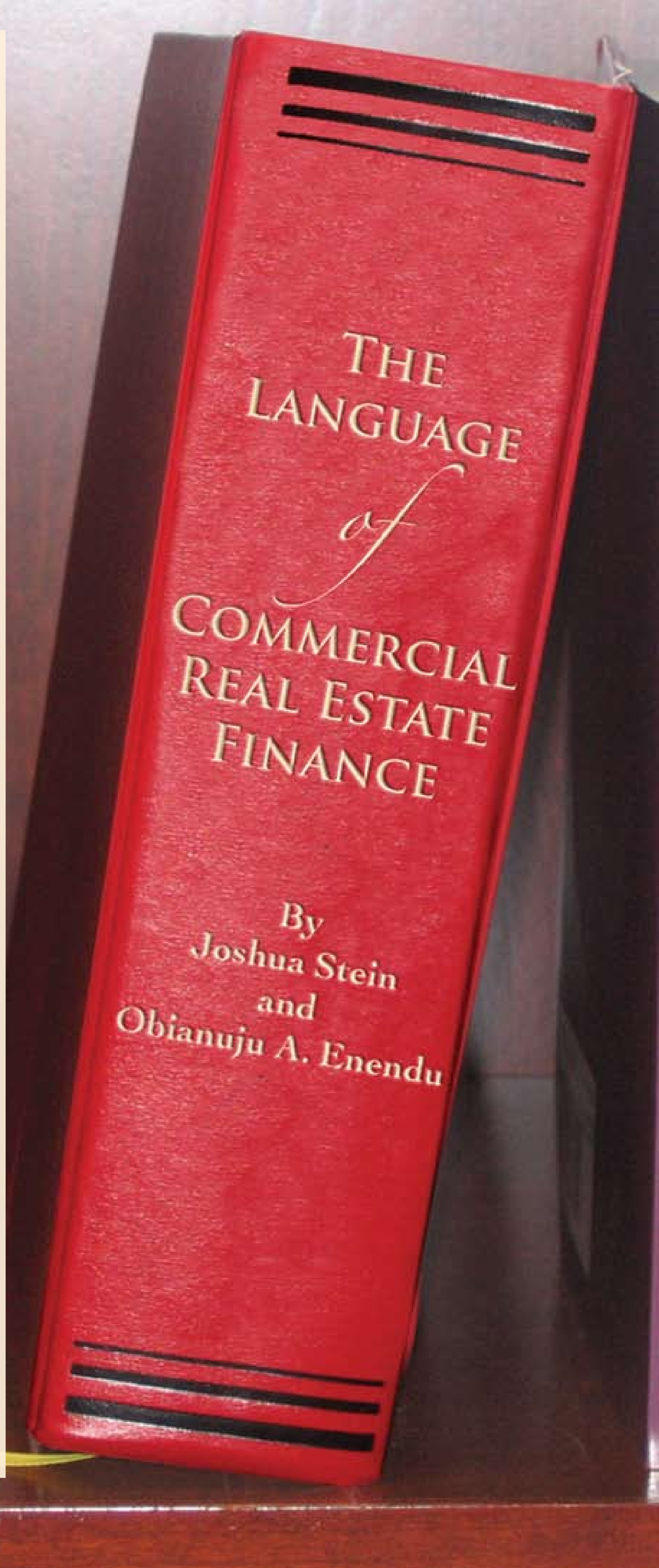

Rick Bright/Andrew O. Alcala

Commercial real estate finance boils down to three "main events": money, property, and transactions in which money gets turned into property or property gets turned into money. The industry has developed its own vocabulary for these events and all their various bits, pieces, and steps. Some of these words and phrases are just descriptive. Others are metaphors or slang that carry some cynicism and humor along with them. Some of these words are cynical and funny, with meanings that are not obvious to the uninformed ear. By fully understanding these words, one can begin to understand the thought processes and overall flavor of the entire commercial real estate finance industry and mindset.

Toward that end, the following lexicon collects words that are commonly and not so commonly used in commercial real estate transactions—primarily loans but also equity investment transactions and commercial leases. A few of these words sometimes have meanings in other areas of business. The authors offer no guarantee about this lexicon, except that it is incomplete and imperfect.

This lexicon limits itself to the areas listed in the last paragraph, ignoring two related industries that could offer fertile ground for additions to the list. First, until mid-2007, many newly originated commercial mortgage loans soon found their way into the "securitization" process, a mechanism developed by Wall Street that permits pools of mortgage loans to secure multiple tranches of bonds issued to investors. As that mechanism became ever more complex, its vocabulary grew accordingly. Given the dismal state of securitizations, the authors' primary areas of expertise, and length limitations, this lexicon disregards any phrases that come exclusively from that area of practice. Second, residential real estate finance has a far more extensive language than commercial real estate finance, but the authors of this lexicon handle only commercial transactions.

Words and phrases in this lexicon come mostly from two areas of commercial real estate finance. The first major source is the process of thinking about, structuring, negotiating, and closing commercial real estate loans. The second major source is the focus of most commercial real estate finance players right now: the process of dealing with troubled and defaulted loans and all the various permutations and elements that can arise in doing so.

The words in this lexicon rarely appear in legal documents, but they often arise in negotiations, meetings, and industry events. And now for the fun part: our definitions of commercial real estate finance terms.

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Amo:

Repayment of principal of a loan, other than a Balloon Payment or Bullet Payment, typically in recurring monthly installments or based on a formula.

Bad Boy Carve-out:

A risk or source of liability for which a borrower's principals may assume personal liability under a Carve-out Guaranty.

Baked:

Language that has been drafted into an agreement (e.g., a change in control provision) in anticipation of a future event. Variations: "half-baked" and "fully-baked."

Balloon Mortgage:

A mortgage whose Amo will not repay the entire principal balance by maturity, triggering the need for a Balloon Payment at that point.

Balloon Payment:

The payment due on maturity of a Balloon Mortgage, called a Balloon Payment because it is much bigger than the individual prior payments.

Bid-out:

A strategy in which multiple foreclosure bidders agree to let one of them acquire the collateral with a low bid, then resell it at a second auction just within the group, with the increase in price being split among the multiple bidders. Often a crime.

Big Box:

A large store operated by a major regional or national retailer, requiring substantial space but relatively little customization by the landlord. Sometimes (but not always) operated on a stand-alone basis, with little integration or interaction with other retail tenancies.

Boilerplate:

Terms and conditions in loan documents that are generic and rarely negotiated but which may become crucial in a meltdown of the loan or of the loan markets generally. Lenders often don't read the Boilerplate, instead assuming that the lawyers got paid to get it right.

Bow-Tie Loan:

Modification of an existing loan in distress, deferring interest that accrues above a pre-determined interest rate. A Bow-Tie Loan rolls any deferred interest into the loan principal.

Bridge Loan:

Short-term interim (allegedly) financing that provides the borrower with money until it arranges long-term financing (also known as a transitional loan). See also Hard Money Loan.

Brownfields:

Formerly contaminated real property, now remediated to a point at which it can be returned to commerce, subject perhaps to use restrictions.

Bucket:

A category of expenditure in a Waterfall. Can also mean any category of asset (e.g., hotels, office buildings, or apartment buildings) in a portfolio transaction.

Bullet Loan:

A loan with no Amo, in which borrower agrees to repay principal in a lump sum at maturity. Interest is generally payable monthly.

Bullet Payment:

Same as Balloon Payment.

Cap:

A Hedge to protect the borrower from the risk that a floating interest rate will float above a certain point, much like an insurance policy against high interest rates. Requires a one-time payment but imposes no other obligations on the beneficiary.

Cap Rate (or Capitalization Rate):

Annual net operating income divided by purchase price (or sometimes total investment or current fair market value), expressed as a percentage. For example, if a property cost $100 and its net operating income is $6, then the Cap Rate is 6%. Low Cap Rates imply high values, and vice versa.

Capital Stack:

The total structure of mortgage and other debt for a property, plus the equity investment made by the borrower and its principals. See also Debt Stack.

Carve-out Guaranty:

A guaranty of certain risks for which a lender refuses to look solely to the collateral. Also sometimes a contingent full guaranty of the loan, to discourage the borrower from doing certain bad things (e.g., a voluntary or collusive bankruptcy). These matters are all "carved out" from the otherwise nonrecourse nature of the loan, giving the lender access to the other assets of the guarantor(s). Of little value, unless signed by a Warm Body. See also Bad Boy Carve-out.

Cash Sweep (or Cash Trap):

Procedure in which any excess cash (beyond operating costs and debt service) goes into a lender-controlled account. Often activated by the borrower's failure to meet a financial test and accompanied by a Lockbox.

Chilling a Sale:

Actions taken at a foreclosure sale to suppress bidding, so a favored bidder can buy below market. See also Bid-out.

Class A:

A high quality category in a particular market, typically referring to office space. Trophy Buildings are of even higher quality.

Closing:

The event when the buyer pays the purchase price, the seller delivers the deed, the buyer gives the lender a mortgage, and the lender funds the loan. Sometimes a meeting of the parties; more often handled by a single party that receives the money and signed documents, then distributes them (an "escrow").

Club Deal:

A substantial commercial mortgage loan originated by a small group of lenders that often originate loans together and not widely offered to the marketplace of lenders. (In contrast, if a single bank originates a loan and then approaches a wide group of other institutions to try to

Sell Down the loan, this takes it out of the Club Deal category.)

Comfort Letter (or Cold Comfort Letter):
Hotel franchisor's letter to a lender, offering very limited comfort that the franchisor will notify the lender of future problems with the franchise and possibly issue a replacement franchise after foreclosure.

Cubing:
Estimating the cost of a Job by estimating the volume and quantities of materials the Job will require.

Cut-Off Notice:
A borrower's notice to a lender saying that any future discretionary loan advances will no longer have priority over debt secured by later recorded security devices (e.g., second mortgages), ostensibly to allow borrower to obtain more credit elsewhere. A law professor's fantasy with no application in the real world.

Debt Stack:
The total structure of mortgage and other debt for a property. Part of the Capital Stack; may include a Permanent Loan, Mezz Loans, and other financing.

Deep Pocket:
A person with extensive Liquidity.

Deep Pocket and Short Arms:
A person with extensive Liquidity who is also very good at not using it.

Developer's Fee:
A fee payable out of a construction loan to a developer, ostensibly to "keep the lights on" in the developer's office. Often one of the first line items removed from the budget of a construction loan.

Dialing for Dollars:
Looking for a lender and trying to negotiate the best deal.

Doctors and Dentists:
Many small investors in a real estate deal and potential plaintiffs if the deal goes bad. Often team up with lawyers who don't follow their own advice.

Draw:
A disbursement from a construction loan to pay for construction and other costs incurred to date on a Job.

Drop Shop:
A dry cleaner that does not actually do any dry cleaning on site.

Dry Closing:
A Closing in which everything is finished except the funding.

Dry Use:
Any use of retail real property other than the sale of prepared food.

Due Diligence:
Checking out an asset and a transaction—reviewing documents, inspecting, testing, and so on. Considered a quaint notion during overheated markets. As a practical matter, a purchaser's Due Diligence period also gives time to arrange its Capital Stack.

Due Diligence Out:
A purchaser's right to terminate an acquisition contract without cost during a Due Diligence period. A recent California case treats such a contract as illusory, *Steiner v. Thexton*, 77 Cal. Rptr. 3d 632 (Ct. App. 2008); one should expect to see option fees as the price of such contracts.

Equity Kicker:
A lender's right to receive a percentage of appreciation or ownership of the collateral.

Exit:
The end of a transaction, such as a buyer's successful sale of the property at a profit.

Exit Strategy:
A buyer's or a lender's plans for its Exit from a property or transaction.

Flag:
Brand name of a hotel or other lodging property.

Floater:
A loan that bears interest at a floating rate, typically for a term much shorter than a Permanent Loan, to enable a borrower to turn around, redevelop, or reposition a property and bring it to Stabilization. Typically requires little or no Amo except during a Mini-Perm period.

Flow Deal:
An understanding between a borrower and a lender, in which the lender agrees in principle to provide financing for a series of similar acquisitions that meet specified criteria, usually including some element of discretionary approval by the lender.

Go Dark:
A shutdown of operations by a Big Box or other major retail tenant, often without assigning the lease or subletting the space to another operator. This shutdown can potentially damage other tenants and, in the worst case, destroy an entire shopping center.

Go Hard:
A buyer's determination not to exercise a Due Diligence Out, and the expiration of buyer's deadline to do so. At this point, buyer will probably lose its deposit if it cannot close, but may litigate and ultimately settle by splitting the deposit.

Good Bones:
Solid structure and foundations of an old building (often unattractive) ready for renovation, as opposed to ready to be Scraped.

Greenfield:
A site where no improvements were previously built. A green field.

Hair:
Complexities, issues, and history about a particular property that create problems, delays, and extra legal fees for the Closing.

Haircut:
A reduction of the amount of a loan or the value of an equity investment for valuation or capital purposes.

Hard Costs:
Costs of construction that create additional value in real property

(e.g., bricks, mortar, architects, and engineers). Also includes contractor's overhead and profit.

Hard Lockbox:
A Lockbox that the lender fully establishes at Closing, with tenants being immediately directed to pay all rent to the Lockbox. Any disbursements from the Hard Lockbox require lender approval.

Hard Money Loan:
An expensive mortgage loan from a nontraditional lender, often obtained because of borrower distress or to meet financial requirements beyond the acquisition. Also employed to close an acquisition, with the idea that the borrower will replace the Hard Money Loan with a Permanent Loan at lower rates.

Hedge:
Any transaction to shift to a third party a risk of market fluctuations. In real estate, typically refers to mitigating the borrower's exposure to interest rate fluctuations by purchasing a Cap or entering into a Swap. Borrowers cannot yet enter into Hedge transactions to cover fluctuations in real estate values, but these may be around the corner, assuming continued development of the derivatives market.

Hedge Pledge:
A borrower's collateral assignment of a Hedge to mortgage lender, as additional collateral and to mitigate interest rate risks.

Holdback:
Funds retained from a contractor pending final completion of a Job or a particular category of work for a Job. Also funds retained by a lender pending completion of necessary repairs or further leasing.

Hope Certificate:
A subordinated position (created in a Workout) that may become valuable if the world changes in a more positive way than it has changed from mid-2007 to early 2009.

In the Money:
The status of a Hedge when the holder of the Hedge has the right to receive current payments from the other party, so that the Hedge can be sold at a positive selling price; that is, it has value.

Jingle Mail:
When a borrower mails the keys to the property back to the lender (an informal deed in lieu of foreclosure).

Job:
Any substantial construction project.

Key Money:
Amounts a tenant pays up front to obtain a new lease or purchase an existing lease. The amount of the Key Money depends on leasing market conditions.

Kick-out:
A right of a party to terminate an agreement, such as a tenant's or landlord's right to terminate a lease based on insufficient percentage rent, or a hotel owner's right to terminate a management agreement based on poor performance. Also, a purchaser's right to exclude certain properties or loans from a multi-property or multi-loan acquisition.

Land Man:
An expert on oil, gas, and mineral titles and transactions.

Lead Lender:
The lender that originates and administers a multiple-lender syndicated loan.

Leakage:
In a partial release formula for a portfolio loan, the ability of the borrower to receive some cash from property sales before the loan has been fully repaid.

Lease-up:
The process of finding "first tenants" for a new or substantially renovated or repositioned building.

Liquidity:
Cash or immediately marketable securities.

Loan to Own:
A Hard Money Loan or Mezz Loan in which the lender's business motivation may consist not so much of being repaid as of acquiring the collateral through foreclosure.

Lockbox:
An arrangement by which property income goes directly to a particular bank account (subject to a lender security interest) to be applied in accordance with a Waterfall. Formally called cash management. Subspecies include Hard Lockbox, Soft Lockbox, and Springing Lockbox, whose definitions can vary (although this lexicon seeks to capture some common definitions).

Lock-in Period (or Lock-out Period):
A period during which a loan prohibits Amo beyond regularly scheduled principal payments, if any.

MAI:
An appraiser who is a "Member, Appraisal Institute," which requires certain training, testing, experience, and adherence to standards. Can also mean "Made as Instructed," referring to an appraisal.

Mandate Letter:
An agreement between a borrower and a Lead Lender by which the borrower authorizes the Lead Lender to seek to arrange and syndicate a loan.

Marry Up:
A lender's sale of an REO property by packaging it with some other property to increase the appeal to buyers.

Mezz Loan (or Mezzanine Loan):
Additional financing secured by a pledge of equity interests in the borrower or by the borrower's issuance of preferred equity interests much like preferred stock. Often used as an alternative to a second mortgage loan.

Mini-Perm:
Short-term extension of a construction loan, after the borrower has completed construction, to give the borrower a year or two to achieve Stabilization.

Mod:

Modification of an existing loan agreement.

Motor:

The person who ultimately makes a real estate company, development, or project go forward. Just as a car has only one motor, usually so too does a real estate company, development, or project.

Neutron Loan:

A loan that destroys the borrower by forcing a sale of the property, while leaving the property itself intact.

NIMBY:

"Not in my backyard." Shorthand summary of almost all the usual arguments mounted against any Job. Related to BANANA ("Build Absolutely Nothing Anywhere Near Anything").

No-Cut Management Agreement:

A management agreement that a hotel owner has virtually no hope of ever terminating before its scheduled expiration.

Out Years:

Any years in the distant future during the life of a property or a lease.

Overrun (or Cost Overrun):

Amount by which the actual cost exceeds the originally budgeted, estimated, or targeted cost of a Job.

Pairings:

A Single-purpose Entity and another identified entity higher in the borrower's organizational chart. Rating agencies fear that if the latter entity files bankruptcy, the Single-purpose Entity might be dragged into it. This leads to requirements for "nonconsolidation" opinions for each Pairing.

Permanent Loan:

Long-term (more than five year) financing for real property that has achieved Stabilization. Typically requires monthly Amo and contemplates a fixed rate of interest (matching the borrower's relatively fixed income stream).

Piece:

Any parcel of real property.

Proceeds:

Total dollars the borrower receives from a loan at closing. During periods of easy credit, lenders compete to give "maximum proceeds" to desired borrowers.

REO:

"Real Estate Owned" or "Other Real Estate Owned"—a category of assets on a bank's balance sheet, reserved for real estate that the bank has acquired through foreclosure or a deed in lieu of foreclosure.

Repo:

A "repurchase" transaction, in which the originator of a loan "sells" that loan to a "purchaser" and commits to "repurchase" it, typically 364 days later. This method of financing loans may give the "purchaser" a better position in bankruptcy than if the originator merely pledged the loan to the "purchaser."

Scrape:

Demolish existing buildings and clear the site in preparation for a Job.

Second-Owner Project:

A Job in which the initial developer will never make any money. Instead, the lender will need to foreclose and resell at a lower price to the next owner, who might make money.

See-Through Building:

A finished building that does not yet have any tenant improvements or occupants and is typically in distress (or about to be). Popularized in the 1980s by Texas developers that had friendly S&L lenders.

Sell Down:

Process by which a Lead Lender sells to a syndicate of lenders' interests in a previously originated loan.

Shill:

A fake bidder at an auction, whose role is simply to increase the bids, with an understanding that the seller won't really require the Shill to buy if the Shill is the highest bidder.

Shotgun:

A process through which one joint venturer can force a buyout by naming a price for all the assets of the joint venture. The other venturer must then either buy out the initiator, or sell to the initiator, at a price based on the distributions that the joint venture would make if it sold all its assets for the stated price.

Silent Partner:

A financial investor in a borrower, typically with very limited rights to approve certain major transactions and no right to control day-to-day management. Often not publicly identified, so that developer can portray itself as owner of the Job.

Single Purpose Entity:

A newly formed entity whose sole purpose in life is to own and operate particular collateral. The rating agencies established elaborate rules for these entities (e.g., cannot share letterhead or telephone number with any other entity).

Sizing:

Lender's determination of the final loan Proceeds.

Snatch Dirt:

Resolution of a defaulted loan by which the collateral is transferred to the lender, often through a bankruptcy.

Snorkeling:

Negotiating, structuring, and closing transactions that relate to mortgages that are Under Water.

Soft Costs:

Marketing, administrative costs, professional fees, real estate taxes, insurance, and purchases of personal property not directly associated with creating a structure but incurred during construction of a Job.

Soft Lockbox:

A Lockbox that the parties establish at Closing, initially allowing the borrower to withdraw funds without lender permission or control. The lender can block those withdrawals if the property later fails certain financial tests.

Springing Lockbox:

A Lockbox to be established or activated in the future if certain events occur.

Stabilization:

The point when a Job is no longer a speculative development or acquisition and instead has become income-producing real estate, by achieving a certain state of physical completion, Lease-up, and net income.

Stalking Horse:

A buyer whose contract will be used to entice other buyers, with whom the seller is more likely to actually close a transaction. Creates a floor for future bidding.

Sticks and Bricks Takeout:

A Takeout conditioned only on finishing construction, with no requirement for Lease-up or Stabilization.

Story Property:

Collateral for a loan that requires significant explanation and optimism to justify the transaction.

Swap:

An agreement in which a borrower (typically under a floating rate loan) agrees to pay a fixed rate, and a counterparty agrees in exchange to cover the borrower's floating rate loan payments. Because early termination of a Swap can create substantial liability for a borrower (e.g., if rates have dropped), lenders disfavor Swaps. Borrowers like them because they require no up-front payment.

Sweat Equity:

The equity value in a property that is earned by a developer who increases its worth through the developer's intangible efforts, such as by obtaining zoning or planning consent, negotiating option rights, producing schematic drawings for a potential form of development, or negotiating terms for a pre-leasing. The developer may convert its Sweat Equity into a share in the future value of the completed development.

Sweetener:

An inducement to someone to enter into a contract or to make a loan (e.g., an Equity Kicker).

Takeout:

A commitment to provide a Permanent Loan for a Job (i.e., refinance the construction loan) after completion of construction and, in most cases, Lease-up and Stabilization.

Taxpayer:

An outdated building (typically less than the maximum development allowed on the site) expected to throw off only enough net operating income for its owner to pay real estate taxes.

Temporary Liquidity Problem:

Common explanation for financial stresses that precede a default.

Tillie Feldman:

A noncreditworthy person, who held real property only long enough to place a mortgage on it, then reconveyed it (subject to the mortgage) to the real owner (who did not assume the mortgage). An early substitute for nonrecourse financing in New York.

Top Out:

To complete the steel frame structure and roof deck for a new building under construction.

Trailing 12:

A 12-month period during which a lender will test the net operating income of a project.

Tranche:

A "slice" of a loan having a particular priority for application of foreclosure sale proceeds. "Higher" Tranches have lower risk and lower interest rates than "lower" Tranches.

Trophy Building:

A building, typically a central business district office building, that attracts the highest rent and delivers visibility and cachet for its owner above and beyond "ordinary" buildings, or even mere Class A buildings, of the same type.

Under Water:

A loan whose amount exceeds the value of its collateral.

Value Engineering:

Modifying the plans, specifications, schedule, logistics, and sequencing of a Job to try to reduce its cost.

Vanilla Box:

A shell interior of rentable space, with landlord-installed utilities, subfloor, and finished but unpainted drywall.

Walk Away Rights:

A party's rights to unilaterally terminate a transaction, such as a buyer's rights under a Due Diligence Out.

Warehouse:

A revolving loan under which a mortgage lender borrows money to originate mortgages and then holds them on a short-term basis, pending securitization. Often structured as a Repo.

Warm Body:

A creditworthy individual, as opposed to a borrower-related entity that might sign a guaranty but has no real assets. See also Deep Pocket.

Waterfall:

The priorities for application of cash, such as in a Lockbox.

Way Out in Front of One's Skis:

Taking positions, raising issues, or expressing views that are premature or poorly thought through.

Wet Closing:

A Closing that is not a Dry Closing. At a Wet Closing, the parties not only sign documents but also fund the Capital Stack.

Workout:

The negotiated resolution of a troubled loan, typically but not necessarily allowing the borrower to retain the collateral, subject to the debt, for some period.

Yank a Bank:

A clause in a loan agreement allowing Lead Lender to buy out the interest of a syndicate member who does not behave. ■