Will This @#*!+#! Ground Lease Ever End?

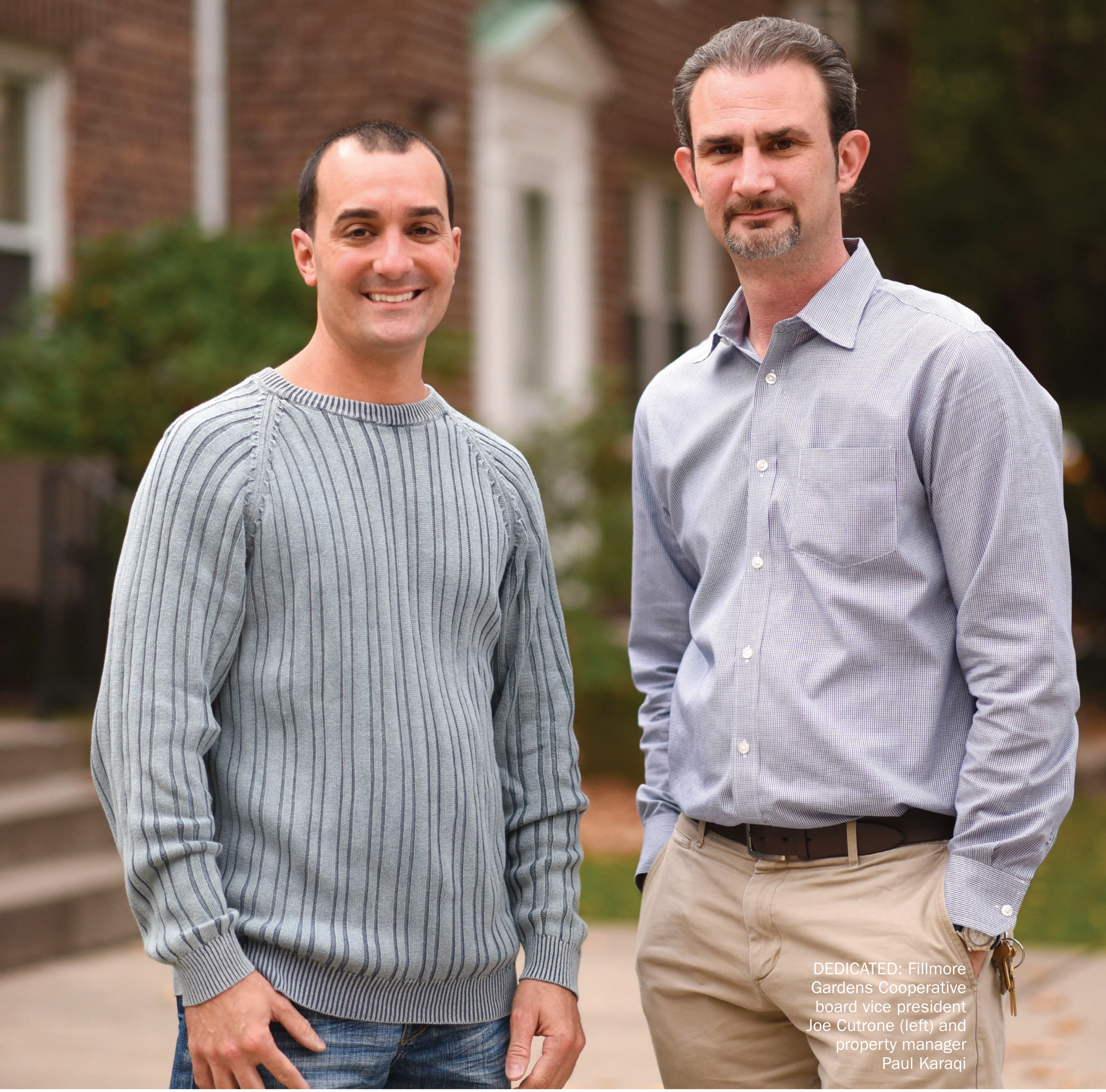
BY JENNIFER V. HUGHES
PHOTOS BY DANIELLE FINKELSTEIN

*a 100-year lease; 35 years to go; 100-year option to renew

No co-op or condo looks forward to a thorny set of legal problems, but in the case of one building, there was a silver lining inside the dark cloud of a slip-and-fall case: finding a way out of its ground lease.

Ground leases are a real estate mechanism where the condo or co-op corporation owns the building, but another entity owns the land underneath, renting it out for long terms, usually 90-plus years. At the Fillmore Gardens cooperative, previous boards of the 340-unit co-op had considered trying to buy their way out of the land lease, says property manager Paul Karaqi, an account executive at Century Management Services. "It was something that had been discussed from time to time," he says. "But it never happened."

The problem with land leases is this: say you have a 100-year lease for which the clock started ticking in 1950. As the lease ages, it can become a problem for those buying in. A potential buyer may intend to get a 30-year loan, but finds there are only 35 years left on the ground lease. Banks get skittish in situations as unstable as that, says attorney Robert J. Cecere, a partner at Daniels Norelli Cecere & Tavel, and it only gets worse as the lease expiration date gets closer. "Banks really start to question the land lease, and they stop lending to shareholders who buy into those buildings," he says.



DEDICATED: Fillmore Gardens Cooperative board vice president Joe Cutrone (left) and property manager Paul Karaqi

Skyrocketing Rent

Simple solution, right? The board should just go ahead and renew the lease. That doesn't always work out well, says David J. Lipson, senior managing director for Century's mortgage division. "The rent can skyrocket," he says. "I have one building on the Upper East Side where they had to raise their maintenance 40 percent to account for ground lease renegotiations. It's a wild card."

Or, says Cecere, the leaseholder can balk. "We represent another building in that same area where the landlord is not willing to negotiate with us," he says.

Back at the Brooklyn co-op, the 2013 slip-and-fall case seemed to be standard, says Cecere. But a problem arose when the ground leaseholder alleged that it was not being defended in the slip-and-fall litigation, and filed a federal claim seeking to have the land lease terminated. If the lease was voided in that fashion, Cecere says, it would have been a windfall for the leaseholder and a disaster for the co-op and shareholders.

"They would have become the property's owner because they would have owned any improvements on the land, and that means the buildings," Cecere says. The building essentially would have reverted to a rental.

The co-op contended, however, that the insurance carrier was at fault because it had neglected to initially cover the ground lease holder. The

FILLMORE GARDENS: a silver lining inside a slip-and-fall case.

carrier agreed, and it immediately defended both the co-op corporation and the leaseholder in the slip-and-fall case.

A Good Deal

But, the lease holder's federal complaint remained, and Cecere says they could have continued to press their case to terminate the lease. It was time to find a way out. The 100-year lease was in its 65th year, and there was another 100-year option to renew. The lease payments were about $3,000.

The two sides agreed on a price tag of $750,000. A $1 million mortgage was taken out on the property (with the added dollars to cover expenses) through a 10-year-fixed rate loan. Shareholders will be paying an added monthly assessment, which will amount to about $3,800 over the life of the loan.

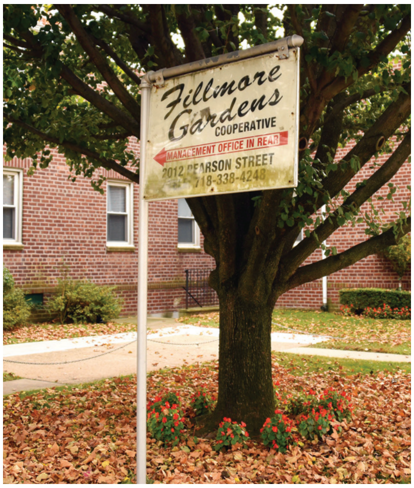
"We have a healthy reserve fund," says Karaqi. "But we do have a lot of capital work that needs to be done and we didn't want to risk depleting those reserves."

Cecere notes that it's never easy to take out a loan that size, but that both the co-op and the leaseholder got a good deal. The co-op no longer has to worry about the threat of the ground lease expiring, and the landowner got a healthy one-shot payment. While $750,000 is a bargain for a project that size in New York City, consider the fact that under its old lease, it would have taken 250 years to get that much in rent.

With every land purchase, you have to obtain title insurance, but the team says it took great care with this step. Title insurance means that research has been done to ensure no one else can claim ownership of the property. If someone does try to make a claim of ownership, the title insurance company would cover the claim so that shareholders don't lose their apartments. Cecere says they used both the bank's appraiser and their own expert to obtain title insurance, which was enough to cover all the cooperative's interests.

Buying the ground lease was "a huge relief," says board president Deborah Malafronte.

"Now we know we are secure in our homes," says Malafronte. "No one can ever come in and say 'You're out,' or 'You have to pay rent, or you lose your investment.'" Asked whether owning the land will make a difference in attracting new buyers into the building, Malafronte says,



"Absolutely, 100 percent."

Karaqi, the managing agent, says it's easy for boards to be complacent when they don't own their own land. "It's a long lease so it gives you a false sense of security," he says. "Plus, board members have their own personal outlook. They think, 'In 20 years I'll be out of here, so why worry?'" Malafronte observes that younger buyers have their own biases. "They think, 'Oh, I'm only going to stay 10 years so this won't affect me.'"

Karaqi concludes: "Even if there are no issues with your ground lease, you should bring up the conversation so you know where you stand." ■