

THE DUE DILIGENCE WINDOW SHRINKS IN COMMERCIAL REAL ESTATE PURCHASES

Arnon Wiener, Esq., CEO, Real Diligence

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The revival of the real estate market is presenting new opportunities for commercial real estate owners and investors across the U.S.. Improved lending conditions and the increase of capital availability are driving market growth on its forward momentum. After hunkering down to wait out the storm of the recession, the commercial real estate market is resurging with an influx of deals.

This is good news for real estate owners and investors. However there is a consequence to the increasing demand for properties: fierce competition. While competition is beneficial to the marketplace, investors should be aware of a secondary effect which may have a negative repercussion on the decision making process; namely the shrinking due diligence window.

Due diligence is the research conducted ahead of purchasing a property. In real estate, the due diligence process should include a thorough review of the financial history and cash flow projection for the property. The buyer should analyze all the financial information which is pertinent to the property, including historical financial statements, projected budget income, reimbursable income and methodology, operating expenses, taxes, insurance and more.

Conducting a comprehensive due diligence review takes time. The perspective buyer needs to carry out a thorough and accurate assessment in order to determine the financial and physical state of the property.

The due diligence period usually begins when the prospective purchaser has made an offer that the seller has accepted. The buyer then places a down payment in an escrow account to be applied towards the purchase. Once the due diligence deadline has passed, the deal goes hard.

Both parties in the transaction want it to move along at a reasonable pace. It used to be that typical due diligence periods ranged from 40 to 45 to 60 days. This was considered a practical amount of time to make an informed decision.

However, because of the increasing competition, due diligence time periods are shrinking significantly. Buyers are now being offered a due diligence window as small as 28 or even 21 days. Tighter due diligence windows of three or four weeks can pose a risk to investors.

With the pressure of a tight deadline, investors may be tempted to rush through the due diligence process in order to snap up a property. There is no denying the importance of speedy and assertive decision making when purchasing real estate. At the same time, it is as essential to have the knowledge to make a decision that is not just quick- but correct as well.

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Buyers are now positioned between a rock and hard place, in which they are pressured to meet the impending due diligence deadline, while still conducting thorough research of the potential property. The increased strain on the buyer may put him or her at risk to make hasty decisions, and then repent at leisure.

Despite the shrinking window of stipulated due diligence periods, real estate owners and investors should still remain conscious of the need to make informed and measured decisions.

ABOUT THE AUTHOR

Arnon Wiener, Esq. is Chief Executive Officer for LeaseProbe, LLC and Real Diligence, LLC., which specialize in commercial real estate lease abstracting and sophisticated real estate financial due diligence reviews and valuation modeling. Mr. Wiener earned his JD from Georgetown University Law Center in 1999, where he was a recipient of the Nordlinger Behrend Scholarship Award for academic achievement. In 1999, Mr. Wiener was admitted to the Maryland State Bar, as well as the United States District Court for the District of Maryland Bar. He also served as a judicial law clerk for the 5th District, Circuit Court of Maryland. After clerking, Mr. Wiener worked as an attorney at the law firms Venable, LLP, and Blades and Rosenfeld, P.A. His areas of practice included complex construction, real estate and commercial litigation.

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For more information, contact:



Carlos Alvarez
Regional Business Director
Madison Commercial Real Estate Services
calvarez@madisoncres.com
(646) 765-7741

www.madisoncres.com



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