Improving Economic Conditions and the Implications for Real Estate Litigation

The outlook for the real estate market is improving. Nationwide, rental rates for multifamily properties have gone up 3.5 percent and vacancy is down 120 basis points to 4.7 percent. Prices and sales volume have also gone up for commercial properties. In Southern California, the commercial real estate market is also improving with office and industrial vacancy rates decreasing and new commercial construction projects on the rise. In Los Angeles County, the vacancy rate for office space decreased to 16.7 percent in 2012 and the vacancy rate for industrial space decreased to 2.9 percent in 2012.

I learned about this positive economic outlook when I recently attended the 2013 Real Estate Law and Business Forum hosted by the University of Southern California Gould School of Law. This ten-year old event drew 1,500 real estate professionals and was a great opportunity to hear from leading real estate experts. In addition, the conference allowed me to learn from investors, real estate developers and urban planners about some of the trends that are likely to take place in the coming years. I came away from the conference with several insights about the current and future state of the real estate market here in Southern California.

Actions Seeking Specific Performance Will Increase

Does the improving real estate market mean that there will be fewer disputes and litigation? On the contrary, I believe that more disputes will arise concerning the sale and purchase of properties. With rising prices, sellers may be less willing to part with their properties than they would have five years ago. Buyers also may try to take advantage of the opportunities present in an improving market. Consequently, disputes may arise when a seller backs out of a real estate sales contract because another party is willing to pay more. In such a situation, the buyer's only option may be to sue for specific performance, which is a legal remedy that seeks a court order forcing the seller to sell their property.

Implications for Commercial Landlords and Tenants

Improving economic conditions may also have implications for commercial landlords and tenants in the rental market. Rising rents may mean that landlords who own commercial properties will want to maximize the profits they can obtain from their real estate holdings. The need to obtain the highest rent is magnified by the fact that commercial leases typically last for several years. Consequently, landlords who entered into leases during the economic downturn may try to seek ways to break their leases with their current tenants in order to take advantage of the rising rents by seeking out new tenants.

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Although conference attendees were bullish about the real estate market as a whole, the commercial mortgage backed securities (CMBS) market and the problems with default continue to persist. CMBS loans were created to provide commercial developments with financing through loans that could be repackaged and sold to investors as securities. Since the 1990s, the CMBS market has been an important source of financing for commercial properties. However, many of these loans are expected to mature in 2017. Consequently, a dark economic cloud is on the horizon and borrowers whose loans were packaged and sold on the CMBS market may want to approach their lenders as soon as they can and begin the negotiation process. This is especially true because refinancing may not be an available option for a lot of borrowers due to increased scrutiny by lenders. Additionally, under Civil Code Section 2924, California's non-judicial foreclosure laws allow lenders to come in and swiftly repossess distressed properties without court approval. This means that borrowers should seek assistance as soon as they can for a loan that has the potential for default.

If you have any questions or comments, I would be delighted to hear from you.

Law Office of Michael Chung
213.700.0198
mchung@lo-mc.com