

# New Jersey Law Journal

VOL. CLXXXVIII—NO.13—INDEX 1180

JUNE 25, 2007

ESTABLISHED 1878

## Real Estate Title Insurance & Construction Law

JUNE 25, 2007 ALM

### When in Doubt, Disclose

Practical considerations for drafting and negotiating the commercial contract

By Aaron Y. Strauss

**F**or seller's counsel, there are five important axioms to keep in mind when negotiating a commercial real estate contract: when in doubt, disclose; choose your battles wisely; always keep in mind the subject property; strive to understand your client's present market position; and maximize the seller's unique negotiation advantage.

No seller wants to highlight any negative features of their property for fear of losing a possible interested purchaser. However, as seller's counsel, you must temper the seller's desire to market its property with a dose of caution. Failure to disclose certain material facts upon which a purchaser relies to its detriment can ultimately lead to a fraud claim. It is always in the seller's best interest that the purchaser knows what they have bargained for from the beginning of the

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transaction. As a general rule, when in doubt about whether to disclose a material item that may negatively impact the value of the property, err on the side of caution and disclose.

Sophisticated seller's counsel will prod their client with questions to draw out any issues requiring disclosure. For example, has the property been impacted by any significant environmental issues, do any tenants have a right of first refusal or first offer, is the seller presently embroiled in any litigation that could affect his interest in the property? Generally, the more problematic the issue, the greater the amount of treatment should be given in the agreement of sale. However, if a specific report prepared by a third party contains a thorough analysis of the problem, a general reference to such report and its findings in a sentence or two is appropriate. It is important to remember that simply including an "as-is" provision in an agreement of sale does not remove a seller's duty to disclose. Additionally, as a practical matter, devoting proper attention to negative items in the initial stage of the transaction ensures that the purchaser and the purchaser's lender stay on track with their due diligence. No party wants a last-minute discovery which sours the entire transaction two days prior to closing.

Every agreement contains terms which, although essential, are only very rarely of consequence. The most common examples are casualty and condemnation. In a standard agreement with a 60-day due diligence period and closing date within 90 days of execution, the chances of the property burning down or being condemned prior to closing are extremely low. Accordingly, while seller's counsel must prepare the initial draft agreement with standard casualty and condemnation provisions affording protection to a seller, it is not wise for either party to devote significant amounts of energy to negotiating such terms. Instead, focus on negotiating the more critical aspects of the agreement, such as defaults, indemnities, contingencies and representations, among others.

Every property is different, and accordingly, different property-specific form agreements and provisions are required. An agreement for the sale of an office building will likely have a specific provision addressing the issue of gathering tenant estoppels from the numerous tenants — is there a certain percentage of tenants which must deliver estoppels and/or certain estoppels from major tenants that the seller must absolutely obtain and deliver? Is the property vacant land? Perhaps rollback taxes must be considered an adjustment item. Is the property a shopping center? If so, provisions must be included to address common area

maintenance adjustments. If your client is closing on a shopping center in June, for example, and common area maintenance charges are not reconciled under the respective leases until January, the agreement must set forth how to address such post-closing adjustments when actual figures are determined. Is the subject property an industrial site? In such instance the parties will likely heavily negotiate provisions related to compliance with the Industrial Site Remediation Act (ISRA). As you prepare or negotiate the agreement of sale, always envision the type of property in your mind to help sharpen your drafting and negotiation positioning.

Before preparing or negotiating the initial draft agreement, you must strive to understand your client's market position. Keep in mind, however, that market position can often fluctuate dramatically within days, or even minutes, if, for example, other offers are presented during the course of initial negotiations. If the purchaser has some leverage in the initial negotiation stage, the purchaser should attempt to neutralize market conditions by negotiating for a stand-still provision, which requires the seller to abstain from marketing the property to other potential purchasers. In addition to market conditions, you must understand your client's

negotiating and drafting philosophies. Some clients simply want to have adequate protections in place and do not want counsel to heavily negotiate unless absolutely critical. Other clients prefer counsel to take aggressive positions to ensure maximum favorability of contract terms. Of critical importance, however, is that fluctuating market conditions can tame the most aggressive-minded client and embolden the generally passive client to take strong positions. Understanding the present market and keeping the communication lines open with your client ensures that the tenor and scope of your drafting and negotiation positions are appropriate — never over-reaching nor overly compliant.

As seller's counsel, you have the distinct advantage of preparing the initial draft agreement. Keep the seller's representations to an absolute minimum — always let the purchaser request any additional representations they require. Be sure to limit any invasive testing by the purchaser during the due diligence period unless the seller grants prior consent. Of critical importance, be sure to include as exhibits to the agreement actual forms of any closing documents. Chances are that the purchaser will be focused more on the actual terms of the agreement and will

only skim over such seller-prepared exhibits. Use this fact to your advantage. Seller's counsel, therefore, may want to include purchaser-indemnification provisions in the assignment and assumption of leases or bill of sale, and exclude any reciprocal seller-indemnification provisions in such exhibits.

Unless absolutely necessary, never "agree to agree" on any critical terms governing closing or post-closing activities, as provisions addressing future, unascertainable terms are generally unenforceable. If an agreement must be finalized before certain terms are determined, be sure to strictly limit the period in which a final determination of such terms may be made to the due diligence period. For example, in the case of a leaseback of space by the seller from the purchaser after closing, the form of lease which will govern the parties' future relationship should be finalized during initial agreement negotiations. If this is not feasible, however, as an absolute minimum an exhibit in the form of a letter of intent containing the basic business terms of such proposed lease should be annexed to the agreement. As a practical matter, preparing the form closing documents in the initial agreement will save all parties valuable time when preparing for closing. ■