

# CBA Interfaith Law Committee



Materials on Management of Illinois Real Estate  
Owned and/or Occupied  
by Religious Organizations

*by*

Michael P. Mosher

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## I. General Legal Issues Related to Using, Occupying and Owning Real Estate.

Nearly all Illinois religious organizations have a place to worship and meet together as a group. In that regard these organizations either own or lease real estate. It is the possession and use of real estate that makes religious organizations legally complicated. Leasing “commercial” real estate includes numerous legal issues that require considerable knowledge and understanding. Often it is relatively easy to move into a leasehold property provided the required people sign the lease. Leaving the property may be a different story; especially if the leaders signed the lease in their private capacity. Far more complicated is the legal adventure of owning real estate. To own and properly operate commercial real estate, the organization’s leaders must be prepared to deal with a myriad of legal and social issues that go far beyond the simple mission of the group.

This part of the Checklist gives the reader a brief overview of many of the more important legal issues that affect the use and occupancy of real estate. The average leader is not equipped to fully appreciate all of the problems that are associated with having a place to worship. As a result, the organization needs access to competent legal services. It must be noted that not all attorneys are skilled in working with the special qualities of religious property. Before retaining the neighborhood attorney or accepting *pro bono* legal services from a well intended person on the board of directors, check their credentials. Do not become a learning opportunity for your attorney. Expect your attorney to have had experience with the legal issues involved. Many religious organizations fail to secure the various tax benefits available in law because they are ill-advised by legal counsel.

## II. Leasehold Interests in Real Estate

It is very common for small, independent organizations to lease a vacant storefront facility in which to conduct public services. When they negotiated the terms of the lease, the landlord pulled a standard form “store lease” from his drawer, filled in a few blank spaces and said, “Here, sign at the bottom and give me the security deposit — you can move in tomorrow.” If the leaders read the lease they realized that it was very different from their apartment lease. In many cases, after a short prayer, a five-year lease is signed; two members sign as guarantors; money is exchanged; and the organization begins to operate from its new space. A few weeks after the services begin the neighbors wonder why religious services are being conducted at the old shoe store. A policeman drops by to inform the minister that the storefront is not zoned for religious activities. The city building department sends a letter to cease unlawful activities. The landlord agrees to terminate the lease for a one-time settlement fee of \$25,000, otherwise keep paying the rent: \$1,000 per month for the 56 months remaining on the lease. Your new attorney shrugs his shoulders and gives no encouraging word.

The above scenario may seem exaggerated, but similar fact situations occur in real life all too

frequently. Some careful planning and a little bit of professional assistance can make leasing property relatively easy. The following paragraphs provide some insights into leasing property that might save a lot of grief.

#### A. Securing and Using Professional Services – Licensed Real Estate Broker and Attorney

Many religious organizations are blessed with members who have useful attributes like a license to practice law or to arrange real estate transactions. If these people are willing to give their professional services to the organization, they should be appointed to the property acquisition committee. Even if their particular skills are not in line with the specific project, their general disciplines are valuable to the organization. An attorney who works in civil litigation should not be expected to negotiate the lease or handle a property purchase. Specialized legal counsel is necessary. However, related professional skills in a member do often translate well as a liaison between the specialist and the board of directors. Effective communication usually results in lower fees and better service by the professional. A Realtor on the committee is valuable when selecting a location and may help when evaluating the potential property. Beware of employing the services of attorneys and realtors who are members of the organizations. No law or public policy prohibits such employment, however there is great potential for conflict of interest. Personal interests and special relationships can become very complicated. When a deal turns out badly it is easy to blame the professional who was supposed to avoid the problem – especially when he or she was paid for the service. It is also easy for some members who volunteer their time to resent others members who sell their time. Finally, it is often the case that professional members may accept an assignment that is outside of their area of expertise, in order to please the other members.

#### B. Terms of Lease Agreement

The first thing to understand is that leasing a storefront or any other commercial property is very different from leasing an apartment. Illinois law provides many protections for persons leasing a home. Commercial leases are negotiated *laissez faire*. Loosely translated, you're on your own. The rules of commercial transactions are harsh, and businessmen are often unsympathetic to inept religious organizations. Treat a commercial lease with great respect. Before signing the lease be sure to understand the terms and know what the organization needs in order to have a satisfactory tenancy.

##### 1. A Written Contract

The lease is a legal contract, enforceable by law. The proper names of all necessary parties should appear at the top of the lease. The true owner's name (or legal agent) should be on one side and the corporate name of the organization on the other side. Do not lease the property in the name of an individual. The person who signs the lease should be sure to identify his or her authority as an agent of the corporation. If possible, avoid having members sign the lease as guarantors. If the organization defaults on the lease, the landlord can go after the guarantors – even if they left the organization years ago. The written lease contains the entire agreement. Oral promises made by the landlord during the negotiations are not enforceable unless reduced into written form and expressly incorporated in the lease. If the landlord promises to decorate or

make important repairs, get it in writing. Most commercial leases require the tenant to maintain the interior of the store or office and the landlord is seldom responsible for anything but major repairs to the roof or structure of the building. Electric and plumbing equipment are the tenant's problem. The tenant cannot cancel the lease when the property gets run down and the toilet does not work any more. In fact, the tenant is required to return the property in the original condition, reasonable wear and tear excepted.

## 2. Basic Lease Terms

Some of the most important terms of the lease should include:

- a. Monthly rent in dollars and the time of the month payment is expected;
- b. Security deposit in dollars and whether interest will be paid and how the security deposit will be returned at the end of the lease;
- c. Late payment penalties and the date of accrual;
- d. Term of the lease in years or months, including the exact starting and ending dates;
- e. Renewal options, if any;
- f. Services provided by the landlord, if any;
- g. Responsibilities of the tenant to repair and replace damaged property;
- h. Insurance responsibilities including limits of coverage and other insured parties, i.e. the landlord;
- i. Default provisions holding tenant liable for any and all failures under the contract and generally holding the landlord responsible only to allow the tenant the "use and enjoyment" of the premises (note "enjoyment" here is not like pleasure);
- j. Restrictions on the use and enjoyment of the premises such as noise levels and other activities that may be obnoxious to neighbors; and
- k. Other special provisions written into the lease by the tenant to ensure that the landlord's oral promises are enforceable.

## 3. Use Contingencies

Some additional terms that should be in the commercial lease deserve special attention. When a religious organization leases property it has very particular plans. The standard form lease is not intended to cover a worship facility so it must be modified. First of all, the lease should be made contingent upon the ability of the tenant to use the premises for public worship meetings. Many local zoning laws do not permit churches and other similar organizations to locate in commercial areas. Residential areas are the authorized zone. Often the law will permit religious organizations to apply for a special use permit in areas not otherwise allowing such activity. In such cases it is best to obtain special permits before occupying the premises. In any case the lease should be "contingent" upon the tenants' lawful use of the property for intended religious purposes. If the local zoning board refuses to give the permit, the lease will become voidable by the tenant. It is important that contingencies be negotiated before the organization has invested time and effort in the leasehold. If the landlord promises to replace the furnace in two months, make the payment of rent contingent upon satisfaction of the agreement. It is easy for the landlord to ignore expensive leasehold repairs unless the rent stops coming in. All important promises of the landlord and all necessary use permits should be

written as contingencies to the continuation of the lease.

#### 4. Civil Liabilities and Insurance

Commercial leases nearly always require the tenant to obtain and maintain property damage insurance. The landlord is protecting his interests. However, religious organizations using property are exposed to a number of legal risks when inviting members of the public onto private property. These legal risks may not be covered by the property insurance. Adequate insurance coverage should include broad liability coverage including personal injuries associated with use of the facility, food service, transportation for members and children, program activities away from the facility and possibly directors and officers liability.

#### C. Land Use and Zoning Restrictions

Virtually all improved real estate in Illinois is subject to some form of use restrictions. Municipal governments enact ordinances designed to protect private property by zoning land use. Homeowners generally do not want the house next door converted to a fast food hamburger heaven. Zoning ordinances control the normal use of real estate so that people can purchase property with a reasonable expectation that neighbors will conform to a common set of land use rules. These ordinances tend to permit religious organizations only in residential areas with certain limitations. Churches and similar institutions tend to attract people who gather to make a joyful noise, which may not please everyone in the neighborhood. When leasing or buying real estate, always check the applicable zoning rules. Consult with the local municipal authorities about the qualified uses of the particular property in question. Authoritative, favorable opinions should be in writing to avoid future conflict in case it should turn out that the official was incorrect. If the authority is not favorable to the initial plan the leaders should, “How can a special use permit or a variance be obtained?” If it is clear that you cannot get there from here, find a different location and avoid a lot of trouble. This knowledge before signing a commercial lease is a great asset. In any case, be sure the lease is contingent upon the ability to use the property for the intended religious purposes.

#### D. Property Tax-Exemption and Leasehold Interests

Under certain circumstances, real estate leased by a religious organization may qualify for tax-exempt status. Generally, the rule in Illinois is that tax-exempt property must be both owned and used by a qualified organization. However, the specific law in Illinois does not specify that religious organizations must own the subject property. The law requires that the property be used exclusively for religious purposes and NOT “used or leased with a view to profit.” Therefore, if a member leases property for the exclusive use of a qualified religious organization and requires only payment of utilities and taxes in lieu of rent, it should qualify for exemption from property taxes. It will require very careful attention to the tax complaint to convince the Department of Revenue of the merits of this case because this situation rarely occurs in real life.

### III. Ownership Interests in Real Estate

Owning real estate involves many of the same legal issues as leasing except there is no

landlord, and the financial responsibilities are much greater. Purchasing real estate is a complex legal transaction that should be attended by a qualified attorney at law. Seeking legal advice at the beginning of the project will enhance the benefits. If an attorney is engaged shortly before the closing, the fees may be less but so will the quality of service. By the time a closing is scheduled the mistakes made may not be correctable. The following paragraphs briefly describe some of the salient legal and practical issues that may be involved in the purchase of real estate. The checklist may help the reader to prepare for such event. This material should not be used in lieu of employing the services of a competent real estate broker and attorney.

#### A. Purchasing Real Estate

The financial investment in leasing property is insignificant compared to purchasing property of similar dimension. The preparation preliminary to the purchase is vital.

##### 1. Evaluation of Organizational Needs

Before a new property can be selected, the religious organization should carefully evaluate its actual needs. Assuming the organization is growing, consider its space requirements for at least the next five years. Consider the location of members as well as any special aspects of the corporate culture. Location is very important to the success of most religious organizations. Does the organization plan to develop or enlarge special charitable or educational programs? This process may seem obvious to the reader. Likewise the process may be taken for granted by the leadership without paying careful attention to the thoughts and ideas of the members. Often a piece of property may seem to “fall into your lap.” Such conditions deserve extra attention to assure that the property may not in fact be “too good to be true”. Always remember that the purchase price will be paid out of the pockets of the members. Be sure they enthusiastically support the project.

##### 2. Evaluation of Financial Resources

The next important planning step is to carefully evaluate the financial resources of the organization. Avoid focusing attention on a single approach to finances. For example, some groups will not borrow funds to purchase property. They must have the cash in hand before buying property. With all due respect for spiritual and fiscal integrity, a good and proper facility is critical in the growth of most religious organizations. Usually the successful purchase of real estate is the result of corporate courage and good planning. Include the members in the financial decisions.

###### a. Charitable Contributions and Capital Campaigns

The first financial resource to consider is the membership. Do not expect the members to generate the entire capital requirement at the front end, but do make reasonable assumptions about membership growth in the new facility. Educate the members about the need for a new facility, and if a location has been selected, conduct tours of the prospective facility. Set reasonably high goals for the capital campaign but do not be daunted if the members do not subscribe to the full cost. Plan for multiple financial resources.

###### b. Negotiating a Commercial Loan

Obtaining a commercial loan commitment is a significant challenge for most

religious organizations. Banks generally do not like to lend money to churches, etc., because of what would happen if the organization were to default. It is not good for public relations when a bank forecloses and evicts a religious group in the neighborhood. The federal government requires that all FDIC-insured banks must make a percentage of loan funds available for community redevelopment and religious organizations can qualify for these set-aside funds. Before meeting with a banker, prepare the most favorable presentation for the loan. (Bankers are busy and do not want to sit with a minister who is begging for a loan.) Have a clear and well developed plan describing the property to be purchased, a detailed account of the organization's income, expenses and current assets, and an explanation as to how the loan will be repaid. If the organization has an accountant or even a bookkeeper in the membership, ask them to help with this part of the project. If the property will need repairs or rehabilitation, the plan should include details about how the work will be accomplished. If the members have pledged personal gifts to the capital project, be sure these pledges are in writing. Show the banker the collection of members' pledges, and emphasize the broad support for the project. By giving the banker a very good first impression, the prospect for a successful loan application increases significantly.

#### c. Bond Issues and Other Special Funding Opportunities

A excellent method for raising capital funds is through a bond issue. There are several companies around the country that do excellent work in this regard for all types of membership organizations. Faithful members of an organization will often *lend* a few thousand dollars to the group when they would not donate the money. Young families often cannot give a large donation even though they fully support a capital project. However, the same family will dip into their savings account and lend five or ten thousand dollars to the campaign in return for a modest interest return, knowing the loan is secured by the prospective land. Their money will be paid back in a few years when they need it for kid's college or to buy the new house. An interesting side benefit to the bond issue plan is that members who invest in the project tend to take a greater interest in the success of the organization.

Religious organizations cannot qualify for tax-exempt bonds but there are other significant tax benefits for investors. For example, the loan account can be set up to qualify as a tax deferred retirement account. Members can rollover their IRA accounts into the fund for long-term investment purposes. Another benefit of the bond issue is that members of the organization will usually accept a lower interest return than a commercial lender would.

#### d. Seller Financing—Installment Purchase Agreements

Perhaps the best initial financing plan involves the seller loaning the purchase funds through an installment agreement or by accepting a note and mortgage in lieu of cash at the closing. If a property is difficult to sell and the seller does not need cash right away, and if the Seller owns the real estate outright, the installment contract is an excellent deal for both parties. The purchaser gains access to the property without having to process a commercial loan, and the seller can obtain a higher rate of return on the investment than by renting the property. Usually, installment contracts call for one or two interest points above the current commercial rate. These agreements often include a "balloon" payment five or six years after the initial closing. In other words, the loan may be amortized over twenty years, but the purchaser must pay the entire

remaining balance of the loan after a few years. By the time the balloon payment is due and payable, the organization should be in a much better position to attract a commercial loan or to induce the growing membership to donate or loan the necessary funds.

### 3. Investigating the Prospective Neighborhood

Experts say there are three critical issues when purchasing real estate: (1) LOCATION, (2) LOCATION, (3) LOCATION. Do not underestimate this issue. A religious organization located in the wrong place will have great difficulty thriving. Sometimes it takes years to find the right location for the new worship facility. If the location is too far away from the members or simply in the wrong neighborhood, the impact on the congregation can be very negative. Avoid the trap of putting a time deadline on the selection process. Until the right place is identified it is too early to buy. Every religious organization has very special needs that should be addressed when choosing a new facility. Personal comfort of the members must be in balance with religious mission, and the actual price in many cases is the least important factor. With any selection procedure the following steps should be taken.

#### a. Meet the Neighbors

After a property has been identified, a committee of members that represents all elements of the congregation should visit the neighborhood on several occasions. Take into account that the affect of a neighborhood changes through the course of the day. Weekends are different from weekdays. The committee should split-up into twos and threes and simply walk around the neighborhood at different times of the week. Talk to prospective neighbors directly; ask them about the place. Maybe the residents think the old abandoned building is haunted or has a bad spirit. Maybe the neighbors are hostile to having another religious organization in the area or they just do not want that kind of religion in the neighborhood. Whether such attitudes are right or wrong, the congregation should know what they are buying into before the contract is finalized. Purchasers take the property as is—for better or for worse.

#### b. Meet the Alderman and the Local Politicals

Most neighborhoods in urban communities have block clubs or other associations that parallel the local political system. In Chicago, every aldermanic ward is divided into convenient subareas which are monitored by ward bosses and their subordinates. These people are very important to consider when choosing a new location. Some of these people will not be concerned about transitions affecting religious facilities. However, if many of the congregants live in or near the ward the new group may be very welcome, since the politicals are always looking for goodwill and votes. On the other hand, they may have negative attitudes which would need to be identified as early as possible. The local political leaders may have prejudicial stereotypes which may be overcome with simple courtesy and respect. This instruction is not intended to say that racial and cultural bias should control the location decision. Merely that the neighborhood will greatly impact the life of a religious organization, and early efforts to reduce social tension are very important.

The center of local political life is the alderman (or local equivalent). It is impolite and impolitic to move into a neighborhood without meeting the alderman and explaining the mission

of the organization. Most aldermen will be very receptive to a courtesy visit and may offer valuable support. A few aldermen will be indifferent or even hostile to the transition plans. All of them will be gratified by a simple show of respect (whether deserved or not) and if the organization has the potential of a supportive constituency, a hostile alderman can be positively influenced.

Communities experiencing demographic changes are volatile and should be evaluated very carefully. Real estate may seem cheap in such communities but the social realities can devastate the life of a religious organization unless its mission is to reach out to people in transition. In any case the alderman is an important part of the puzzle and should be part of the solution.

#### 4. Selection and Use of Licensed Real Estate Brokers and Legal Counsel

As explained above, the services of an experienced licensed real estate broker or sales person (broker) and a skilled attorney are very important to a successful real estate transaction. Be sure that the broker is familiar with the neighborhood and that the attorney has experience working with the special requirements of religious organizations. Locate a broker by visiting the target area and interviewing local brokers. Many real estate agents have become associated or organized into regional or national offices. For the most part these associations are created to share information and marketing expenses. Do not substitute the big name agency for an effective local office. Identifying a property that will be suitable for a religious facility can be done only by someone who has local experience. Once the property is located, most brokers become committed to the process of closing the deal. This is not a bad thing but the buyer should be sure about who is representing its legal interest. The attorney should be selected by a careful process of interviewing and evaluating. Unless the organization has a regular attorney the selection process may be daunting. The broker usually will suggest the name of a “real estate attorney” who does all of his closings for cheap. These are often people who do a lot of residential closings and may have little experience with commercial, let alone religious, properties. The cheapest attorney is usually not the best person for the job. Retain an attorney who will charge a reasonable hourly fee and who has had experience with the type of property in question. As soon as a property is identified, and before a purchase contract is presented, the attorney should begin working with the broker. The attorney has only one job to do—protect the legal interests of the client. Closing the deal is not the most important thing to a good attorney. For that reason, some brokers encourage their clients to bring in the attorney after the contract is signed. The most important service an attorney can provide is a well written and negotiated purchase agreement. If the contract is done right the rest of the transaction can follow without putting the purchaser’s legal interests in jeopardy. See the attorney before signing the contract.

#### 5. Initial Identification of Property

The broker is the person who is most able to help the organization locate a specific property to purchase. If the purchaser can clearly express the requirements for the new facility, the broker, using personal experience and computer-aided research, may readily locate possible options.

##### a. Existing Religious Facilities

It is usually best if a suitable existing religious facility can be located, however, there are relatively few such buildings on the market. When a religious organization is selling property, it is often an excellent opportunity for the prospective purchaser. In addition, purchasing a preexisting religious facility will usually simplify the zoning and land use requirements. On the other hand, if the seller is not a *thriving* congregation, there may be substantial deferred maintenance, and special care should be given to the condition of the building. Be sure to inspect the property carefully.

b. Storefronts and Other Commercial Properties

Some religious organizations prefer to utilize an adaptable existing commercial building rather than adjusting to the specialized designs of a previous congregation. In urban areas many religious organizations have successfully adapted stores and office buildings to their needs. The cost to rehab a commercial building is usually far less than new construction. Furthermore, when the congregation is finished using a commercial building, the building can often be readily sold to a commercial buyer at a profit. Traditional religious facilities are usually much more difficult to sell. School buildings and old theaters have been effectively converted for religious use. In any case, when a religious organization plans to acquire a commercial building, it must carefully consider the relevant local zoning ordinances.

c. Residential Properties

Small congregations can sometimes make good use of residential buildings. This is especially the case when a house is located on a busy thoroughfare. The first floor space may be easily opened to accommodate 50 or 60 worshiping people, while the upstairs can be used for classrooms and offices. As with commercial property the purchaser must carefully research the applicable zoning ordinances before acquiring a residential property (unless it will be used as a parsonage).

d. Beware of the “Handyman Special”

Often religious organizations acquire a building in need of substantial repairs. Surely the members will volunteer to work on the building during evenings and weekends. It is good to have skilled people in the congregation but risky to assume that they will be able and willing to see the job through to completion. It is better to employ the services of a professional contractor and build into the contract that some of the simple labor intensive jobs will be done by volunteers. The contractor can prepare the facility for use, and the jobs like painting and nonessential repairs can be done over a longer time period at the volunteer’s convenience. Do not count on volunteers to perform jobs under heavy time pressures.

Remember that many rehab projects require local building permits. Plumbing, electrical and structural repairs almost always involve local building codes and should be done by a skilled professional who is familiar with local rules. All buildings of public accommodation, including worship facilities, are closely scrutinized by municipal safety inspectors and the owner can be made to pull out all construction work that does not meet the code specifications.

## 6. Preparing and Presenting the Contract Offer

Often the broker will prepare the initial draft of the real estate purchase contract in smaller transactions such as residential purchases. Commercial property often involves complex legal issues that are beyond the skill of the broker and, therefore, should be prepared by an attorney. A well-prepared seller may have its attorney draft the contract so as to control the terms and basic form of the agreement. When the seller is not so prepared, the purchaser's attorney usually drafts the contract, obtains the purchaser's signature and earnest money and the broker makes the initial presentation. Negotiations may take a few days or several months depending on the matters at stake. Remember, the attorney's primary job is to protect the interests of their respective clients and the broker's job is to bring the seller and the buyer to a closing. Working together, these professionals can provide both parties with a successful transaction.

### a. Basic Terms of the Contract

A real estate transaction begins to come together through a written contract to sell or purchase real estate. Under Illinois law an agreement concerning the transfer of real estate is not enforceable unless it is in writing and is supported by earnest money. The following paragraphs will briefly describe some of the most important parts of a contract. Preparing a proper contract should be done by an experienced attorney; brokers should not be preparing contracts to buy or sell commercial property.

#### (1) Necessary Parties to the Contract

The proper names of both buyer and seller must be identified in the contract and all interested parties should be signatories to the contract. Often a corporation is selling its commercial property, in which case be sure to use the full legal name of the corporation and identify the officers who are authorized to sign on behalf of the corporation. (If there are any doubts about the legal status of a corporation, a quick call to the Secretary of State Corporation Department will provide some information about every corporation authorized to operate in Illinois.) If more than one person owns the property, be sure to include all full legal names and be sure that everyone signs the contract. If property is held by a land trust, the trustee should sign the contract and the buyer should obtain a copy of the trust agreement and evidence that the person who purports to be the seller has the authority to transfer the property.

#### (2) Consideration

Consideration is money or other valuable property being used to purchase the real estate. This is an obvious part of the contract which is often neglected. The consideration is often transferred in two or more units. First the buyer gives earnest money to the seller's broker, attorney or some mutually trusted third person. The buyer should *never* give the earnest money directly to the seller. If a conflict arises during a transaction and the buyer decides not to buy the property, it may be very difficult to recover the earnest money if it is in the seller's possession. The second unit of consideration is given at the closing unless the contract calls for special terms of payment. For example, an installment agreement may call for regular monthly payments over a period of years. The deed is conveyed after full payment, if received by the seller. There are many variations on the exchange of consideration and this part of the contract needs careful attention and very clear language.

### (3) Contract Contingencies

A contract contingency is an event that must occur before a contract becomes fully enforceable. Because of the time pressure that attends most real estate transactions, buyers seldom have all necessary information about a piece of property when the contract is signed. Therefore the careful buyer will make the contract subject to inspections and reviews by other people who have special expertise. Also the buyer who plans to borrow the funds to buy property will usually need some time to obtain the bank's loan commitment. There are several specific contingencies that every buyer should consider.

#### (a) Contingency to Secure finances

The finance contingency gives the buyer a few weeks or months to secure a loan commitment from the bank. Even if the buyer has been "pre-approved" by a bank, the finance contingency is very necessary. Many things can happen to a commercial real estate transaction and the buyer will want to avoid the contract and recover the earnest money if the finance plans fail. Some religious organizations need to raise charitable support before a purchase can be closed. Whatever the case, if the buyer does not have the full purchase price in the bank at the time the contract is signed, the contract should include a finance contingency that specifically says that unless the buyer obtains a certain financial commitment within thirty (or forty-five or ninety) days, the contract is voidable by the buyer and the earnest money can be recovered without penalty.

#### (b) Contingency to Inspect the Property

The initial property selection process seldom includes a thorough inspection of all parts of the building. The buyer is generally not ready to pay the fee of a skilled building inspector until after a contract is in place. A careful buyer will include a contract contingency that provides for a complete inspection within a week or two, depending upon the nature of the building. If the inspection reveals substantial problems with the property, the buyer may want to avoid the contract or renegotiate the sale price. In any case the buyer should include in the contract a contingency that gives ample time to make sure the building is right for the organization.

#### (c) Contingency to Evaluate Environmental Conditions

Environmental problems are almost always a problem with commercial property. Even property that has been used for religious purposes for many years can have environmental problems such as buried heating oil tanks or asbestos wrapped steam pipes. Merely having an environmental problem does not necessarily mean the deal will fall through. Rather, the buyer should be fully aware of the environmental issues affecting a property before the transaction is closed. If necessary, a hazardous chemical problem can be cleaned up by the seller before the closing, or the buyer can simply take the title subject to an identified problem. The important thing is that the buyer can avoid the contract and recover the earnest money if the environmental problem is unacceptable.

#### (d) Contingency to Clear Zoning Issues

One other special issue that often affects commercial property is the

zoning or land use restrictions. Many communities restrict the locations that religious organizations can occupy. The buyer should not acquire a law suit when buying property. To avoid potentially serious problems, the buyer should write the contract so that the zoning issues, if any, are identified and resolved before the closing. If the buyer will not be able to use the property for the purpose intended, it is good to have such information before the closing. A well drafted contract will give the buyer between 120 and 180 days to clear up all land use issues. If the local zoning board refuses to permit the intended use, the buyer can void the contract and recover the earnest money.

#### (4) Occupancy Issues

It is important that the contract describe who will have possession of the property immediately after the closing. Usually the parties will arrange for the possession of the property to change hands at the closing. If the seller has a leasehold tenant in part or all of the property, the possession date will be negotiated in light of the lease agreement. The contract may require the seller to remove the tenant before the closing so the new owner will not be forced to deal with landlord/tenant litigation as the first issue of ownership. If the seller refuses to remove the tenant, the buyer must consider the inconvenience and expenses to legally evict the lawful occupants. Do not assume the seller will be ready to vacate the premises on the closing date. If the seller needs to hold-over occupancy, then the contract should provide a reasonable amount of rental to at least cover the buyer's costs. The buyer may want the rental to be high so the seller will be encouraged to leave quickly. All of these issues should be detailed in the contract so that both parties can make appropriate plans.

#### (5) Condition of Title

When the buyer agrees to purchase real estate, they assume that the seller's title to the property is good and marketable. There are many things that can affect title to property and the buyer should be sure to include in the contract a description of what is acceptable title. Standard form contracts for residential property usually include a brief description of acceptable title. Commercial property is far more complicated and a standard description is often insufficient. Careful attention to this part of the contract will ensure that the buyer is not required to buy property that includes unacceptable easements, covenants, and encumbrances such as tax liens or unsatisfied mortgages. In most communities, buyers can obtain title insurance when buying property. Customarily, the seller is required by the contract to obtain a title insurance commitment before the closing. The buyer's attorney can evaluate the condition of title and can work to resolve problems before the buyer's money is paid out. However, if the contract does not clearly specify the condition of acceptable title, the buyer may be required to accept title with unacceptable defects that will be shown as exceptions to the title insurance policy.

#### (6) Land Survey

It is customary in Illinois for the seller to pay for an ALTA land survey of the land showing the location of all buildings and other improvements. If the contract does not specify the seller's survey requirement in commercial contracts, the buyer will need to pay for one before a bank will issue a loan commitment. The survey is important in determining that the

buildings, fences, driveways, etc., are in fact located on the subject property and not on the neighbor's land. A good survey will also show recorded easements and right-of-ways that may affect the buyer's use of the property.

#### (7) Type of Conveyance

There are many different types of standard conveyance deeds. For example, a warranty deed gives very important and specific warranties by the seller to ensure that the buyer will not experience title problems. A quit claim deed gives the buyer no warranties except the legal right to convey title. Such conveyance transfers only the title in the seller's name. If other people share interest in the property, the buyer may unintentionally have an unacceptable co-owner or an unanticipated unpaid mortgage. The seller can take the money and walk away from the closing unless the contract specifies what warranties will accompany the deed.

#### (8) Closing the Purchase

The contract should provide a specific date and place for the closing. Also, there should be some reasonable details as to what documents the seller must provide at the closing. For example, the seller should provide, in addition to the warranty deed, a financial closing statement, a bill of sale for personal property included in the contract, and an affidavit of title to cover title issues that may arise after the title commitment was issued and before the closing. Other items that the buyer should expect to receive include keys to all locks, warranty papers for items of equipment, etc.

### b. Presenting the Contract

#### 7. Between Contract and Closing

After the contract has been successfully negotiated and the earnest money is in escrow, the buyer must promptly take care of the contract contingencies. The broker may be able to recommend a good building inspector and an environmental consultant to conduct a "phase one" survey. The inspector will need full access to all parts of the facility and the seller may need to make arrangements if there are tenants in the building. The finance contingency is very important and the buyer should start immediately to secure a commercial loan commitment. Most banks and loan brokers making commercial loans will require the buyer to have a phase one environmental survey conducted prior to issuing a commitment. This inspection is valuable to the buyer as well. The phase one survey is a report by a qualified inspector that describes the history of the property as to previous industrial or commercial uses, describes the land and all improvements from the perspective of environmental issues, and projects possible problems that may affect the property. If the survey indicates possible environmental problems the buyer may cancel the contract or renegotiate its terms, if the contingency was properly drafted. In any case, the buyer may want to purchase a phase two inspection, which provides for an environmental engineer to go on the property, take samples of possible hazardous materials and perform a laboratory analysis. The phase two report will specify the precise environmental problems and propose remediation solutions.

## 8. Corporate Resolution and Authority

With a contract in hand, it is necessary for both corporate buyer and seller to prepare certain documents to establish the appropriate legal authority to proceed with the transaction. The seller must be able to prove the corporation is in good standing with the state authorities and that the governing board has authorized the sale of the property. The buyer must also be able to establish proper corporate authority, but the resolution of the governing board must be to borrow money and to place a mortgage on the property. When either buyer or seller is organized as an Illinois Religious Corporation, there may be special problems with establishing corporate authority. For more information about the nature of religious corporations, as distinguished from Illinois not-for-profit corporations, see Chapter One of the Illinois Institute Continuing Legal Education publication on *Organizing and Advising Illinois Not for Profit Corporations* (2000).

## 9. The Closing

After the buyer has satisfied all contract contingencies and the seller has provided evidence of marketable title, the attorneys will set up a closing. The closing is the event at which contract consideration is exchanged, i.e. the seller transfers title and the buyer delivers the purchase funds. Very often there are numerous legal issues to resolve at the closing including possession and post closing repairs. If the contract was well negotiated and both parties are prepared, the closing should be relatively easy, even though complicated.

### B. Occupying the Premises

As explained above, the buyer should not assume the seller will turn over possession at the closing. If a buyer goes to the closing without confirmation of the seller's intentions in this regard, there can be some serious difficulties. Again the contract should have carefully described parties' expectations as to closing. If the buyer's expectations are not satisfied at the closing, it is a good idea to postpone the closing until the possession issues are resolved. If the seller plans to holdover possession, the buyer should have the anticipated rent paid up-front and the closing and a holdover possession escrow agreement funded by the seller's proceeds. If the premises are subject to a third party lease, the buyer may be required to wait until the lease expires or negotiate with the tenant to quit the premises early. It may cost the buyer dearly to buy out the remaining term of the tenant's leasehold interests.

### C. Making Necessary Repairs and Renovations

If a religious organization acquires a storefront or other commercial building that was not previously used for religious purposes, the building will probably need substantial alterations to make the facility usable to the congregation. Be sure to check with the local building department before starting repairs or renovation. The worship facility is a place of public accommodation and local building codes will apply insofar as public safety is concerned. Many religious organizations have gone into a new facility and started doing major repairs, using the well intended volunteer efforts of members. When the local building inspector gets news of such repairs, he conducts a surprise inspection. A few days later a municipal order comes in the mail providing a housing court date and a demand that all unauthorized plumbing, electrical and heating repairs be torn out and a building permit be applied for immediately. The penalties for

failure to follow the court order can be substantial. Therefore, religious organizations should be making plans to alter the property long before the closing. A qualified contractor is usually necessary to obtain the required building permits and to perform the renovations in accordance with the local building code. Also, before the building permit is issued, the owner must also be able to demonstrate that the intended use of the property is in compliance with the zoning laws.

#### IV. Property Tax Exemption

One of the most important benefits for religious organizations owning real estate in Illinois is the ability to have the property exempted from property taxes. This status does not come automatically when a qualified organization acquires property. **ALL NEW PROPERTY OWNERS MUST APPLY FOR PROPERTY TAX EXEMPTION!** Just because the seller owned tax-exempt property does not mean the buyer will be likewise entitled to the tax-exempt status. The law requires the exempt owner to notify the local tax assessor if there is any change in the use or ownership of the property. The assessor will automatically put the property back on the tax rolls when the notice is duly received. The new owner must prepare and file an appropriate application or "Real Estate Exemption Complaint" with the local county tax assessor's office. Each county in Illinois has slightly different rules concerning the application procedure. The application must establish three basic tests: (1) the owner is a qualified religious organization; (2) the intended use of the property is qualified in accordance with state law; and (3) the property will not be "leased or otherwise used with a view to profit." These tests can all be satisfied by providing a copy of the deed, copies of the organization's corporate charter and bylaws, an affidavit of use certified by a principal officer of the corporation, and evidence that the Department of Revenue has issued its "E-9" sales tax exemption number.

When the application has been filed with the county office, a local evaluation of the organization will be made within a few weeks. If more information is needed, the applicant will be invited to appear before the local property tax appeals board in order to make a personal presentation of the fact concerning the application. If the local board approves the application, it will be sent to the Springfield office of the Department of Revenue. This step may take six months to a year before the certificate of exemption will be issued. If the application is denied at the state level, the applicant may appeal the adverse ruling and have a full hearing before an administrative law judge. An appeal and determination may require a year or more to process. In the meantime, the property remains subject to property taxes. Some organizations have experienced serious financial problems with making timely payment of taxes. When purchasing property (especially property that was not previously tax-exempt) the buyer should budget property taxes for up to two years. Be aware that these taxes can be substantial. If the application for tax exemption is successful the taxes paid will be refunded on a prorated basis to the date the exemption was approved. However, it may take a year or more to recover the taxes paid. The best plan for the new owner of tax-exempt property is to file the application as soon as possible after the purchase. Most counties will accept applications at any time of the year. Cook County, for example, will accept applications only at four or five specific times each year between September and April.

## V. Sharing Space with Other Tax-Exempt Organizations

Often when religious organizations acquire real estate, the facility includes more space than is immediately required for operation of the religious programs. In such cases, the owner may wish to allow another organization to share part of the facility. Assuming the property is, or will be, exempt from property taxes, the choice of co-tenants is very important. As explained above, the law affecting tax-exempt property is very specific and does not include the use and occupancy of a non-qualified person or organization. Obviously, if tax-exempt property is leased to a for profit entity, the exemption will be jeopardized. However, the same result may occur if the property is shared with a nonprofit organization that is not itself a qualified tax-exempt entity. Generally, only charitable, religious and educational organizations that qualify under Internal Revenue Code Section 501(c)(3) will qualify for tax-exempt status under Illinois law. Even then, the Illinois law is much narrower than the federal law in relation to qualified tax-exempt status. It is most likely that an organization that has qualified for tax exemption under the Illinois sales tax laws will qualify for property tax exemption provided that the intended use is also qualified.

If keeping the property off the tax rolls is important then the owner must find a similarly qualified organization to share the space and the expenses with. A non-qualified tenant will disqualify part-of or all-of the property from tax-exempt status.

A space sharing agreement should always be in writing. This is the case to ensure a clear and carefully designed sharing agreement but also to enable the assessor's office to determine that the agreement is not for profit. The agreement should start with a description of the mutual tax-exempt purposes of both parties and explain that the sharing agreement is intended to promote a common charitable or religious purpose. The mutual consideration must be described, i.e. the specific area of the facility that the guest will be able to use and the amount of financial contribution the guest will make to the owner. The usage may require a description both as to space and time.

Due to the brief nature of this checklist the space sharing agreement will not be discussed in greater detail. However, any organization that wishes to have detailed instructions about setting-up a space sharing agreement may contact the nonprofit organization called Inspired Partnerships at 53 W Jackson # 852 in Chicago, Illinois, phone number (312) 294-0077. Ask for a copy of Space-sharing Agreements in Houses of Worship: Federal and Illinois Tax and Legal Implications written by Michael P. Mosher attorney at law. There is a small charge for this manual but you can not afford to pay for the document you can review it at the office.

## VI. Selling Real Estate

The foregoing comments generally have been directed at religious organizations in the process of leasing or purchasing real estate. At some time all property owners become sellers. The next few paragraphs deal with the special legal problems that affect religious organizations when they want to sell property. All of the foregoing paragraphs instructing potential buyers will tend to apply to sellers as well—simply consider the other side of the coin with each buyer

instruction. The written terms of the contract are equally important to buyer and seller.

#### A. Choosing a Viable Buyer

When selling real estate, do not waste time and effort trying to sell to a buyer who cannot afford the property. Just about every Buyer wants to buy more than they can afford, so the Seller should come to the market place with clear expectations of how much they are willing to lower the price. Draw a line in the financial sand before negotiating the sale. Do not accept a lesser amount unless the governing board carefully considers the alternatives. The Seller may want to insist that all prospective buyers be “pre-approved” for a bank loan before the contract is negotiated. Attorneys will charge legal fees for preparing the contract, which are not contingent upon the sale closing. Remember that disorganized or desperate organizations do not make viable buyers. Ask the serious prospective buyer to submit evidence of corporate authority and financial status before negotiating the contract. Many small religious organizations are unincorporated associations and may be very problematic buyers.

#### B. Seller’s Contingencies

Sellers, like the buyers may have certain legal issues that cannot be resolved until a contract is in effect. For example, the seller may feel it is necessary to have a contract to purchase another facility before selling its current property. A contract contingency may allow the seller to cancel the contract if a new facility is not acquired by a certain date. If the financial prospects of the buyer are limited, the Seller may want a contingency that allows the contract to be cancelled if another buyer comes along and the buyer’s financial contingency is still in place. Usually this contingency provides that the seller can give the buyer a 72-hour notice that another bona-fide purchaser has made an acceptable offer. The first potential buyer has three days to withdraw their finance contingency or the seller will be free to cancel the first contract and negotiate with the second buyer. If the seller knows there may be some environmental problems with the property, they may make the contract contingent upon not being required to remediate any such problems. Depending upon the circumstances of each seller, there may be many other situations that require a contract contingency to protect the seller.

#### C. Possession and Occupancy Issues

Invariably the seller will need a place to meet and conduct its religious programs shortly after the sale of the property; it cannot afford to be without a location for more than a few days. Possibly the seller cannot purchase a new facility until the sale proceeds from the current property are in hand. In these cases it is clear that the seller must provide for hold-over possession for a few days or weeks after the closing. The contract should explain exactly how and when the property will be turned over to the buyer. If the seller is sharing space with another organization, the contract should specify who is responsible for the tenant. If the income from the tenant is important to the seller, they will not be willing to terminate the lease until the Buyer has removed all contingencies to the contract.. Remember, it takes several weeks to remove a tenant who will not voluntarily vacate the premises. The contract should include ample time to clear the property if the buyer insists upon having possession at the time of the closing.

#### D. Title Clearance Issues

Often a parcel of real estate is affected by minor encumbrances that cannot be reasonably remedied but which may cause the sale to be delayed or leave the seller vulnerable to being forced to drop the purchase price before closing. For example, the concrete patio or the backyard fence may extend over the property line. The next door neighbor may have an easement across the property that gives direct access to a side street. The seller may have used the property for many years without being adversely affected by these matters that technically affect the title. If the encumbrances are truly insignificant, the contract should identify the specific problem and provide that the buyer will take title subject to such defects of title. By putting this issue into the contract at the start of the transaction, both parties have the opportunity to deal with the issue before the work and effort has gone into preparing for the closing. The seller avoids the awkward problem of not being able to feasibly convey clear title, which could become a very costly matter.

### VII. Civil Liability Issues Affected by Real Estate

Owing and operating real estate involves certain inherent risks of civil liability. The most obvious risk concerns injuries to persons. Whether outside on the front lawn or inside sitting on a church pew, the invitees of religious organizations are under a limited legal protection against the negligent causes of personal injury. Slipping on a cracked stair step or being clobbered by a piece of falling ceiling plaster are two ways that the owner can be held accountable for injuries to people who were invited to attend religious services. Every property owner faces the same problem. Liability can arise from injuries suffered by members of the organization as well as all members of the general public who were welcomed to use the facility. When the facility is used for the care of children, the infirm, elderly or any otherwise disabled people, the risks of liability increase substantially. It is sometimes easy for the earnest religious leader to imprudently use defective facilities while trusting higher powers for protection. The absence of actual injury from day to day is no good testimony of faith while the unfortunate occurrence of injury is usually the evidence of negligent ignorance. When the religious leader intentionally disregards the local building safety codes, the stakes become higher and person liability often becomes an issue.

#### A. Repairing and Rehabilitating Buildings for Public Accommodation

The first line of defense involves proper maintenance of the property. Most places of worship are public facilities and civil authorities expect the owners to exercise more prudent standards of operation. In the foregoing paragraphs there was a brief discussion of the necessity for the leaders of religious organizations to use good judgement when repairing or rehabilitating public worship facilities. The handyman at home should not be working on public facilities without qualified professional supervision. Local building codes are often seen as an avoidable obstacle to the effective utilization of potentially valuable property. Some religious organizations expend their financial resources to acquire the largest feasible property and neglect to allocate the resources for the proper development for a place of public accommodation. This is often the case when private commercial buildings are converted to religious facilities. Building codes are generally developed for the safety of the citizens and should not be seen as

expensive obstacles to using a public facility. The local building inspector can be very helpful to property owners who ask questions and view the building department as a resource.

#### B. General Maintenance Program

Assuming the building is in full compliance with the local building codes, the next critical component to risk management is regular maintenance. This task is often delegated to one skilled person in charge of a small committee of capable members to support the overall maintenance of the property, both inside and outside. In Chicago and other large cities in Illinois, there are classes available to people who work on the management of religious facilities. The organization referred to above, Inspired Partnerships, is an excellent resource for this kind of information.

#### C. Insurance Protection

Having done everything right with the rehabilitation project and maintaining the building in excellent condition, there is still no way to guarantee that no one will be injured while using the property. Insurance is the final component to every risk management plan. A comprehensive property liability policy should cover the usual risks. This type of insurance is generally affordable to organizations that have taken reasonable steps to maintain the property. Fire and casualty are the main part of the policy. Public liability coverage protects the organization when visitors slip and fall or sustain other types of personal injury. The policy should have these areas covered at a minimum. In addition the organization may want the policy to cover theft of property and it may cover the leaders and staff regarding personal liability for errors and omissions. Most reputable insurance companies that market to religious organizations include all of the above protection in a standard affordable package plan. If the organization operates social service programs involving child care, overnight shelter, feeding and personal counseling, the insurance agent should be made fully aware of the special risk factors. Most insurance policies include many paragraphs that explain what risks are excluded from coverage. It is very important for one or more member of the organization to carefully read the insurance policy and to be sure that it covers all of the significant risks associated with the building and the programs.

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