



IN YOUR COMMUNITY

Air Rights Issues

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Introduction

The Portland HUD Office has approved and participated in three air rights projects: Westshore Apartments, which is a risk-sharing project underwritten by the State of Oregon with a mortgage insured by HUD and the State; the Alberta Simmons Plaza, a HUD Capital Advance Project, underwritten and financed by HUD; and the Laurel Parc complex, consisting of a 221d4 independent living facility and a 232 assisted living facility, all housed in one building. While this discussion focuses on FHA processing concerns, similar issues will present themselves no matter what the form of financing.

Air Rights Defined

An “air rights” case involves the conveyance of fee simple title to a three dimensional space located at a precisely defined location. Most likely it is in the air, but it might just as well be underground, on the ground, or partially above and partially below ground.

Due Diligence, including Title, Liens, Encumbrances, Encroachments and Environmental

Like any real estate development case, one must start with due diligence. At this initial stage, it is assumed that the three dimensional space has not been severed from the original fee simple title. Due diligence involves determining who or what owns title to the property; and what liens or encumbrances or encroachments burden the property. The usual Phase I/II environmental study must be done as the rules providing for liability for owners and operators would presumably apply to subsequent owners and operators of air rights. The requirements of NEPA must be determined and followed.



Westshore Apartments: HUD/Oregon Risk-Sharing Project in a “One-Unit Condo”

Air Rights Not Understood By All Real Estate Professionals

Although the original title officer stated that his company did not do “air rights” titles, a quick conversation with title company counsel confirmed that the company indeed did and does “air rights” cases. The point is that the concept may be foreign even to real estate professionals. In the case of the Alberta Simmons Plaza, the developer determined early that most persons, even persons active in real estate development, are not familiar with or comfortable with the concept of air rights. On the other hand, everyone thinks they know what condominiums are. Since an air rights project can be contained within a one-unit condominium, and since the State of Oregon has an efficient system for creating one-unit condominiums, the developer planned from the outset to create a one-unit condo in the air space in order to facilitate understanding of the nature of the project.

Basic Areas and Easements

The developer, the architect, and the surveyor must then conceptualize the air space to be used. The air space will include the basic area which will be owned in fee simple, where the primary structure will be constructed; and the supporting structure which will probably be in the nature of an easement, which will provide for physical support, utilities, ingress and egress, garbage chute, etc. The basic air rights area should include cantilevered or overhanging structures like decks or fire escapes. The easement area might include parking space and must include access to the street. The developer should restrict development of space above its space, which theoretically will remain the property of the owner of the land.

Partition Restrictions and Sequencing

The developer must determine whether state or local statutes, ordinances, or administrative practices control the process. Most states will have restrictions on partitions that could well be applied to a horizontal partition. At the Alberta Simmons Plaza, the Oregon State Real Estate Agency determined that the condominium application could not be even filed until the supporting platform had been constructed. The parties agreed in that event to file the condo application immediately upon completion of the platform. This could be a problem for a party to the transaction who wants all the approvals in hand at closing.

Surveys Required and Legal Descriptions

It is necessary to prepare two surveys.

(1) The *boundary* survey should follow standard procedures, contain the usual certifications, and be accompanied by the Surveyor’s Report. The legal description must be one that the title company concurs in—one cannot be record legal while the other is measured legal. It is appropriate to integrate record legal with measured legal, and most parties seem to like that. The ground survey will disclose non-record rights to the site which could limit the rights of the air rights owner. An old encroaching fence may impart title to property by adverse possession that goes up into the atmosphere and may include an area included in the air rights parcel. A boundary agreement can be used to deal with this problem.

(2) The *air rights* survey should be prepared by a surveyor familiar with condominium surveys. It will *not* follow the ALTA rules, so the surveyor will not want to sign the standard HUD Certificate. It may not be possible to file it until state approval of the condo, and if state approval of the condo is

dependent upon construction of the platform, it will not initially have all the certifications and approvals. In that event, have the surveyor certify that it complies with state condo requirements.

Choice of an Attorney Important

It is important to have an attorney involved who understands real property, titles, and condo laws. To create a condominium in Oregon the Developer is required to file or record a plat, Declaration and Bylaws. The Oregon Condominium Act requires the creation of an owners' association, even though the condo consists of only one unit. The fact that the one unit will contain multiple apartments has *no* significance in the condo approval process. The attorney must understand the interrelationships among these areas or will have to learn them as the project develops. The developer, attorney, surveyor, title company and lender must all have a common conception of how this all fits together if the project is to progress.

The Easement Agreement

The easement agreement will be between the owner of the air rights, or condominium, and the owner of the land. It will set forth rights and obligations of the two parties upon development of the two estates, and will create easements for the benefit of the air rights owner for access, utilities, parking, trash recycling/removal, and other uses related to the land.

The easement agreement itself should identify all needed supporting and facilitating easements, define them as precisely as possible, designate who is responsible for what kind of maintenance, and address sharing of costs. One may include restrictions upon use of the commercial space to prevent activities which would interfere with the enjoyment of the residential area by its residents. The architect and surveyor will probably say that the exact location of the support structures and easements for access and utilities cannot be determined until construction is complete! Therefore, the easement agreement must be sufficiently flexible that it will accommodate minor changes in the locations and allow construction to proceed smoothly.

The Title Policy

The title policy should insure legal title to the air rights and the supporting easements—that is, Schedule A should include the legal description of the air space together with the legal descriptions of the easements.

Title should be free of earth-bound encumbrances. That means, if the fee title is initially subject to a mortgage, there should be a partial release of the mortgage, which describes the air space and easements.

Alternately, a subordination agreement can be obtained, subordinating other liens to the development mortgage, but then the subordinated liens remain on the title.

The Remaining Parcel

When the severance is complete, the legal description of the ground reads: Blackacre, except for [air space together with easements]—brackets are intended to emphasize that the air space and the

easements are inseparable. A subsequent lien on the ground that does not except the air probably slanders the title to the air rights and should therefore be avoided.

HUD Handbooks

If the project is funded with HUD Capital Advance money, or if a mortgage is to have HUD insurance, HUD Handbooks apply and provide guidance on the use of air rights. HB4465.1 Valuation, has a chapter on the valuation of air rights. HB4430.1 REV-1, Initial Closing for Project Mortgages, requires several actions (paragraphs 1-10 and 1-12), which are discussed in this paper. Air rights are discussed in the MAP Guidebook 2011, REV-1 at paragraph 11.5 A; and in the 2011 MF Closing Guide at paragraphs 3.2 A, C, and E. The old requirement that the platform be constructed before initial closing has not been carried forward in the new MAP Guide or Closing Guide.

Coordination of Construction Schedules

Because the air rights are (or are to be) owned by a party other than the owner of the ground then a clear, enforceable agreement must be made between the parties that the owner and developer of the facilities on the ground (in most cases commercial facilities) will adhere to an agreed construction schedule that allows construction of the facilities in the air (in most cases residential units) on time and in the proper sequence.