SINCE 1854

Chicago Daily Law Bulletin®

Volume 154, No. 109 Tuesday, June 3, 2008

New practice group targets ripple effect

By Jerry Crimmins
Law Bulletin staff writer

Faced with falling real estate values, reluctant customers and risk-averse lenders, the business world has moved into uncharted territory, according to lawyers at Arnstein & Lehr LLP.

For some difficult business situations, cooperation among borrowers, debtors, contractors and creditors may be a solution.

But such cooperation can itself lead to unexpected tax liabilities, according to Arnstein attorneys Konstantinos Armiros and Samuel H. Levine.

This concern, Armiros and Levine say, has prompted their firm to form a Commercial Solutions Service Group to offer business wide-ranging legal advice across many disciplines, advice they say is geared to the current downturn.

Co-chaired by Armiros and Levine, the group combines the expertise of lawyers from seven different practice areas: banks and financial institutions, bankruptcy and creditors' rights, condominium and community associations, construction, litigation, real estate and tax.

To show what the new Commercial Solutions Service Group offers, Arnstein & Lehr created a unique section on its Web site that tells four generic stories that the law firm says its group members are experienced in dealing with.

Found at www.Arnstein.com, the four types of troubles described are the collapse of a home builder, failed condominium conversion, failure of a manufacturer and the mortgage meldown.

Armiros and Levine cited a number of pressures that together have put U.S. business into "uncharted territory:"

- Simultaneous distress in residential and commercial real estate markets.
- Traditional retail customers reluctant to spend or switching to wholesale outlets.
- Retailer bankruptcies (Wickes Furniture, Sharper Image, etc.) starting to flood the commercial real estate market with vacant space.
- Banks losing bargaining power because too many foreclosures would mean too many unwanted properties.
- Condo owners and associations forced to deal with failing developers in half-sold buildings.

"What's unique about today's troubles," Levine said, is that "lenders have lent money on the expectation that the real estate … would rise in value and the real estate itself would be sufficient to carry the property in case the borrower wasn't able to pay back the loan. That's not the case today."

Also, Armiros said, "The last time the real estate market has been this bad was in the early 1990s," but then "the pain was felt primarily in the commercial area. Now the residential market is in horrible distress."

Developers with unsold homes might have been able to sell some through risky mortgages in the past, Armiros added, but that option is gone.

The gasoline crisis means that even willing buyers won't touch developments in the exurbs. As part of that ripple effect, retailers and commercial developers on the fringes of the urban areas are also in trouble.

Construction contractors are not getting paid for work completed, and are filing mechanic's liens on the properties, the attorneys point out.

"Everybody is in a world of hurt," Armiros said. "But they have to pull together."

Chapter 11 bankruptcies are not always the best option because they can persist for years and can add another layer of expense to the problem, according to Levine and Armiros.

"Workouts," or out-of-court arrangements among borrowers, debtors and creditors may sometimes be the best answer.

But liquidation of assets can create "paper profits" that create new tax liabilities. Debt forgiveness can also create tax problems unless these matters are properly structured, these attorneys say.

"We represent all sides" in different matters, Armiros said. He said the firm recently did hire a new partner, Justin L. Weisberg, who typically represents contractors in mechanic's liens actions.

"What everybody's talking about in the law or in their professions," Armiros added, "is where is the bottom?"

Levine guessed, "I have a feeling in 2009."

"That's what we're hearing," said Armiros.