BUYING AND OWNING TEXAS LAND

10 CRITICAL MISTAKES TO AVOID

JAMES WALLACE
TEXAS LEGACY RANCHES

texaslegacyranches.com
512-585-6019
jw@texaslegacyranches.com

1. Inadequate due diligence *before* contract negotiations or a decision to pass.

Not spending enough time on the ground to see all or most of a property's attributes (positive or negative).

Sometimes brokers and buyers will do only a "drive-by" tour of a ranch, and then either pass on that property or jump right into contract negotiations. Certainly, if a prime property hits the market priced below fair value, acting quickly makes sense. But that's rarely the case, and there is almost always time to give a property a full look, even (and especially) larger ranches.

For larger properties and properties with lots of tree cover and/or topographical variances, a quick drive around the front and easily accessible parts of the ranch is not adequate. You'll likely miss important features – or potential problems.

Large ranches can sit on the market because the listing broker or buyers didn't take the time or effort to explore the entire property. Getting to back areas, spending hours on the ground, tromping through brush, woods, and down creeks, can result in discovering "hidden assets" that other prospective buyers miss. These hidden assets included springs, creek branches, waterfalls, scenic vistas, rock formations, home sites, and wildlife – none of which were part of the standard tour or marketing. Take the time to explore fully the properties you're interested in, and it may pay off with a "hidden-assets" ranch at price similar to ranches without those assets.

On the downside, failing to see all parts of a property may result in missing trash dumps, fences down or in disrepair, signs of trespassing or poaching, misrepresented "live water" or "strong springs," oak wilt, areas of the property that are significantly inferior to the guided-tour areas, and/or any number of other facts important to a buy/price or pass decision.

Not checking on groundwater, minerals, or other key factors.

Prospective buyers should find out about groundwater in the area before spending too much time or money. Is there an adequate aquifer? How strong are the wells? Great groundwater is gold, and the absence of it can really adversely impact land values and use. [See #10 below – "Missed opportunities for value enhancement."] If groundwater is poor, does the property have access to a water supply, what's the cost, and will it be sufficient for the intended uses?

If control of the surface is important to a buyer (it almost always is), the buyer should have some idea about the minerals on a property. If the area is not within a known production region or play, often the minerals (all or part) are still intact. Prospective buyers should try to obtain as much of the mineral estate as possible in those areas, as the price premium is close to zero, and it affords surface protection (as well as an economic flyer should a new play be discovered or new technology be deployed to access minerals previously unrecoverable (witness the shale oil/gas fracking boom)).

Details can come later (with title review and option-period due diligence), but have some idea early-on about the big-ticket items that impact use and value.

2. Failing to revise and supplement the TREC Farm and Ranch Contract.

Many buyers and brokers simply fill in the blanks, sign and submit. This is almost always a mistake - potentially a costly mistake.

The TREC Farm and Ranch Contract is the standard contract used by the majority of non-commercial/non-residential land buyers and sellers. Certainly (at least on larger transactions) a buyer can have an attorney draft a custom contract, but sellers and brokers are instantly at ease with the TREC contract because it has been used so much and

its contents are established and known. The negotiation path is smoother since the starting point is a familiar document. But that doesn't mean just to accept the contract as is. Brokers are prohibited from making substantive changes that would be deemed practicing law. But they should advise their clients to have an attorney review the contract and make appropriate changes.

The TREC contract, while a good form overall, is deficient in several areas, including provisions pertaining to title objection and waiver deadlines, closing date, closing documents, default remedies, seller representations, survey provisions, document production, and some boilerplate items. *Caution note to buyers: under the TREC contract, if the buyer defaults, the seller can force purchase of the property and/or seek any other remedies provided by law; liability extends significantly beyond the earnest money. An option contract is a far better choice for buyers.*

These items can easily be addressed in an addendum. They will typically be negotiated by the parties, but pushback against any changes is rare. Most sellers want to work with qualified buyers, and they realize (particularly on larger deals) that most of these buyers are sophisticated and will have counsel.

Sellers, of course, also benefit from representation and seller-oriented revisions to the standard TREC contract. *Caution note to sellers: certain notices to purchasers beyond those in the TREC contract may be required (and expose the seller to liability if not given).*

Items that can be covered in an addendum include representations about agricultural or wildlife valuations and filings, representations about environmental and governmental matters, indemnity for pre-closing claims and liabilities, unrecorded easements or leases, details about any mineral or other reservations, details on personal property included or excluded, details about what the deed will contain, survey and title commitment requirements, due-diligence documents to be delivered to the buyer, environmental site assessments, defining what constitutes a default, details on drafting and reviewing closing documents, and supplementing/clarifying various provisions in the base contract.

Generally, the more detail and clarity, the less chance of a misunderstanding – and litigation. This approach benefits both parties.

3. Failing to review and scrub title.

Catch value-demolishing problems before it's too late.

One of the most common and critical mistakes many buyers make is neglecting the title review. Once a deal is in escrow, the title company issues a title commitment and delivers legible copies of all the title exceptions listed in Schedule B. NOTE: some title companies inexplicably fail to deliver copies of the exceptions. Be sure your title company is responsible and responsive. Always obtain and review (and have an attorney review) all Schedule B exceptions promptly. Some title companies in larger cities provide links in Schedule B to digital copies of the exception documents.

What could happen if you fail to review title thoroughly? Here are some examples:

- Reservations/conveyances of all or part of the mineral estate and/or portions of the surface estate. In one recent deal, the title company missed a reservation of all the rock on a ranch property. The documents were listed in the seller's title policy, issued by a different title company. Ask for the seller's title policy (otherwise you will not get it). This unusual reservation meant that third parties could, if desired, mine surface rock and essentially destroy the ranch from the standpoint of a recreational buyer. The property also had iron-ore reservations, in an area of semi-active mining. Many buyers would have missed these exceptions, only to wake up one morning to the sound of heavy equipment outside the cabin window. With respect to oil and gas, the mineral estate is the dominant estate, so buyers should be aware of the potential for exploration and development in the area, and understand that (absent an agreement to the contrary) the mineral owner and lessee can use as much of the surface as reasonably necessary to explore for, produce, and remove the minerals. The mineral owner's or lessee's rights regarding surface use are much broader than most landowners

realize. Understand this area of the law before you contract for a property, or at least before expiration of your option period.

- The seller tells you he owns half the minerals and will convey half of what he owns to you. Reviewing the title documents reveals the seller only has a ¼ mineral interest and that an outstanding royalty interest further impacts the seller's interest.

- You miss the fact that two utility companies have blanket electric or pipeline easements across the entire property. Two years later, that idyllic pasture surrounded by woods and next to a scenic pond becomes ground zero for a main transmission line or just a stone's throw away from a high-pressure gas pipeline being installed.

  NOTE: check the specs on any pipelines crossing (or that could later cross, under the terms of existing easements) the property you want to buy. The blast radius ("Calculated Hazard" radius, or "High Consequence Area") of a 36-inch pipeline operating at 1,100 psi is 825 feet. Build in an extra cushion of safety, and you're at 1,000 feet. Pipeline explosions are rare, but deadly; who wants to take the chance? A 1,000-foot setback could severely impact the use of a smaller ranch. What is the value of a house built within the blast zone? How many buyers know to make this valuation adjustment?

  NOTE: pre-existing pipeline easements often allow multiple pipelines and/or do not limit the pipelines to a specific size/pressure, so even if an existing pipeline is small/low pressure, be aware the situation could change. The same is true for electric-line easements.

- You miss an access easement in favor of ("appurtenant to") the ranch next door. It was on page three of a four-page, 1972 deed five conveyances back in the chain of title. The easement is not apparent on the ground (so no worries, right?), but per the metes and bounds in the recorded document it bi-sects the ranch you had planned to high fence (or that is already high-fenced) for a premium hunting ranch. Or even worse, the access easement affects the entire property (e.g., a blanket easement). The ranch benefitting from the access easement is divided into ranchettes after you close on your property. One day you encounter

regular vehicular traffic disrupting your best deer-hunting areas and/or your headquarters compound. Yikes.

Throw out the trash.

You can (and likely will) get stuck with a ton of garbage on your title policy if you don't review each exception for applicability. Many (if not most) title companies throw everything plus the kitchen sink onto the title commitment. If they see anything of record that references the same survey abstract(s) as the subject property, on it goes, regardless of actual applicability. These garbage exceptions cloud title by making the property appear "hairy" or "messy" (not legal terms, but appropriately descriptive). When time comes to resell, these garbage exceptions can deter a buyer, or at least cause delay, stress, and expense.

It is far better to keep them off your title commitment and policy in the first place. Be detailed, aggressive, and stubborn here. If the title company can't show you how and why an exception is valid, subsisting, and applicable to the land you are buying, they must remove it.

Even if resale is not on the horizon, having inapplicable exceptions on your title policy and deed can raise questions and cause undue work and stress down the road. Cleaning up title adds value. On large properties, that value can reach six figures. It's not unusual for six or more pages ("Items aaa - zzz") of exceptions to be whittled down to one or two pages.

NOTE: Many, if not most, title companies insist on inserting an exception for any and all minerals (in Schedule B), or simply excluding the mineral estate from the insured property (in Schedule A). Be persistent and adamant in having the title company delete a global exception or exclusion of minerals; have it only list specific reservations and conveyances in the chain of title. They will whine. They will say they can't. They will say a minerals search is the province of landmen, so go hire one. *Au contraire, monsieur*. An initial reservation (or conveyance) of a mineral or royalty interest is no different from a reservation (or conveyance) of an access easement or any other title matter. You care not what happened to the mineral interest once reserved or conveyed (that is the landman's or examining attorney's job, working on behalf of

an oil and gas company desiring to lease or buy minerals). All you want to know is what minerals remain with the surface estate. If the title company still refuses, consider changing title companies (find one whose plant goes back over 100 years).

A lean, clean title policy beats messy title by a country mile.

4. Failing to obtain and review a current land-title survey.

Some buyers simply accept an old survey, usually outdated. The title company will include a blanket survey exception in the title commitment and policy, meaning the buyer takes subject to anything a current survey might reveal. Like what?

- Fences way off the boundary line.
- Boundary conflicts (per the recorded adjoinder deeds).
- Unrecorded and apparent access roads or pipelines.
- Improvement encroachments and protrusions.
- Material acreage discrepancies.
- Ingress/egress problems.

Always get a current survey, or have a relatively-recent survey updated and certified to the buyer. Make sure it ties into the title commitment as a land-title survey. The plat should identify inapplicable or unlocatable exceptions. Make sure the survey plat matches the metes and bounds legal description to be used in the deed (invariably, a good review catches mistakes).

5. Failing to obtain a Phase I Environment Site Assessment.

Most farm and ranch buyers don't get one. In many cases, a reasonable case can be made not to get one. Smaller, "clean" ranches (e.g. no

apparent past or existing uses that could give rise to environmental contamination) rarely present problems. Larger ranches and high-value acquisitions, however, don't get as easy a pass. Why? The cost-to-value ratio is skewed heavily in favor of getting a Phase I ESA. If a buyer is spending $2,000,000 to $5,000,000+ on a ranch, what's another $2,000+/- for a Phase I ESA, especially since it acts as both peace-of-mind relief (reasonable due diligence, nothing bad found) and legal relief (a qualifying ESA can give help a buyer achieve the status of a bona fide prospective purchaser with accompanying protections from liability for pre-existing contamination). Since the liability can be large if an environment condition is discovered, the benefits of conducting "all appropriate inquiries" almost always outweigh the cost.

If the property has oil wells, pipelines, trash dumps, any industrial/farm equipment areas, signs of ground stains, discolored water, or similar red flags, strongly consider a Phase I ESA as an indispensable part of your due diligence. Be sure to allow at least 30 days in the contract. The ESA can be done concurrently with the buyer's option period. Be sure to include language in the contract requiring the seller's cooperation. And don't forget to conduct additional environmental due diligence with respect to both significant existing structures (examples: asbestos, lead, radon, mold) and natural conditions (examples: wetlands, endangered species).

6. Accepting the seller's or title company's closing documents without meaningful review or negotiation.

This mistake is common in residential transactions, because the parties are typically unrepresented by counsel and have limited knowledge of what the documents should say. In larger land deals, however, there really is no excuse for not reviewing/controlling and negotiating the closing documents. There are always gaps to fill in – content not fleshed out in the contract. And the parties should always make sure the closing documents exactly match and incorporate the terms that are spelled out in the contract. What if, for example, a seller did not reserve minerals

in the contract, but the deed signed at closing contained a reservation? That is an obvious mistake, and if the buyer delays in seeking reformation, he may be out of luck. How costly could that mistake end up being in an active mineral area? If the contract contains a partial reservation, make sure the deed accurately describes the split; it's not hard when drafting mineral reservations and conveyances to mess up the parties' intent, particularly when other mineral interests are already severed and held by third parties.

Other mistakes include not checking the settlement statement charges, credits, and prorations against the contract and against the actual numbers, omitting a document (for example, a bill of sale for personal property included in the sale), including blanket-exception language in the deed when the contract only permits specific items, and botching the legal descriptions or other attachments.

7. Failing to obtain a final title commitment and/or check the title policy.

Most buyers skim over the title commitment and title documents. Not only should these documents be scrutinized and scrubbed, as discussed earlier, the revised title commitment should be down dated to the closing date, and all Schedule C items notated by the title company as deleted/satisfied. Schedule C items are those things that have to happen before the title company is obligated to issue a policy (or issue it without including the items as exceptions). They include items such as delivery of the deed, payment of the purchase price, release of liens, delivery of affidavits, and any specific items unique to the deal at hand. When the buyer releases the purchase price from escrow, he should obtain assurance that all the outs are gone – that the title company indeed will issue the policy with only the agreed Schedule B items. This assurance is achieved via the Schedule C deletion/satisfaction procedure described above and by a down date of the commitment at closing. The down date removes any gap that may otherwise exist between the date of the prior commitment and the date of closing. The commitment form (in Schedule C) excepts from coverage any matters arising or filed after the effective date of the commitment. Buyers don't want gaps in

coverage, since funds have been disbursed. Some title companies resist the down date and Schedule C deletion, but persistence almost always pays off here.

The title policy should issue within 30 days after closing. Be sure to follow up if not received within this time frame. Check the policy against the final title commitment. If the policy contains additional exceptions or otherwise does not match the final title commitment or include agreed endorsements, have the title company re-issue the policy as corrected.

8. Post-closing omissions and neglect.

After the deal is closed, the fun and enjoyment of the ranch begins. But many buyers neglect operational details. Ranches require maintenance and attention to operations. 90% of the time you spend on the property may be the fun stuff, but 10% requires attention to details and follow up.

Here are two examples.

The property will have some type of ag/timber/wildlife valuation for tax purposes. These valuations keep property taxes at a minimum. Without them, the property would be taxed at market value, resulting in big tax bills. Don't forget to file (in the county appraisal district office) for the continuation of the existing valuation in the buyer's name, no later than April of the year following acquisition. Some buyers simply forget to file the application on a timely basis. While many appraisal districts are amenable to working with landowners and fixing mistakes, some may be tougher. Don't take the chance. The rollback tax penalties are severe if a "change in use" is deemed to have occurred.

A year or more has passed since your purchase. You are ready to build your dream lodge on the ranch. You don't even think about the closing documents or survey, much less any notion of reviewing them. You excitedly find the ideal home site. You spend a small fortune building your house, be it a barndominium, cabin, or lodge. A few months later

you notice a marker on the property, then another. Or you get a knock on the door. Turns out, you built the improvements within a gas pipeline right-of-way. The recorded easement is in your file, as is the survey plat depicting the easement. The underground pipeline runs under the middle of your new lodge. Oops.

Before improving your land with permanent structures, check your title documents and survey plat. Check the Texas Railroad Commission's online GIS maps. Call 811. Locate all easements - pipeline, access, or other. Don't dig or build until you are sure your proposed improvements are outside all applicable ROW easements. Be an active owner. Verify the facts yourself and save the heartache and stress and fix-it money. If your property has or could later have (per existing easement(s)) one or more large/high pressure gas pipelines, build outside the blast radius, not just the easement boundaries.

9. Ongoing ownership mistakes.

Being an active, hands-on owner can prevent many mistakes, but even involved owners may face situations that seem innocuous but in reality could result in serious value diminution.

Here's one example. Recently a ranch owner called me with a concern about an electric co-op pressing him with some urgency to sign what the representative called the co-op's "standard-form" right-of-way agreement, to allow a 3-phase power line to be installed along the boundary of his property. He knew enough to know what he didn't know. Turns out, the "standard form" was a blanket easement over the entire property that would have allowed any type electric transmission system, or multiple systems, to be installed, upgraded, added to, or changed, with no limitations. Anyone who has seen those steel-tower transmission lines knows they severely impact valuations. Buyers don't want them, because they ruin the aesthetics of an otherwise picturesque property. On very large ranches, this is not as serious a matter, but on mid-size and smaller properties it can be a killer. In the case mentioned above, every other landowner along the route had simply signed the co-op's standard agreement. When contacted, the co-op representative

was amenable to tying the easement down to a specific route for specific wooden poles with no expansion permitted and with other landowner protections.

Another example, relating to being an active, onsite manager or having someone else take on this responsibility:

In this case, a high-fenced ranch with enhanced-genetics deer (brought in several years earlier to increase antler and herd quality) had portions of the fence line down for an extended time due to flooding and falling trees. The new owner had not yet started a feeding program, so nothing was holding the deer onsite. A game survey and wildlife-management plan are pending, but the bet is that a significant portion of the enhanced-genetics deer population has wandered offsite.

Another critical reason for checking the perimeter regularly is to catch signs of trespass and poaching.

If cattle are on a farm or ranch, checking fences is just as critical. One client had a ranch that fronted a curved section of farm-to-market road. Every six to nine months a vehicle would miss the turn and crash into the perimeter fence. Make sure the county sheriff's office has your and your manager's cell or other numbers so they can alert you immediately of downed fences and escaped livestock.

10. Missed opportunities for value enhancement.

Become knowledgeable about the various ways your land can be enhanced through good stewardship and land management. Even inferior-quality ranches can be transformed. Even dry ranches can sometimes be turned into live-water jewels.

My best example to illustrate this point is the Selah Ranch in Blanco County, Texas, covering about 5,000 acres. At the time the ranch was purchased (in the 1970s), the extension agent told the buyer it was the worst piece of ground in the county – dry, cedar-choked, and rocky with poor topsoil. The owner brought in large amounts of native grasses and

cleared much of the cedar. Within a few years, springs popped up. The pastures had knee-high grass. Ponds and small lakes were created. Exotics were brought in. The ranch is a showplace for stewardship and good land management.

The grasses allowed the rainfall to soak slowly into the ground and fill the aquifer. Removing much of the water-hogging cedar contributed to the rejuvenation. The ranch has a fascinating "rainfall machine" to illustrate how this transformation happened. The machine has a cedar-and-rocky-ground side and a grasses-and-dirt side. When equal amounts of water (simulating rainfall) are poured into each side, about 90% of the water on the cedar/rocky side very quickly runs off and never soaks into the ground, but on the grassy/dirt side about 90% of the water is captured by the grass blades and soaks into the ground. The captured rainwater was the life spring for the ranch's transformation from dry and dusty to lush and watered. Indeed, in this case, live-water was developed. The "before" and "after" pictures are remarkable.

Learn about your property's natural resources. Seek help from your local extension and conservation offices. Research grasses. Find out about cost-sharing conservation programs. Understand your groundwater. Look for places to impound water. Figure out how best to maximize the wildlife and how to manage the game. If wildlife enhancement is part of your plan (over 90% of all Texas ranches are purchased for recreation, including hunting and wildlife as a major component), engage a wildlife biologist early-on, get a plan, implement the plan, and stay active in maintaining and improving it. The payoff will be immense, both in your own enjoyment and if and when you want to sell. A well-managed game ranch with a top-category MLDP (Managed Lands Deer Permit) can have a 20% valuation premium over similar ranches without MLDPs.

I hope understanding these 10 common mistakes in buying and owning land helps your land transaction be trouble-free and your ownership be both enjoyable and profitable. This list is by no means exhaustive, and we all have "war stories." The key is to be engaged and seek the advice of experts when needed. The goal of this pdf is help land buyers and

owners recognize pitfalls and situations in which extra due diligence and timely advice make sense.

May you and your family enjoy many beautiful sunrises and sunsets on your special patch of Texas land.

- James Wallace

512-585-6019
jw@texaslegacyranches.com