

REALESTATE & THE LAW

Fall 1996
Volume VI
Number 2

In This Issue:

*BOMA Releases New
Standard For
Measuring Office
Floor Area* 1

*Wetlands Mitigation:
Can You Bank On It?* 1

*Previous Violent
Crimes May Make
Property Owners
Responsible For
Future Violent Acts
of Third Parties* 2

*Rent Insurance:
Avoiding Financial
Loss When Casualty
Occurs* 2

*Consider Endangered
Species in Connection
With Your
Development Plans* 3

Recent Decisions 4

BOMA RELEASES NEW STANDARD FOR MEASURING OFFICE FLOOR AREA

The Building Owners and Managers Association (BOMA) has recently adopted a new standard for measuring floor areas in office buildings. The standard, *ANSI/BOMA 65.1-1996*, includes a common method for completing a building-wide measurement of office space. The first major update of the standard in 16 years will allow traditional "building amenity" types of common areas (such as a large common lobby on one floor), which benefit all tenants, to be allocated to all floors, on a pro-rata basis.

The new standard also includes a variety of new definitions, to be used in helping to understand the new standard. Among the newly defined terms, which include illustrations of the concepts, are "Building Common Area," "Floor Common Area," "Floor Rentable Area" and "Floor Usable Area."

The new standard also provides detailed examples of how to assess and measure "common area" types of amenities, such as vending areas, loading docks, security stations, exercise clubs and restaurants, and how to convert building usable areas to rentable areas. While there is no requirement or law that this new standard be used to measure office areas, tenants and landlords will look to these standards to resolve the vexing questions of what areas are fairly charged as "rentable" to a tenant.

Copies of the new standard cost \$25 for members of BOMA or \$35 for non-members, and can be obtained from:

BOMA
Suite 2830
6855 Jimmy Carter Boulevard
Norcross, Georgia 30071
(770-825-0116)

WETLANDS MITIGATION: CAN YOU BANK ON IT?

The United States Army Corps of Engineers has issued wetlands guidelines which permit the use of Mitigation Banks. *Banking Guidance*, 60 Fed. Reg. 58, 605 (Nov. 28, 1995). Under Section 404 of the Clean Water Act, the Corps can issue permits for the dredging and filling of wetlands. These permits require that developers avoid wetland damage and where damage is unavoidable, provide "compensatory mitigation" by enhancing, restoring or creating replacement wetlands. Wetlands "creation" consists of developing a wetland where one did not previously exist, or restoring certain areas of damaged wetlands.

Under the new guidelines, developers may be able to meet their compensatory mitigation requirements by purchasing a "credit" from a Mitigation Bank based on the enhanced, restored or created wetland held by that Mitigation Bank. A few Mitigation Banks are already operating in Georgia, Florida and several other states.

Whether Mitigation Banks will provide a long-term solution to loss of wetlands is uncertain for a number of reasons, including:

- A goal of "no-net loss" of wetlands may require that replacement wetlands be equivalent in size, quality, function and location to the wetlands being destroyed. Environmental groups may challenge any time delay between when the new ecosystem becomes functional and when project site wetlands are destroyed. Even a perfectly constructed Mitigation Bank may not provide replacement habitat for wildlife displaced by a development a hundred miles away, nor would wildlife be likely to use ten discrete mitigation wetlands separated by urban development.

(Continued on page 2)

(Wetlands Mitigation..., continued from page 1)

Real Estate & The Law is a quarterly publication of the Real Estate Group of Troutman Sanders LLP, providing up-to-date information on recent legal developments affecting real estate and general insights into related areas of interest. *Real Estate & The Law* is a free service to clients and is not designed to render legal advice or legal opinion. Such advice may only be given when related to actual fact situations.

Readers are encouraged to reproduce articles for educational purposes. In doing so, credit must be given to Troutman Sanders LLP and *Real Estate & The Law*. Please advise our editor of all reprints.

Troutman Sanders LLP
NationsBank Plaza
600 Peachtree Street, NE
Suite 5200
Atlanta, Georgia
30308-2216
Telephone: 404-885-3000
Facsimile: 404-885-3900

999 Peachtree Street, NE
Suite 750
Atlanta, Georgia
30309-3964
Telephone: 404-885-3651
Facsimile: 404-885-3652

1300 I Street, NW
Suite 500 East
Washington, D.C. 20005
Telephone: 202-274-2950
Facsimile: 202-274-2994

Editor:
Jeffrey F. Hetsko

- Because the replacement wetlands must be the functional equivalent of the wetlands being destroyed, the characteristics of the existing wetlands will need to be delineated with particularity in order for the developer and the Corps to determine which Mitigation Bank, if any, can provide the functional equivalent of the existing wetlands.
- There are no guarantees that the created or banked wetlands will survive and continue to provide the functional equivalent of the destroyed wetlands. What happens if the Mitigation Bank fails? What obligations, if any, will the developer have after purchasing a credit from the Mitigation Bank and constructing its development on the destroyed wetlands? Will the developer be subject to sanctions if the Mitigation Bank, for whatever reason, should fail? At a minimum, the land in the Mitigation Bank should be encumbered by permanent conservation easements in favor of some public agency or non-profit conservation organization.

Even with these and other potential problems, wetlands mitigation banking may prove to be a superior solution for destroyed wetlands than current on-site mitigation. The scattered nature and sheer volume of on-site mitigation projects represent difficult oversight problems for the Corps, whereas large Mitigation Banks could more easily be monitored. Mitigation Banks also provide the potential of consolidating resources to ensure better planning and technologically more advanced resources and facilities, thus ensuring longer-term viability of the mitigation areas. Also, as guidelines are developed for the design and monitoring of wetlands Mitigation Banks, these facilities could provide far superior unified habitat than the fragmented habitat otherwise provided by hundreds of individual on-site mitigation projects.

PREVIOUS VIOLENT CRIMES MAY MAKE PROPERTY OWNERS RESPONSIBLE FOR FUTURE VIOLENT ACTS OF THIRD PARTIES

In Georgia, the owner of real property may be liable to a person injured in a common area if the owner negligently fails to prevent the injury. In certain circumstances, negligent failure to prevent injury includes the failure of the owner to take action based on prior violent occurrences in the common area.

The Georgia Court of Appeals recently held that the rape of a tenant in the underground parking deck was not foreseeable even though the tenant presented evidence of nine thefts and three acts of vandalism in the prior twelve month period. In *Doe v. Prudential-Bache/A.G. Spanos Realty Partners*, the Court of Appeals distinguished between crimes against property and crimes against people. Thus, even though prior crimes against property had occurred in the parking deck, these did not mean the owner should have anticipated and protected against the possibility of a rape.

However, where there is evidence that the owner knew of prior violent crimes against persons, the owner may be liable. For instance, in *Shoney's Inc. v. Hudson* (1995), a restaurant owner was held liable for an attack in the restaurant's parking lot because three prior acts of violence against employees had recently occurred there.

The extent of an owner's knowledge of substantially similar crimes is also important. In a 1991 decision, the Georgia Supreme Court found that Savannah College of Art & Design was not liable for a sexual assault that took place in a college dormitory because previous crimes occurring in the dormitory were not so substantially similar as to alert the College to the risk of sexual assault.

Several other factors can also provide evidence of the owner's negligence. The Georgia Court of Appeals has held that where employees (i) have classified a parking area as unsafe, (ii) have asked for a parking area security guard, and (iii) have always escorted the female employees to their cars, the owner may be held liable for injury to persons by violent crimes. The Court of Appeals has also found the owner liable for violent crimes where the premises are located in a high crime area.

RENT INSURANCE: AVOIDING FINANCIAL LOSS WHEN CASUALTY OCCURS

Rent insurance, which is often overlooked in lease drafting and negotiations, can be used to avoid significant financial loss to either the landlord or the tenant in the event of damage or destruction of the premises. The interests of both the landlord and the tenant are well served by coordinating the abatement and rebuilding provisions in the lease with the use of rent insurance.

There are three basic types of rent insurance.

- *Business interruption insurance.* When a lease does not provide for rent abatement if a casualty occurs, the tenant should carry business interruption insurance. This protects the tenant against loss of earnings if the building is destroyed or damaged from a fire or other insured peril, allowing the tenant to cover its lease obligations when it cannot conduct its business because the premises have been rendered untenable.
- *Rental income insurance.* When a lease provides for rent abatement if a casualty occurs, the building owner should carry rental income insurance. This covers a landlord for the loss of rental revenues in the event the building is damaged or destroyed to the point that one or more tenants cannot use their premises and therefore are excused from paying rent.
- *Rental value insurance.* This protects a building owner who is also an occupant of the building against the loss of value of its occupancy resulting from an insured peril.

Whether the lease provides for rent abatement, and thus which party takes out rent insurance, is one part of the overall economics of the transaction. The negotiations on this point may be driven by the terms of the mortgage, which may require that the landlord carry such insurance. In such situations the tenant may be in a position to insist that its rent be abated. In addition, if the tenant is small, it may be to the landlord's advantage to allow abatement. The landlord can obtain rent insurance and pass the cost of the insurance through to the tenants. Otherwise the landlord should make sure that the tenant has rent insurance coverage so that the tenant can continue to pay its rent in the event of damage or destruction to the premises.

On average, rent insurance costs between \$.60 and \$1.00 per \$1,000 of coverage for a one year period. The duration of coverage should coincide with the calculated period of reconstruction or repair plus a few months contingency. There are several other factors to consider in purchasing rent insurance. In leases where the tenant pays base rent plus additional rent consisting of pass throughs of a proportionate share of real estate taxes, insurance and common area charges, the party carrying the insurance, whether it is the landlord or the tenant, should be sure to insure for the additional rent in addition to the base rent. Otherwise, the insured party will be underinsured.

The parties should also be careful to avoid gaps in coverage. In some cases the lease allows for rent abatement for loss of use other than resulting from casualty (e.g., when access or services are unavailable

to the tenant). Rent insurance often does not cover rent abatement for loss of use because no insured peril has physically damaged the property. The landlord should consider purchasing an endorsement to cover this circumstance. Similarly, the tenant may have a gap in coverage where rent abatement may not begin for several days or weeks following a given event, such as elevator failure or lack of running water. Careful attention to the terms of the business interruption insurance can avoid losses in such circumstances.

CONSIDER ENDANGERED SPECIES IN CONNECTION WITH YOUR DEVELOPMENT PLANS

The Endangered Species Act (ESA) encompasses various protections designed to safeguard species from extinction. Under Sections 7 and 9 of the ESA, no person may take any species listed as endangered or threatened. The ESA broadly defines "taking" as any act that would kill, harm or harass a species. The Code of Federal Regulations further defines "harm" as including significant habitat modification or degradation that actually kills or injures wildlife. Since development activities may constitute a taking of an endangered species, developers should understand the scope of private takings under the ESA and attempt to structure their projects so as to minimize adverse impacts on listed species and their critical habitat.

Last summer, the United States Supreme Court focused its attention on Section 9 of the ESA and provided some guidance for those involved in real estate development. In *Babbitt v. Sweet Home Chapter of Communities for a Great Oregon*, the Supreme Court clarified what types of actions constitute a "taking" under Section 9. Specifically, the Court held that habitat modification constitutes the harming of species protected by the ESA. The small landowners and logging companies who brought the *Babbitt* suit unsuccessfully argued that the application of such a broad "harm" regulation to the extensive habitat of the northern spotted owl and the red-cockaded woodpecker had economically injured them.

As a result of *Babbitt*, the ESA will have a greater impact on all types of land development where listed species or their critical habitats are located. This impact can be mitigated by using endangered species investigations and reviews. Consultants can conduct walking field inspections of the property, research potential endangered species and work with the appropriate agencies to relocate species or modify the project.

Real Estate Group:

*James W. Addison
Maureen T. Callahan
Lexie L. Craven
Mark L. Elliott
Robert d. Fortson
Larry E. Gramlich
John W. Griffin
Jeffrey F. Hetsko
Tracey I. Holmes
James H. Keaten
Diane L. Lidz
Rosemarie McConnell
John W. Moore
Richard A. Newton
Wendy W. Silliman
Joseph R. White, Jr.
A. Michelle Willis*

(Continued on page 4)

(Consider Endangered Species..., continued from page 3)

In addition to this Review, Troutman Sanders LLP also publishes six other newsletters:

Business & The Law addresses the needs of publicly and privately held companies and seeks to provide items of interest to owners and executives of these companies.

Employment & The Law details current issues in labor, compensation, ERISA and tax that impact the relationship between employers and employees.

Environment & The Law tracks developing trends in environmental law, including air and water quality and hazardous substances.

Intellectual Property & The Law covers current issues in intellectual property/high tech areas, including copyrights, trademarks, patents, trade secrets, employment agreements and tax issues applicable to the development of technology.

International Business & The Law details current issues that impact international business transactions, trade in merchandise and services, and international investment opportunities.

Lending & The Law details current issues that arise in the commercial loan industry.

Please contact Yolanda Head at 404-885-3639 if you would like to receive any of these publications.

Copyright © 1996
Troutman Sanders LLP

In those instances where a developer cannot avoid adversely impacting listed species or their habitat, the developer may apply for an "incidental take" permit from the Department of the Interior pursuant to Section 10 of the ESA. Increasingly, developers are relying on Section 10 permits as an alternative to abandoning a project because of ESA restrictions. Section 10 requires that an applicant: (1) provide evidence that the taking will be "incidental"; (2) minimize the impact of the taking; (3) develop and fund a habitat conservation plan; and (4) prove that the taking will not appreciably reduce the likelihood of the survival of the applicable species. Developers and private landowners alike must weigh the disadvantages of the delay and expense inherent in the Section 10 process against the advantages of continuing with their projects.

RECENT DECISIONS

Waivers of Subrogation Not Against Public Policy

A waiver of subrogation typically provides that, to the extent of any applicable insurance, a landlord and a tenant will look to the insurance company and will not sue each other for loss or damage allegedly attributable to the negligence of the other party. This provides a method for shifting the risk of loss to the insurer.

In *May Dept. Store v. Center Developers Inc.*, 266 Ga. 806 (1996), several tenants and the insurance companies of several tenants sought to sue the landlord and a neon sign company for damage due to fires allegedly caused by the neon signs. The leases all contained provisions waiving rights of recovery by each party against the other.

The tenants and insurers argued that Section 13-8-2 of the Official Code of Georgia made the waivers unenforceable. That section provides that an agreement in connection with or collateral to a contract concerning the construction, repair or maintenance of a building "purporting to indemnify or hold harmless the promisee against liability for damages arising out of ... damage to property caused by or resulting from the sole negligence of the promisee, his agents or indemnitees is against public policy and is void and unenforceable...."

The Georgia Supreme Court rejected the argument and held that a subrogation clause was an unequivocal expression of "the mutual intent of landlord and tenant to shift the risk of loss and to look solely to insurance coverage for loss or damages incurred by either party." The express language of Section 13-8-2 only prohibits hold harmless or indemnity clauses. Thus, according to the Court, Section 13-8-2 does not prohibit subrogation waivers in lease agreements.

Discount Received by Co-Lender upon Purchase of Loan from Other Co-Lender Does Not Render Loan Usurious

Cobb Federal Savings Bank loaned money to Westover to develop a subdivision. Shortly thereafter, United Federal Savings and Loan purchased a 15% interest in the Cobb Federal loan. When the loan was renewed in a year, Cobb Federal sold a 30% interest to First Alliance Bank.

Cobb Federal subsequently experienced financial difficulties, with RTC being appointed receiver. First Alliance then purchased the interests in the loan of Cobb Federal and United Federal at a 25% discount. A modification and renewal of the loan was entered into by First Alliance and the borrower, and the loan was ultimately paid in full by the borrower.

In *First Alliance v. Westover, Inc.* (Ga. 1996), the borrower claimed that the 25% discount received by First Alliance should be used to calculate the interest rate paid by the borrower for purposes of Georgia's usury statute on the modification and renewal of the loan. This would have rendered the loan usurious.

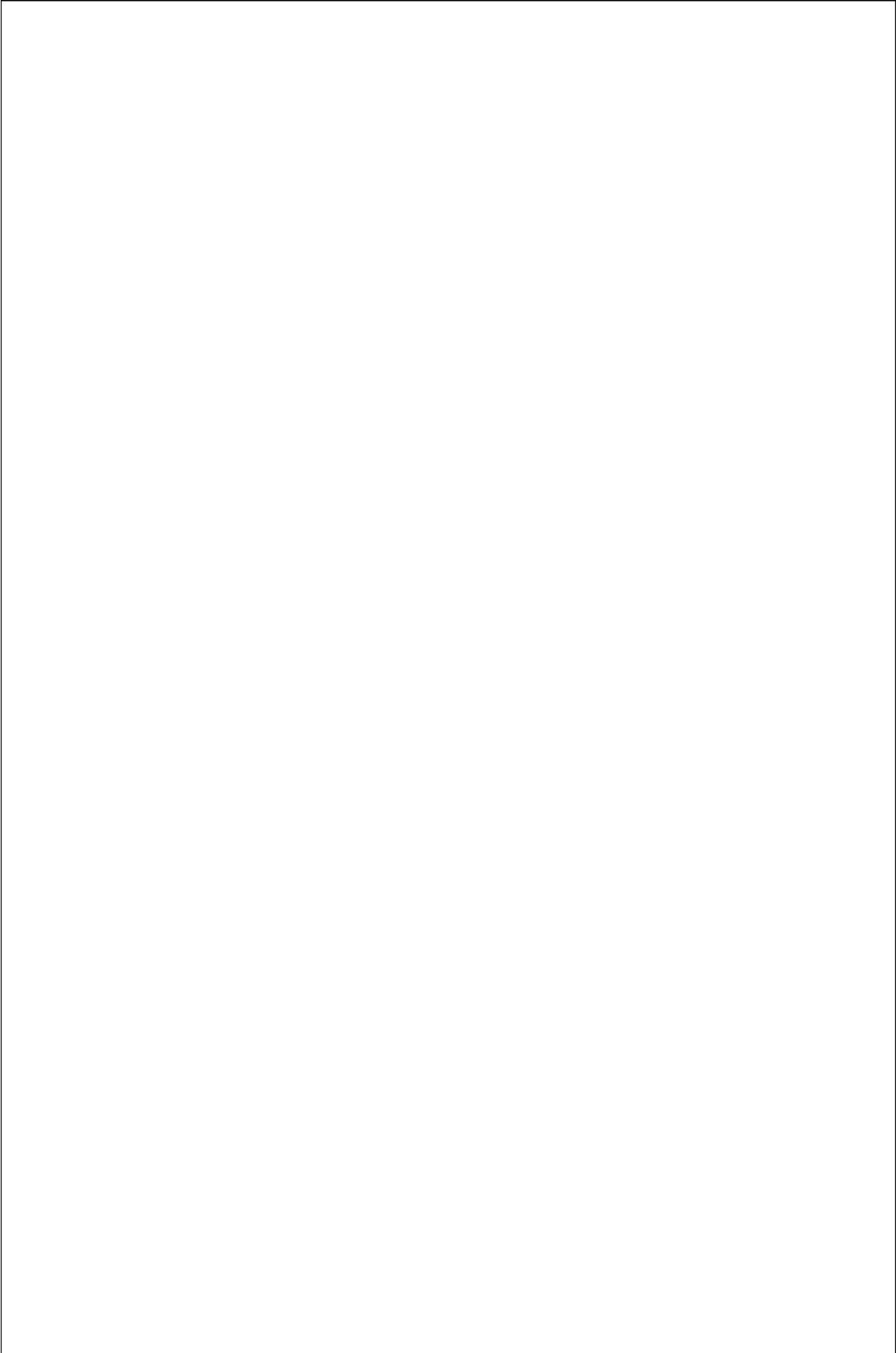
The Georgia Court of Appeals rejected the borrower's assertion, noting that the borrower received the benefit of the entire \$1.48 million principal amount, and that this amount was in fact disbursed to the borrower.

Intervening Landowners Who Assumed Debt but Were not Parties to the Deficiency Action Under the Foreclosed Security Deed are Released from Liability for the Deficiency

Michael Hill and David Hayes purchased property subject to an existing loan, and agreed to assume and pay the loan. The property was later sold to Benny Mitcham, who also took the property subject to the existing loan and agreed to assume and pay the loan. Mitcham failed to make all the payments on the loan, and the property was foreclosed on by Jones, the holder of the loan.

Jones then filed a deficiency action against Moye and Dennard, the original makers of the loan, to recover the difference between the outstanding amount of the loan and the amount received at the foreclosure sale. Neither Hill nor Hayes was made a party to this action. Jones obtained a deficiency judgment against Moye and Dennard. Moye and Dennard then filed suit against Hill and Hayes to collect the deficiency Moye and Dennard had paid to Jones.

The Georgia Court of Appeals held that Hill and Hayes were not liable to Moye and Dennard since neither Hill nor Hayes had received notice of the deficiency, and the Georgia deficiency statute provides that no confirmation is valid against a debtor unless the debtor has been given at least five days legal notice of the proceeding. *Hill v. Moye* (Ga. 1996)



In addition to this Review, Troutman Sanders LLP also publishes six other newsletters:

Business & The Law addresses the needs of publicly and privately held companies and seeks to provide items of interest to owners and executives of these companies.

Employment & The Law details current issues in labor, compensation, ERISA and tax that impact the relationship between employers and employees.

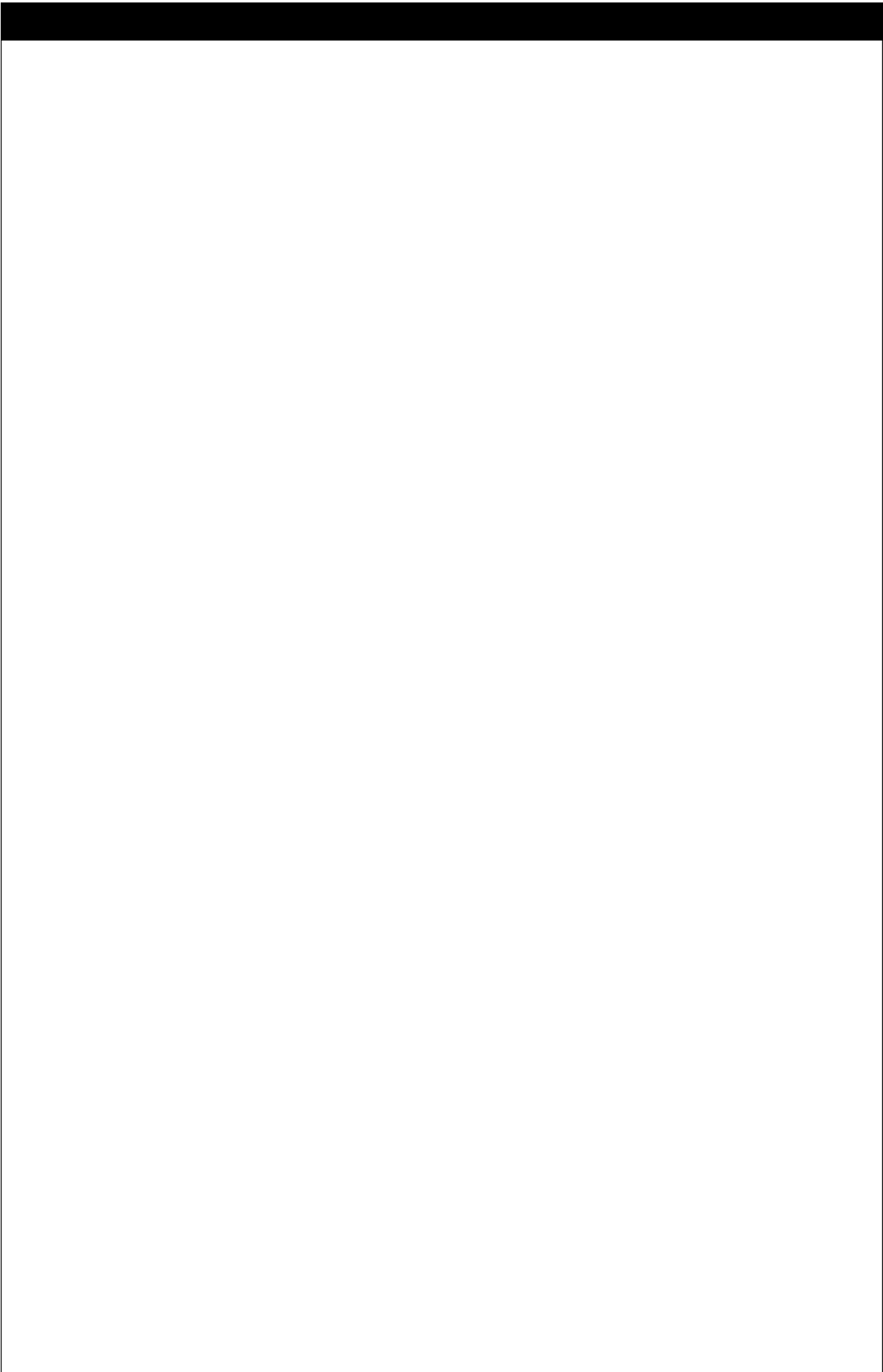
Environment & The Law tracks developing trends in environmental law, including air and water quality and hazardous substances.

Intellectual Property & The Law covers current issues in intellectual property/high tech areas, including copyrights, trademarks, patents, trade secrets, employment agreements and tax issues applicable to the development of technology.

International Business & The Law details current issues that impact international business transactions, trade in merchandise and services, and international investment opportunities.

Lending & The Law details current issues that arise in the commercial loan industry.

Please contact Teri Eaton at 404-885-3731 if you would like to receive any of these publications.



In addition to this Review, Troutman Sanders LLP also publishes six other newsletters:

Business & The Law addresses the needs of publicly and privately held companies and seeks to provide items of interest to owners and executives of these companies.

Employment & The Law details current issues in labor, compensation, ERISA and tax that impact the relationship between employers and employees.

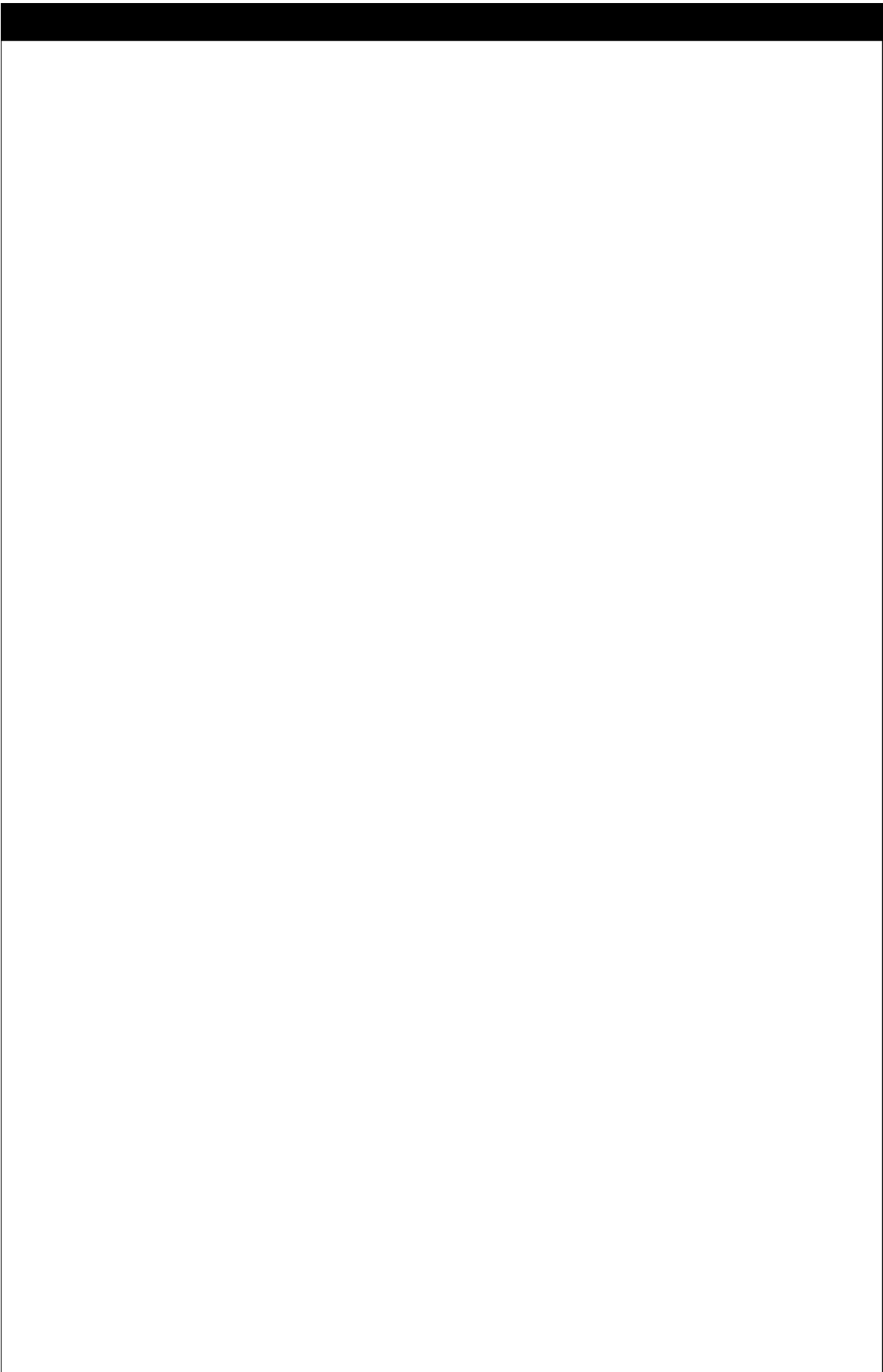
Environment & The Law tracks developing trends in environmental law, including air and water quality and hazardous substances.

Intellectual Property & The Law covers current issues in intellectual property/high tech areas, including copyrights, trademarks, patents, trade secrets, employment agreements and tax issues applicable to the development of technology.

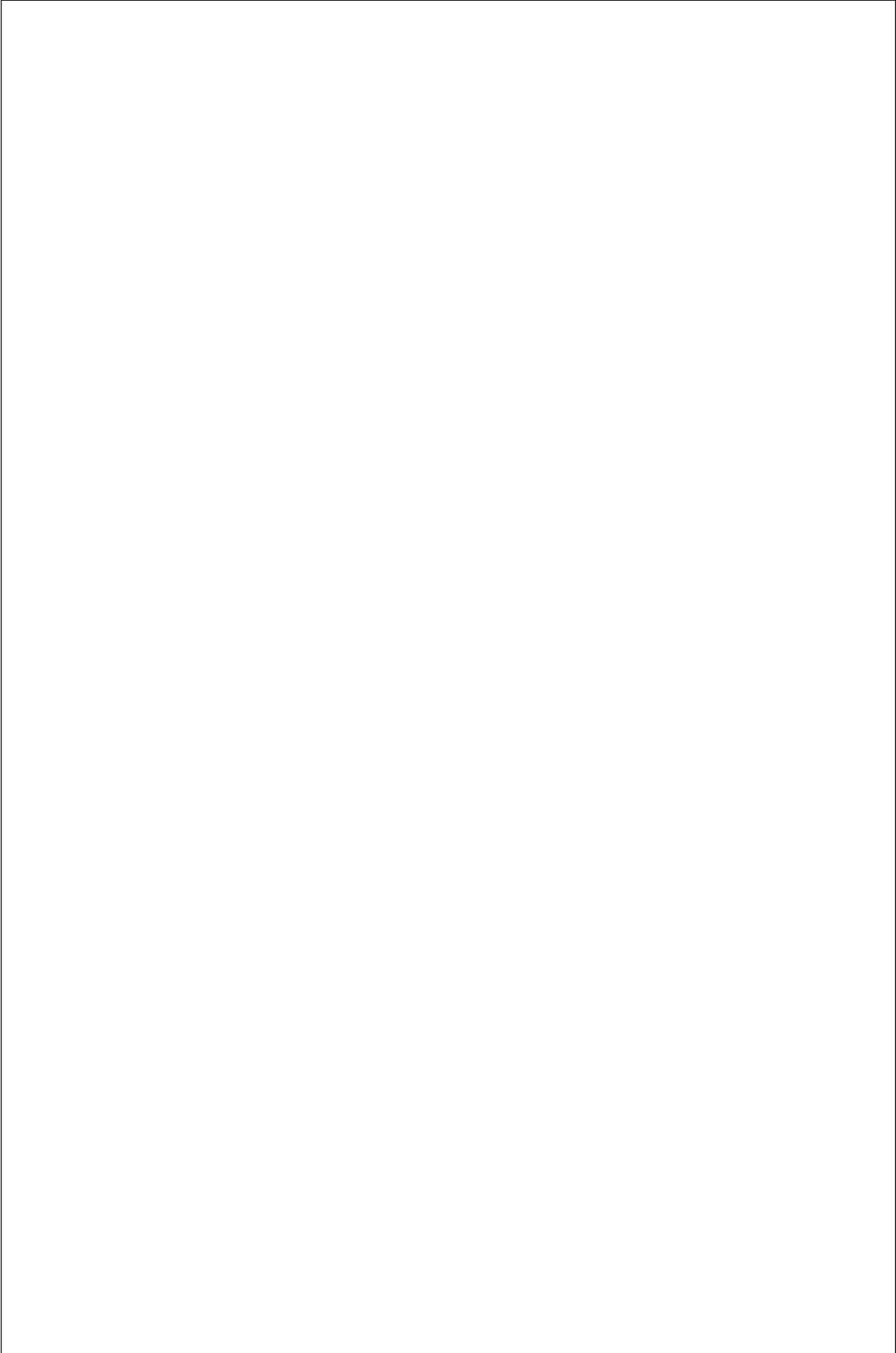
International Business & The Law details current issues that impact international business transactions, trade in merchandise and services, and international investment opportunities.

Lending & The Law details current issues that arise in the commercial loan industry.

Please contact Teri Eaton at 404-885-3731 if you would like to receive any of these publications.



R E V I E W



R E V I E W

