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The March to Complete Lease Accounting Standards Changes Continues

The Financial Accounting Standards Board (FASB) and its international equivalent, the International Accounting Standards Board (IASB), are close to finalizing major changes to the financial accounting standards for leases that would require the capitalization of nearly all real estate and equipment leases on balance sheets by recognizing the rights and obligations of tenants. On August 17, 2010, FASB and IASB (collectively, the "Boards") released a draft proposal, known as an Exposure Draft, of the new lease accounting standards. Although the Exposure Draft was open for public comment until December 15, 2010, commentators have noted that it is unlikely that the key elements of the draft will change.

Since December, FASB and IASB have undertaken various public outreach activities to discuss the proposals with a wide range of interested parties. The Boards held public roundtable meetings around the globe during December 2010 and January 2011 to discuss their Exposure Draft with key stakeholders. FASB's stated purpose in holding these meetings was to "engage in a constructive dialogue

about the Exposure Draft with a wide variety of stakeholders, representing a variety of perspectives, including those of preparers, auditors, investors, and other users of financial statements." In addition to the public roundtable meetings, FASB has made webcast discussions available on its web site and held a Leases Working Group Meeting on January 7, 2011, in Norwalk, CT, to continue the discussion process.

After the public discourse and deliberations have concluded, the Boards have announced that they will revisit all feedback, deliberate significant issues and issue a final lease accounting standard sometime around June 2011. The Boards have not announced a date for the issuance of the final revised standard, but FASB has indicated, and it is generally expected, that the final standard will be issued during the second quarter of 2011.

If adopted, the new accounting rules would require almost all leases to be capitalized on a tenant's balance sheet. Under current International Financial Reporting Standards (IFRS) and U.S. Generally Accepted Accounting Principles (GAAP), leases that are classified as "capital" or "finance" leases are accounted for as

a sale and included on the tenant's balance sheet. Leases classified as "operating" leases are not recorded as assets or liabilities on a tenant's balance sheet. These models have been criticized for failing to provide a faithful representation of leasing transactions, as they omit relevant information about rights and obligations that would otherwise meet the definitions of "assets" and "liabilities."

The Exposure Draft generally maintains the positions released by FASB in its preliminary statement of May 2009 and establishes a single method of lease accounting that would require tenants to list nearly all leases on their balance sheet as a "right of use" asset and as a corresponding "future lease payment" liability. In addition, tenants would be required to document the lease value or rent obligation over the entire lease term, including renewal options. Tenants most affected are those with a significant portfolio of assets held under operating leases. Currently, US GAAP and IFRS account for lease payments arising from operating leases by recognizing them in the period in which they occur.

Placing the entire lease obligation on the balance sheet, resulting in a negative pull on corporate earnings, will dramatically affect companies' perceived financial performance. The long-term effects of this change in lease accounting are still unknown. Many industry experts are predicting that companies will seek short-term leases or favor ownership over leasing, to avoid the consequences of this new accounting methodology. In addition, we are advising companies facing the challenge of meeting these new requirements to assess the appropriateness of their existing lease administration systems and to make sure that their administration systems will accommodate the new accounting requirements.

ALTA Revises Its Land Title Survey Standards

The American Land Title Association (ALTA) and American Congress on Surveying and Mapping (ACSM) have adopted new Minimum Standard Detail Requirements for ALTA/ACSM Land Title Survey (the "Standards"). On February 23, 2011, the new "2011 Standards" will become effective. The changes to the Standards mark the first major rewrite since they were initially adopted by ALTA and ACSM in 1962. While many of the revisions are limited to reorganization and wording, there are a few notable revisions and additions to the prior Standards.

- The sections of the 2011 Standards now follow a different logical path and include a chronology of the client/surveyor procedures for procuring and providing an ALTA/ACSM survey.

- For the first time, the Standards define what constitutes an ALTA/ACSM Land Title Survey. The Standards spell out the particular requirements a surveyor must follow for on-site fieldwork, the preparation of a plat or map, and the completion of any optional information requested from Table A. In addition to the foregoing, an ALTA/ACSM survey must also include the certification specified in the 2011 Standards.

- There has been a noteworthy addition to the standard of care to be exercised by surveyors, with ALTA and ACSM recognizing that "prudent surveyors" must abide by unwritten local, state and/or regional standards of care, not simply those described in the Standards themselves.

- The list of documents required to be provided to the surveyor has been expanded to include the most recent title commitment, the current record descriptions of adjoining properties, and any documents necessary to determine the relationship between senior and junior encumbrances where gaps and overlaps are identified.

- Two sections regarding easements affecting the surveyed property were added to the 2011 Standards, which clarify and delineate how surveyors must describe easements (e.g., showing the width and recording information and/or providing additional notes).

- Surveyors are provided with additional guidance on nonstandard types of properties, such as marinas, campgrounds, trailer parks and

leased areas, since these properties may present issues beyond those normally encountered on a more common ALTA/ACSM survey.

Table A, which sets forth optional survey responsibilities and specifications that may be required by clients, has been modified. As with the Standards in general, many of the changes involved rewording and clarification. More significant is the fact that some optional items under the prior Standards will be mandatory under the 2011 Standards. For example, all ALTA/ACSM surveys conducted after February 23, 2011, must include (i) a vicinity map showing the surveyed property in reference to nearby highways or major street intersections; (ii) visible evidence of physical access to abutting public ways; and (iii) evidence of access to and from waters adjoining the surveyed property, such as paths, slips, launches, piers and docks.

In addition, several new items have been added to Table A. For example, if requested, the surveyor must now (i) disclose the location of wetland areas; and/or (ii) show the location of improvements within any off-site easements benefiting the surveyed property. In addition, another new item attracting attention would allow the client to require that the surveyor obtain professional liability insurance for the survey project, to be effective throughout the contract term. One would expect that selecting this optional item could result in a significant increase in the price if a surveyor does not already carry this type of insurance. Many surveyors have objected to the addition of professional liability insurance as an ALTA/ACSM item. They have argued

that insurance should be an issue between the surveyor and client for the contract, not part of the survey requirements.

While there are few significant changes in the 2011 Standards, those ordering an ALTA/ACSM survey should be aware of them, especially the increased optional requirements provided in Table A. Survey clients should not only find the additional details and qualifying sentences, along with the changes in wording, helpful to their understanding of the product they are obtaining, but also find that the resulting survey will permit them to obtain a more comprehensive understanding of the property itself. Clients may also find it helpful to discuss these changes and their potential impact on title insurance policies with a member of our Real Estate Practice Group before ordering surveys subject to the 2011 Standards.

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