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NJ Redevelopment Projects Face Foreclosure

As open space for new development continued to diminish across New Jersey due to its dense population and seemingly endless development and expanding preservation efforts, redevelopment became a popular tool to implement smart growth over the past decade. With the commercial foreclosure rate rising, however, a number of lenders are now faced with the prospect of foreclosing on these redevelopment projects. There are numerous legal and practical issues that a lender should consider when a loan on a redevelopment project goes into default.

By Dean E. Loventhal

The borrower, as the redeveloper, may be in default under the redevelopment agreement with the municipality or redevelopment agency. However, under the agreement, lenders should have an opportunity to cure any defaults. Without this provision, the municipality might de-designate the redeveloper with respect to incomplete phases of the project, take back property within the project area or terminate pending condemnation proceedings.

A redevelopment agreement will typically permit the transfer to a mortgagee, but will likely place conditions, such as consent of the municipality, on any subsequent transfer. In addition to customary lender protections, such as notice and cure rights, the rights of the lender or any subsequent transferee to complete the project must be examined.

With the use of eminent domain for redevelopment in question after Gallenthin v. Borough of Paulsboro, lenders should note that assembling all of the property for purposes of a project may not occur as originally contemplated. Redevelopment designations utilized to justify eminent domain in the early stages of a project, which were relied upon by municipalities, redevelopers and lenders alike, may now be susceptible to challenge years later. Moreover, municipalities across New Jersey will be more reluctant to use the power of eminent domain to acquire additional parcels necessary to complete a redevelopment project, potentially leaving the value of the lender's collateral at risk.

Many redevelopment projects utilized public financing. Based on the state's tax exemption and abatement laws, these programs are intended to run to the benefit of a foreclosing lender, but certain steps may be necessary to keep the benefits intact. For example, if the redeveloper qualified for tax abatements under the Long Term Tax Exemption Law, a foreclosing lender will need to take title to the property in the name of an "urban renewal entity" that satisfies a number of requirements in order to reap the benefits of the program.

During the course of a foreclosure, a lender may want to have discussions with the municipality in order to facilitate an orderly transition of the property. In some instances, however, a lender may decide to wait until a final judgment has been entered before initiating any dialogue with the municipality in order to avoid potential claims of lender liability or tortuous interference. In exercising its remedies in a redevelopment project, and structuring future deals, lenders must examine all potential pitfalls.

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