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What Is a Rent-Ready Credit in Multifamily Real Estate?

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A rent-ready credit is a legal provision commonly included in a multifamily real estate purchase agreement that allows a buyer to recover turnover costs at closing. The credit is used to cover the costs needed to make vacant units ready for occupancy.

While often mistakenly considered a buyer-friendly provision, a rent-ready credit is a practical compromise when buying or selling an operating multifamily property. Conflict can arise when a buyer wants each unit in turn-key condition on the closing date, while the seller prefers to continue operating the property in its ordinary course. A rent-ready credit resolves these conflicting positions by giving the buyer upfront capital to turnover vacant units along with control over the means and methods of turnover. Conversely, the seller can sell the property “as is” and continue to operate in its ordinary course.

When Should Buyers and Sellers Use a Rent-Ready Credit?

Rent-ready credits are helpful when a buyer is acquiring a stabilized multifamily property and wants to control the unit turnover process. Offering this credit early in a transaction can ease concerns about vacancy rates and unit condition, which can reduce low purchase offers from cautious buyers.

However, the credit is not appropriate in every multifamily transaction. The credit is generally not appropriate in situations where the condition of the property is reflected in the purchase price, such as a buyer planning a value-add or buy, rehab, rent, refinance, repeat (BRRRR) strategy. Because the buyer will presumably renovate vacant units before placing them in the marketplace, the buyer is impliedly accounting for turnover cost in its renovation budget.

The credit is also generally not appropriate if the property has low turnover. A seller with tenants keeping multi-year tenancies is in a good position to oppose a rent-ready credit. In this situation, there may not be enough vacant units to justify the hassle of effectuating the credit at closing. A few vacant units may also be commonplace in the particular submarket, so these turnover costs are more like general property management costs.

Additionally, special attention should be paid by the buyer to lender requirements. Loans with Fannie Mae (Fannie), Freddie Mac (Freddie), the U.S. Department of Housing and Urban Development’s (HUD) Federal Housing Administration (FHA) and the U.S. Department of Veterans Affairs (VA) may have limitations on the amount of seller concessions in a transaction. If seller concessions are extensive, a buyer may need to implement additional tools, such as an escrow holdback, or forfeit all or a portion of the rent-ready credit to keep its financing.

Legal Considerations for Rent-Ready Credits

Once the parties have determined that a rent-ready credit is appropriate, they must then agree on three points:

1. the condition of the units

2. which units are eligible to receive a credit
3. the amount of the credit provided

1. Defining Rent-Ready Condition

First, it is good practice to clearly define “rent-ready” condition in the purchase agreement because the term can vary significantly between transactions. At minimum, “rent-ready” condition means that a unit complies with all applicable laws, including local housing codes, so that it can be leased immediately. However, buyers will often want to include items that are standard in similarly situated units even if those items are not required by law. Often, this will include a deep clean, fresh paint and finishings that are the same quality as occupied units.

However, the practical realities of operating a multifamily property demonstrate the importance of a clear definition. An unsightly stain may persist even with the most experienced cleaners. Wall impacts may persist even after a fresh coat of spackle and paint. For appliances, quality can vary greatly. A seller may argue that any functional appliance is in “rent ready” condition, but a buyer may expect that the seller continue to upgrade a unit’s finishings if the seller has historically re-finished vacant units. For “luxury” properties, a buyer may also expect that the unit’s finishings meet specific standards or are compatible with the unit’s aesthetics. The definition will vary between transactions, but buyers and sellers can avoid unnecessary conflict by paying particular attention to “rent-ready” standards.

2. Identifying Eligible Units

Second, buyers and sellers should identify which units are eligible for the rent-ready credit. Most buyers will request that the credit apply to all vacant units, and sellers commonly make exceptions to this standard. The first exception may be made for non-residential units, such as the management office, laundry rooms, hallways and other non-revenue generating spaces. Repair and maintenance costs for these areas are more properly categorized as general property management matters and not as a matter of unit turnover. Garage space, especially if leased separately, may also be included here.

The second exception may apply to residential units that have been converted into maintenance shops, storage spaces, showrooms or other non-residential uses. If the unit is not currently intended for a tenant, turnover costs turn into capital expenditures.

The third exception may apply when there are more vacant units than the market is likely to absorb in the foreseeable future. If there is no reasonable expectation that every vacant unit could be leased on the spot, it makes less economic sense to turnover a unit only for it to continue to sit vacant.

The fourth exception may apply for units that become vacant within a reasonable proximity to the closing date. Sellers require time to turnover units, and, as expectations increase, the number of days included in this exception may also increase.

3. Determining the Credit Amount

Finally, the credit amount is typically expressed as a fixed dollar amount on a per-unit basis. This means that any unit determined not to be in rent-ready condition is eligible for the credit, regardless of how far or close the unit is to the rent-ready condition.

There is no set standard when determining the dollar amount of the credit, but it is often a number reasonably related to the cost to turnover the unit. A buyer will often rely on its past experience and preliminary diligence when determining the credit. The seller will often rely on prior operating costs when determining the credit. In rare cases, a general contractor may inspect the units to provide an estimate. However, both parties have an interest in keeping the number small enough to avoid a significant cost on either party should a disagreement arise.

The total credit amount is typically determined following a final walk-through inspection. A seller will likely be motivated to remedy the close calls, and a buyer will often look to other provisions of the purchase agreement when material issues are identified. Reasonable disagreement is still possible, and parties may coordinate a final walk-through inspection with a neutral inspector. Experienced advice is essential for the successful implementation of a rent-ready credit.

Need Assistance with a Multifamily Property?

Gould & Ratner represents apartment owners, operators and managers in the financing, purchase, operation and sale of multifamily property. Our team can help you draft or review purchase agreements, navigate lender limitations, resolve disputes over unit conditions and protect your investment.

If you need legal guidance for your next multifamily transaction, please contact a multifamily real estate attorney in [Gould & Ratner's Real Estate Practice](#).