot Issue #1: Workouts and Other Changes Due to Financial Conditions
 - A. What properties are in play?
 - i. Office
 - ii. Big box retail
 - iii. Urban vs. suburban
 - B. What kinds of transactions are involved?
 - i. Deeds in lieu of foreclosure
 - ii. Foreclosure by private lenders
 - iii. Mortgage Modifications
 - iv. Redevelopment
 - v. Conversion from one use to one or more different uses

- II. Hot Issue #2: Cannabis Transactions
 - A. Types of transactions
 - i. Dispensaries
 - ii. Grow/processing facilities
 - iii. Distribution facilities
 - B. How do different underwriters view these transactions?
 - C. Handling the transaction funds?
 - D. Differences between states
 - E. Zoning endorsements
 - F. Cannabis Specific Exception

- III. Hot Issue #3: Mechanics Liens



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- A. What coverage is involved?
 - B. Tenant improvement issues
 - C. Sale before completion of improvements
 - D. What do underwriters need to insure?
- IV. Hot Issue #4: Creating and Selling Outparcels in Existing Retail Centers
- A. New Construction versus Stabilized Assets
 - B. Easements
 - i. Access/Parking
 - ii. Utilities
 - C. Timing Considerations
 - D. Non-Title Concerns
 - i. Use Restrictions
 - ii. Construction Restrictions
 - iii. Signage
 - E. Deal Structure
 - i. Condominium
 - ii. Ground Lease
- V. Practical Tips



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SESSION MATERIALS

- I. Hot Issue #1: Workouts and Other Changes Due to Financial Conditions
 - A. What properties are in play?
 1. Office. As work-from-home continues to be normalized, office tenants continue to reduce their footprint. For example, in Michigan:
 - a. “TD Auto Finance is slashing its real estate footprint as it plans to move its headquarters from Farmington Hills to Southfield. The auto lender is leasing about 35,000 square feet in the Two Town Square office mid-rise, replacing its 155,000 square feet in The Standard at Farmington Hills, at 27777 Inkster Road. That represents a 77.4% reduction in its office space.” – Crain’s Detroit Business, January 9, 2024
 - b. “Although there have been exceptions, many companies and organizations locally have downsized and/or consolidated. Those include Plante Moran, Deloitte LLP, Comerica Inc. and the Detroit Regional Chamber, just to name a few. Meridian Health's parent company, St. Louis-based Centene Corp., put over 300,000 square feet of prime downtown office space up for sublease last year.” – Crain’s Detroit Business, November 27, 2023
 2. Big box retail. As retail continues to be cannibalized by e-commerce, these locations have been repurposed. For example, in Michigan one anchor store at a regional shopping center has been repurposed into a 120,000 square foot gym. – Crain’s Detroit Business, November 3, 2023. These changes in use may lead to leasehold title policies.
 3. Urban vs. suburban. Neighborhood retail in downtown cores may be more greatly impacted than suburban uses, as the office market drives retail uses more greatly in those cores.
 - B. What kinds of transactions are involved?
 1. Deeds in lieu of foreclosure. Creditor’s counsel should consider obtaining a Commitment for an owner’s policy.
 2. Foreclosure by private lenders. Creditor’s counsel should consider obtaining a Foreclosure Guarantee and Commitment, which can be converted to an owner’s policy with a discount post-foreclosure.



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3. Mortgage modifications. Based upon the scheduled rate filings in a particular state, this may be a significant transactional cost.
4. Redevelopment. These transactions may involve splitting off outlots, conversion to a new use, or demolition and new construction. All of these have different potential title issues.
5. Conversion from one use to one or more different uses. As discussed in Hot Topic #4, these conversions may involve zoning issues, split/subdivision/condominium issues, and other title issues (cross-easements, etc.). As a result, a commercial title agent or title company/underwriter should be included in the discussion early in the process.

II. Hot Issue #2: Cannabis Transactions

A. Types of transactions

1. Dispensaries. These parcels are generally repurposed retail-use parcels. Because of the nature of the repurpose, users should consider requesting access endorsements, utility endorsements, and same-as-survey endorsements.
2. Grow/Processing facilities. These parcels are often repurposed or newly constructed light industrial parcels. Due to the nature of the use, users should consider requesting utility-access endorsements. Many large-scale growers operate both indoor (warehouse-style) and outdoor (secure farm-style) facilities. If the use is indoor, utility access is essential.
3. Distribution facilities. Although these facilities are sometimes integrated with grow and processing facilities, they can be separately located. Often, these are logistics/tech-flex facilities. Again, access and utilities are essential, so requesting these endorsements provides significant protection to the user.

B. How do different underwriters view these transactions? Because of the unique states of cannabis and federal law, most of the “family of companies” underwriters (First American, Fidelity, Old Republic, and Stewart) will not, or have, not insured cannabis parcels. The explanation for this is generally related to the integrated nature of those underwriters’ businesses, and the fact many of them also own federally-regulated financial institutions. There is a concern that handling cannabis transactions may introduce regulatory risk for affiliated financial entities.

C. Handling the transaction funds? For the same reason that many underwriters may not insure cannabis related parcels, many title insurance agencies will not handle, or are unable to handle, escrowed funds. It is important to clarify the agent’s ability and willingness prior to initiating a transaction. In order to handle escrowed funds, an agent



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generally must create a separate escrow account for all cannabis transactions at a state-chartered (rather than federally-chartered) financial institution.

- D. Differences between states. Obviously, because cannabis is legalized at a state level, rather than a federal level, it is critical to understand the legalization of cannabis in a specific state. For example, both recreational and medical cannabis are legal in Michigan under state law, subject to significant regulation. The regulatory situation in Ohio (as of the time of the drafting of these materials) remains in significant flux.
- E. Zoning endorsements. Currently, due to the nature of cannabis specific parcels, zoning endorsements are not available from underwriters.
- F. Cannabis Specific Exception

Example: “Without limiting, modifying, abridging or negating any provision of the Exclusions From Coverage stated in this Policy or any other exception included in this Schedule B, and as a supplement and addition thereto, this Policy does not insure or provide title insurance coverage directly or indirectly for or against any and all consequences and effects, legal, equitable, practical or otherwise, civil or criminal, of any violation or alleged violation of any United States federal, state, county, municipal or local laws, statutes, ordinances or regulations or any actual or threatened action, court order or mandate for the enforcement thereof, relating to or governing the use, processing, manufacture, growth, possession, distribution, sale or any other activity on, about, or relating to or concerning the land, title thereto or any interest therein, of any Schedule I drug as defined by the United States Controlled Substances Act, including, without limitation, marijuana and/or cannabis, and any component, derivative or product thereof. This Policy insures title only; nothing contained in this Policy shall be construed to insure the subject premises for any particular use.”

III. Hot Issue #3: Mechanics Liens

- A. What coverage is involved?
 - 1. All commitments, regardless of the jurisdiction, contain a standard exception for mechanics’ or materialmen liens that ties either specifically or generally to the mechanics’ lien statutes or issues in the state.
 - 2. There are three main types of coverage that are available to be considered.
 - a. Full coverage – Full coverage is given either with the deletion of the standard mechanics’ lien exception or with the deletion of the standard exception and raising a specific pending disbursement exception tied to the statutory authority in the jurisdiction.



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2. Who is responsible for the work being done?
 - a. Some jurisdictions allow for different underwriting standards when the tenant is fully responsible for the work being done. This means that there are no lease-related reimbursements or incentives for the work.
 - b. Does the state have any statutory protections or case law setting out who has the obligation to responsibility for liens?
- C. Sale before completion of improvements
 1. Who is responsible for the work post-closing?
 - a. If a buyer is assuming the responsibility of work done post-closing, there is a carve out in the policy for coverage suffered, created or assumed by the Insured. Title companies will generally not provide coverage over the acts or obligations of an Insured.
 2. What is the nature and scope of the work being done?
 3. Who is available to act as an indemnitor?
 - a. If a seller is obligated to complete construction post-closing, how are the parties dealing with these obligations? Are the parties entering into some form of escrow agreement?
 - b. Is the seller, or a parent, willing to act as an indemnitor?
- D. What do underwriters need to insure?
 1. Underwriters need to understand what is happening or what has happened to date?
 - a. Has work already commenced?
 - i. If so, do we have a way to limit the risk?
 - A. Notices of Commencement – Allow for the ability to set or rehabilitate priority of the Insured Mortgage.
 - B. Protections for purchase money debt or construction debt. What are the limitations of these protections?
 - b. What are the amounts involved?



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- c. Is there a creditworthy indemnitor?
 - i. Does the indemnitor make sense?
 - ii. Will the indemnitor be sticking around or have responsibility for work post-closing?
- d. Have any liens been filed to date?
- e. Are there lien waivers available for review?
 - i. Conditional lien waivers
 - ii. Unconditional lien waivers
 - iii. Documentation setting out subcontractors, materialmen or other parties with lien rights within the jurisdiction.
- f. Documentation underwriters ask to review:
 - i. Construction Contract
 - ii. Construction Loan Agreement/Loan Agreement
 - iii. Mortgage
 - iv. Budget/Sources and Uses
 - v. Draw Schedule
 - vi. Financials of a potential indemnitor

IV. Hot Issue #4: Creating and Selling Outparcels at Existing Retail Centers

Fact Pattern: A real estate developer owns an open-air shopping center and is looking to create value by selling off a portion of the shopping center and/or creating outparcels for development and sale.

- A. New Subdivision/Development versus Stabilized Assets
- B. Easements
 - 1. Access/Parking: Need to confirm that existing title documents provide sufficient access/parking easements to serve both the outparcel and the main shopping center. While the center may presently be accessible, need to ensure that outparcel and shopping center have continued access to and parking on each tract as applicable, once ownership is bifurcated.



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2. Utilities: To ensure that outparcel has access to utility easements and/or has ongoing right to modify existing utility lines in the event of a change in use or further development as contemplated. Impact on No Forced Removal Endorsement coverage in connection with utilities at Shopping Center.
 3. Signage: In the event that outparcel utilizes signage on the balance of the shopping center, or vice versa, there is a need to ensure that the parties can continue to maintain existing signage rights on a going forward basis.
- C. Timing Considerations: In the event of a new subdivision, there are a number of local factors at play that can elongate timing concerns.
1. Subdivision Process: Amount of time to finalize and complete subdivision process varies wildly amongst jurisdictions, with each jurisdiction having unique requirements.
 2. Tax Parcel: Even after subdivision is completed, it may be a significant period of time before the new subdivision has its own tax parcel. Parties will oftentimes need to prepare a tax sharing agreement to handle this gap, and will potentially be unable to obtain requested endorsement coverage.
- D. Comply with Existing Leases/Encumbrances: Given that the full “Shopping Center” as likely defined in each of the leases is no longer owned by one party after the sale of the outparcel, if the new Declaration is not properly prepared, there could be a gap between a tenant’s rights and what the owner is able to provide, potentially providing a smart tenant with a remedy/negotiating chip. Examples of these are as follows:
1. Use Restrictions: All Tenants need to ensure that the exclusive and prohibited uses that they bargained for in their leases will stay in place even if the Shopping Center ownership is bifurcated.
 2. Construction Restrictions: If there is a No Build Area, Protected Parking Area or requirements on construction (height, visibility, etc.), there is a need to make sure those would apply on a going forward basis.
 3. Consent Requirements: Oftentimes, tenants have the right to consent to a New Declaration or modification of an existing encumbrance (with such consent right often being limited to a situation where the New Declaration would have a material adverse effect). Parties need to ensure that they obtain any consents required, or at least have a clear understanding as to which tenants may allege a consent right.



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4. ROFR Rights: Need to analyze how a ROFR right applies to selling a portion of the real estate if applicable.

 - E. Deal Structure: In the event that a party is unable to quickly obtain a subdivision, or if there are certain characteristics that prohibit a subdivision from occurring, a party may attempt to put in place a condo regime or ground lease structures to achieve their stated business objectives.
 1. Condominium
 2. Ground Lease

 - F. Existing Financing – Partial Release: If the full Shopping Center is subject to one loan, the seller/land owner should work proactively with its lender on a partial release if the financing will stay in place from and after the sale of the outparcel.
- V. Practical Tips