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Peer to Peer 8

Risky Business or Business as Usual – Advanced Issues in Purchase and Sale Agreements

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by:

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With the economy beginning to recover from the recession caused by the pandemic and segments of the retail trade coming back to life, investors are looking at their positions in the market with an eye to the future. Some have determined that they need to be sellers, while others see an opportunity to take advantage of a retail outlook that rewards vision and adaptation to our changing marketplace. Because the evolving retail environment is polarizing more distinctly between strong A-type retail locations and more vulnerable B and C-type retail locations, more than ever buyers tend to be either focused on the income characteristics of a property (an Investment Buyer), or its attributes for redevelopment or repositioning (a Development Buyer). The negotiation of a purchase and sale agreement for these differing types of assets will typically involve all of the same points of contention, but may very well require different approaches to reach resolution depending on the prospective future for the property envisioned by the buyer.

PSA Issues	Seller Position	Buyer Position	Special Considerations and Compromise positions

PSA ISSUES	SELLER POSITION	BUYER POSITION	SPECIAL CONSIDERATIONS AND COMPROMISE POSITIONS
INSPECTION PERIOD	True "free look" is typical. Seller will want earnest money to truly go hard at end of IP and may ask that additional earnest money be deposited at that point. IP typically starts from date of PSA but, if Buyer has been given early access, Seller may want IP to start from then and not from PSA date. Provide for nominal consideration to be paid to Seller if Buyer terminates before end of IP. Frequently, Buyer will ask Seller to make information in Seller's possession or control available to Buyer to assist Buyer with its due diligence. If Seller agrees, Seller will want to say the information is provided as a courtesy to Buyer and is delivered without representation or warranty except as otherwise expressly provided in the PSA. [Practice tip: whenever a buyer is required to deposit additional earnest money, consider adding language that says if they do not do so within a certain number of days a receipt of notice, Seller may terminate the PSA and receive whatever earnest money has previously been delivered under the PSA.]	Buyer will want the agreed inspection period to be a true "free look", allowing buyer to terminate for any or no reason with a full refund of its deposit, perhaps less token consideration for the contract. Buyer may prefer that the inspection period commence on delivery of all required seller diligence deliverables if any of those have not been delivered at the time the PSA is signed. Buyer may request the ability to extend the inspection period either for specific purposes (such as completing the review of 3rd party reports that may be slow coming in) or upon payment of an additional deposit. An extended inspection period may also be advantageous for additional environmental reviews necessitated by Phase I results, and the pursuit of any required governmental determinations that exclude or limit buyer's liability for existing conditions. If any diligence is not complete by the expiration of the inspection period, buyer must either negotiate specific contractual conditions or termination rights based on the results of such diligence or else run the risk that the diligence results are unfavorable, leaving buyer exposed for its earnest money deposit.	This is one of the areas of the purchase agreement where the interests of an Investment Buyer and a Development Buyer may not differ markedly. However, a Development Buyer may require time and cooperation from the Seller in seeking governmental approvals for future development as a condition of the purchase. If the Seller entertains those proposals, which may result in a higher sales price, it may be appropriate to have a separate, and shorter, free look inspection period for property condition due diligence after which the deposit goes hard except if the buyer fails to obtain the government approvals during a longer period designed to accommodate the application and hearing process.
LEASE REVIEW, TENANT AND SHADOW ANCHOR INTERVIEWS	Seller will typically covenant to provide Buyer with copies of all leases and any amendments and guaranties. Seller may not want Buyer to interview tenants or, if Seller permits tenant interviews, Seller may want adequate notice and the right to have a representative present.	Buyer will typically accomplish its lease review and key tenant interviews during its inspection period, as part of the decision regarding whether to "go hard" on its earnest money deposit. .	The Development Buyer will want to be at liberty to discuss planned future changes to the property, especially with tenants or shadow anchors that hold approval rights over changes, and to obtain any necessary third party approvals. If the Seller is retaining any portion of the property, the Development

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			Buyer will want approval of its plans and a covenant to cooperate with further specified future changes.
No Material Adverse Changes as a Condition of Closing	A Seller seeks to lock in the Buyer to close on the transaction as quickly as possible. Toward that end, the Seller will want to incentivize the Buyer not to terminate the agreement once due diligence concludes without the Buyer paying a heavy price for that termination—i.e., the Seller wants the Buyer "hard on the deal" and on their deposit with no termination rights following due diligence. The Seller's position being that the risk of changes to the property occurring after due diligence should be borne by the Buyer.	The Buyer's position will be that it cannot complete a transaction to purchase should there be some material and adverse change in the income or the expenses associated with operating the property following due diligence – this is especially true for the Investment Buyer. The Buyer will argue that it is purchasing a stream of income and any reduction in that stream of income will render the business proposition for the purchase untenable—and, perhaps, un-financeable. The Development Buyer that has not conditioned its purchase on obtaining governmental approvals will also want to address any zoning changes or moratoriums that would preclude or delay its future plans.	Confine a material adverse change termination right to: (1) a lease termination by a "major tenant" [will need a definition of a major tenant—typically, the definition will center on the size in square footage and/or percentage of income of the overall center paid by such major tenant]; (2) a bankruptcy filing by a major tenant and the rejection of the lease in bankruptcy; and/or (3) the cessation of business from the shopping center by a major tenant pursuant to a "go dark" right in the lease.
Irrevocable Commitment by the Title Insurance Company to Insure the Buyer as Owner as a Condition of Closing	A Seller will take the position that the Buyer can arrange such title insurance as it desires prior to expiration of the due diligence period, but that once due diligence is up, absent a material change in the status of title, the Buyer should not have a termination right on account of the title insurer making new or additional requirements that can inhibit the issuance of title insurance coverage as of the date of closing.	A Buyer will take the position that it cannot close the transaction unless it has title insurance coverage as of the moment of closing subject only to those matters approved by the Buyer.	The Buyer should approve of the exceptions to title coverage before the end of the due diligence period and if some new exception arises after due diligence, if its material to ownership or operation of the property, then the Buyer would have a termination right. If caused by the acts or omissions of the Seller, the Seller would be obligated to cause the release of the same prior to closing.
Reliance on Title Insurance for Coverage on Matters Affecting Title	Sellers may want Buyers to rely upon their Title Policies for any claim relating to a breach of a	Buyers want an independent right to make claims relating to a breach of a representation, warranty or covenant	Sellers and Buyer can compromise by requiring Buyer to make a claim first

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	representation, warranty or covenant made by Seller in the Purchase Agreement or Deed, and only have a right to make a claim against Seller once Buyer's remedies under the Title Policy are exhausted.	made by Seller in the Purchase Agreement or Deed, and do not want to have to pursue a claim against the Title Company under the Title Policy.	against the Title Policy. This area is hotly negotiated, with some Sellers refusing to concede, and some Buyers refusing to concede. Need to consider whether title coverage in some state (e.g., Texas) is impacted by limitations on Buyer's rights to pursue claims under the purchase agreement or deed.
REPRESENTATIONS AND WARRANTIES – IN GENERAL	The reps and warranties that a Seller is willing to make may be influenced by several factors. (1) How long has Seller owned the property? This will affect how much knowledge the Seller has about the property. (2) How long is the IP? If Buyer has ample time to conduct its due diligence, Seller may say rely on your due diligence and don't look to us as an insurance policy. (3) Is the information covered by the rep and warranty something the Buyer can find out through its own due diligence. If so, again Seller may want the Buyer to rely on its own due diligence and not look to Seller as an insurance policy. (4) Seller may want to qualify reps and warranties to its knowledge rather than make absolute statements. Sellers also frequently want to define what Seller's "knowledge" means; i.e., if an employee or property manager is aware of something but that information has not been communicated to others, Seller will not want that information imputed to the entire Seller entity. (5) As long as Seller is not	A Buyer will typically want three basic kinds of representations and warranties from a Seller: (1) "fundamental" representations and warranties regarding the Seller itself, including, e.g., its existence, authority and legal capacity to perform its PSA obligations without the consent of any other party ("Fundamental Reps"); (2) economic "risk allocation" representations and warranties regarding the revenue from the property, including representations covering leases, rent roll (including CAM), tenant defaults, security deposits, and tenant inducement costs such as TI obligations, leasing commissions and free rent ("Economic Reps"); and (3) representations and warranties regarding the property itself, including such things as title, physical property condition, legal compliance of the property, and litigation or claims affecting the property ("Property Reps").[Practice tip: if Seller's reps are qualified by knowledge, Buyer's should negotiate the right to terminate the PSA if the factual matter covered by the rep turns out to be false regardless of	Length of Inspection Period may influence how to reach a compromise. Seller will rarely have a problem giving the Fundamental Reps with no knowledge qualifiers. On the Economic Reps and Property Reps, distinguish between items that can be verified by Buyer (e.g., title; physical condition of the property) and those that are most likely only known to Seller (e.g., litigation; notices of violations). On those that can be verified by Buyer, consider some combination of allowing Buyer adequate means of verifying the information (estoppels, tenant interviews) and Seller accepting risk for material deviation from information provided to Buyer (see rent roll discussion below). The more opportunity Buyer has to verify information, the less

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	intentionally keeping information from Buyer, is not aware that any rep or warranty is inaccurate and Buyer has been given adequate opportunity to conduct its due diligence, Seller may try to limit is liability if it later turns out that a rep or warranty was incorrect. (6) Seller may also be hesitant to make reps based on information prepared by third parties (see discussion below regarding accuracy of information provided by Seller). [Practice tip: if Seller's knowledge is defined to be the knowledge of certain named individuals, include a provision saying that such individuals shall have no personal liability under or with respect to the PSA and obligating Buyer to indemnify and hold the individuals harmless if Buyer or any party related to Buyer brings any claims against those individuals.]	whether the Seller knew the rep was inaccurate.]	risk Seller should be asked to assume. Regarding information prepared by third parties, Seller can rep that it is not aware of any [material?] inaccuracies or omissions. [Practice tip: if Seller's reps are limited to the knowledge of certain individuals, Seller should represent that the named parties are the individuals with responsibility for the matters covered by the reps. If there is a separate property manager, consider defining "knowledge" as after making due inquiry of the property manager.]
REPRESENTATION AND WARRANTY THAT THE RENT ROLL AND THE OTHER SELLER PROVIDED INFORMATION IS TRUE, ACCURATE AND COMPLETE	The Buyer is free to do such due diligence on the tenants and the rents being paid and on the other due diligence as it desires. The Buyer will be gathering estoppels to back up the rent roll numbers. The due diligence period is given so that Buyer can confirm the information given and makes its own judgment on the property.	As to the rent roll, the Buyer should not have to expend due diligence dollars to determine the truth of the rent roll put forward by the Seller (through a broker, if a broker is involved), which rent roll was used to justify the offered purchase price.	The Seller can represent and warrant that the rent roll provided to the Buyer is the rent roll used by the Seller in owning and operating the property. Such a rep/warranty can give the Seller some comfort that if there are errors on the rent roll, it will not be actionable against them and the Buyer can take some comfort in knowing that the Seller has an interest to see to it that the rent roll has some degree of accuracy if in fact the Seller is using it to own and operate the property. As to the due diligence materials,

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			the Seller can represent and warrant the accuracy of those materials (other than the rent roll) which it prepared and can represent and warrant "to its knowledge" the accuracy of those materials prepared by 3rd parties. The question will arise as to whose "knowledge" is the Seller's knowledge—a Buyer will want that to be the knowledge of the property manager on the ground who would seem to know the most; the Seller will want that to be the knowledge of a higher level asset manager or executive but without any due diligence as to the accuracy of the information or materials. A reasonable compromise would be that there should be some modest level of inquiry due diligence with the property manager on the ground.
SURVIVAL PERIOD OF REPRESENTATIONS AND WARRANTIES	Seller will want to representations and warranties to expire as soon as possible after closing. Survival periods of 6 to 12 months are relatively common. Sometimes there are no limitations on the survival of corporate authority and good standing representations. Sometimes representations don't survive closing at all in very simple deals. If a Seller is agreeing to the survival of representations, Seller should include an "anti-sandbag" provision that protects Seller from liability for a breach of a	A Buyer should beware of provisions in a purchase agreement that provide that Seller's representations and warranties merge with the deed at closing, which means they do not survive. Assuming Buyer avoids representations and warranties merging with the deed, the issue for debate will be the survival period for representations and warranties. Buyer will want Seller's representations and warranties to survive indefinitely, but most Sellers will not accept indefinite survival. Most breaches of representations will be discovered by Buyers relatively soon	Most Sellers and Buyers settle on a survival period of 6-12 months. Discussion item: Reps and Warranty insurance in real estate deals.

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	representation or warranty that a Buyer discovers pre-closing. Seller may also want to have the option to "revise" its representations to reflect changes or discoveries prior to closing, although this may require Seller to give Buyer a termination right for a material change. [Practice tip: If Seller is required to deliver a certificate at closing that re-certifies the representations and warranties, make sure that the certificate references the survival (and other limitation) language in the purchase agreement.]	after closing, so most Buyer will accept a survival period of 6-12 months, ideally long enough to take Buyer through the CAM reconciliation period with tenants for the year in which closing occurs, or, for the Development Buyer, for the period that they will be engaged in redevelopment or construction. A related issue of concern to Buyer is the value of the survival period – Will Seller have any assets post-closing (or at least through the survival period)? Can Buyer get a guarantor or escrow to back-stop Seller's post-closing obligations?	
ESTOPPELS AND SNDAS	A Seller will take the position that it will obtain, as a condition, some modest number of tenant estoppels—in the 50% of the square foot area range—and that it will deliver the SNDAs to such number of the tenants as the Buyer's lender shall require but that obtaining the return of the same as executed by the tenants will not be a condition to the closing particularly if financing is not a condition to the transaction. Seller will typically agree to use best efforts or good faith to obtain tenant estoppels, but issues to be negotiated include (a) whether any particular estoppels (by tenant, size of leased premises, and/or percentage of total space in the project) must be obtained as a condition of closing, (b) what constitutes a "clean" estoppel, (c) whether Seller can substitute a Seller estoppel for any tenant estoppels. Seller may want Buyer to make its decision on whether to go hard at the end of the IP based on	A Buyer will want a much higher percentage of the square foot area covered by leases to be accounted for in the estoppels—something in the 80% of the small shop space plus all of the major tenants. If SNDAs are required by the leases, a Buyer will take the position that the Seller should simply enforce the leases to get the tenants to enter into the SNDAs. Buyer will also typically want signed "clean" tenant estoppels from designated "key" tenants (typically anchor tenants) and other tenants occupying at least a certain number of square feet). 80% of total occupied square footage, inclusive of "key" tenants, would be very typical but more or less may be required for particular properties. Buyer may agree to take Seller estoppels, but usually not for "key" tenants or for more than a stipulated amount of the occupied square footage. An Investment Buyer may require that the Seller "top-off" the estoppels that are required to be provided as a minimum so that if Seller	As to estoppels, the market for "clean estoppels" as a condition is in the 65% to 75% range on the small shops space together with estoppels from the major tenants. Also, Sellers might agree to give "Seller estoppels"—effectively representations and warranties on the tenants' relationship with the landlord—if tenant estoppels are not received from the minimum number of small shop tenants. Typically, a Buyer will want to confine the number of such Seller estoppels it will be required to accept to something not exceeding 20% of the small shop tenants. A Buyer will rarely accept a Seller estoppel as to a major tenant. On SNDAs, the determining factor will be how much the Seller is willing to cooperate to facilitate the

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	estoppels in hand at that time. Seller may want Buyer to make its decision on whether an estoppel is acceptable within a certain time period after the estoppel is delivered to Buyer. Seller will not want Buyer to use immaterial matters disclosed in an estoppel as an excuse for not closing. Attach the estoppel form to the PSA. If an estoppel is attached to a tenant's lease, Seller will want Buyer to agree to accept that form. If Seller estoppels are used as a substitute for any tenant estoppels not delivered by closing (a) pay attention to the language in the estoppel form and negotiate pro-Seller changes up front, (b) provide that if a missing tenant estoppel comes in post-closing, it replaces the Seller estoppel for that lease and (c) provide that the Seller estoppel survives closing for some specified period of time. Consider giving Seller the right to extend the closing if necessary to deliver any estoppels to meet whatever is required under the PSA. Address any on-going lease commission obligations or commissions that have not yet come due (i.e., the tenant has not yet opened for business)	delivers tenant estoppels that exceed the required minimum, but not 100% of the estoppels, the Seller is required to certify, or provide a Seller estoppel, for the tenants that did not provide an estoppel. If Seller is back-stopping tenant estoppels, will Seller have any assets post-closing (or at least through the survival period of the estoppel)? Can Buyer get a guarantor or escrow to cover Seller's post-closing obligations?	Buyer's financing—if the Seller really wants to make the sale, it will more likely agree that receipt of some minimum number of SNDAs will be a condition to closing.
ESTOPPEL: WHAT MAKES AN ESTOPPEL ACCEPTABLE?	A Seller will take the position that any estoppel that confirms in all material respects the business terms and conditions of a lease will be acceptable for purposes of meeting the estoppel threshold. A Seller will require that "knowledge qualifiers" added to the estoppel by the tenant should not invalidate the estoppel	A Buyer will take the position an acceptable estoppel will not only confirm the material business terms of the lease, but also that no defaults will be alleged by the tenant. A Buyer may not accept tenant added "knowledge qualifiers" in the estoppel.	The typical compromise is to look to the applicable lease, first, to see if there are provisions on what the tenant must provide by way of estoppels. If a particular form is required, then, as to that tenant, the matter is settled. For national tenants, typically, either a form is

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			attached or specific language on what form of estoppel the tenant will give will be included. If no form and no language is included, the customary compromise will allow for knowledge qualifiers in the estoppel for matters relating to whether or not the landlord has defaulted. Knowledge qualifiers are not typically accepted with respect to confirmation of the salient business terms of the lease.
OPERATING/LEASING COVENANTS	Sellers will typically agree to continue to maintain, operate, lease and manage the property in substantially the same manner as past practice, with a high degree of discretion and without Buyers' approval. Sellers would like this discretion to last all the way through closing, but frequently will agree to limitations on discretion applicable after expiration of the inspection period. Sellers often want the right to enter into temporary occupancy agreements and service contacts, so long as they can be terminated on no more than 30 days' notice and without any termination fee.	Buyers will want Sellers to covenant to continue to maintain, operate, lease and manage the property in the same manner as past practices. Buyers may want more detailed Seller obligations relating to such things as maintaining insurance and performing all Seller obligations under leases and service contracts. Buyers also will want to limit Sellers' discretion to enter into leases, service contracts and other agreements binding upon the property or Buyers at least a few days prior to expiration of the inspection period, and will want prompt notice of any such actions by Sellers.	Compromise usually is achieved by focusing on what actions by Seller are permissible before the expiration of the inspection period and what actions require Buyer's approval after expiration of the inspection period.
REMEDIES FOR SELLER'S PRE-CLOSING DEFAULT	Sellers will typically want to limit liability for pre-closing defaults and breaches of representations and warranties. Sellers would like to limit Buyer's remedies for Seller's pre-closing defaults or breaches to terminating the PSA and receiving a return of the earnest money and perhaps a suit for specific performance.	Buyers will want full, uncapped damages as a remedy for a pre-closing default or a pre-closing breach of representations and warranties by Seller, but most Buyer's realize that is not realistic in most transactions. If the Buyer is going to terminate the PSA and walk away as a result of a Seller default, not only will they expect the return of their earnest money but will	Buyer to have the right to (1) terminate the PSA, receive a return of the earnest money and be reimbursed for its out-of-pocket expenses (subject to a cap?), (2) seek specific performance, or (3) sue Seller for damages (subject to a cap?) if specific

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	See also discussion in next section regarding baskets and caps on Seller's liability	also want to be reimbursed for their out-of-pocket costs. See also discussion in next section regarding baskets and caps on Seller's liability .	performance is not available because of Seller's actions. See also discussion in next section regarding baskets and caps on Seller's liability Consider: what if Buyer has to put up a sizeable non-refundable commitment fee for its loan to buy the property? What if the Buyer is purchasing the property as replacement property in a 1031 exchange?
LIMITATIONS ON SELLER'S LIABILITY: BASKETS AND CAPS	If Seller is going to have monetary liability for pre-closing defaults and pre-closing breaches of representations and warranties or for breaches of representations and warranties discovered post-closing or for defaults under post-closing obligations, it would be highly unusual for Sellers to agree to full, uncapped damages as a Buyer remedy. In order to avoid being bothered by insignificant or nuisance claims, most Sellers will negotiate for a minimum threshold ("basket") before Buyer may pursue a claim against Seller. Most Sellers also will negotiate a cap on aggregate liability so that it can plan for a worse-case scenario.	Buyers will want full, uncapped damages as a remedy for a default by Seller identified post-closing. If Buyers agree to a basket limitation, they will want the basket to be a "tipping basket" where Buyer can collect from the first dollar after the threshold is exceeded. If Buyers agree to a cap on Seller's liability, Buyers will want the cap to be high and for carve-outs for fraud, willful misconduct and commissions to apply	Sellers and Buyers typically reach agreement on a low basket ($25-$100K, depending on size of transaction), and a cap equating to 1-7% of the purchase price. Back-stops (guarantees, escrows, promises to maintain assets during survival periods) are not common, but are appropriate in some circumstances. [Practice note: If Buyer desires a back-stop, it should be negotiated up front in the LOI.]

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POST-CLOSING CONSIDERATIONS	Rent and expenses attributable to the period before the Closing need to be addressed, especially if they are covered by an executory Forbearance Agreement that is in the process of being satisfied. For credit-tenants, Seller may want the net present value of that cash flow, after deduction for Buyer's handling and collection costs, to be paid in addition to the Purchase Price. For other tenants, payment as it is collected is acceptable. Seller will want the Buyer to use good faith diligent efforts to collect such past due amounts.	Buyer does not want to take any collection risk on amounts attributable to the period prior to its ownership. In addition, it does not want the payment of old debts to threaten the payment of current obligations or to economically weaken the prospects of their tenants. Buyer will want all debts from the tenants to the Seller to be assigned to Buyer at Closing, for all amounts collected from tenants to go first to present obligations and to have broad discretion regarding the collection of past debts. Buyer may require a post-closing Seller enhancement of tenant obligations for a variety of reasons, including for a tenant that may be on shaky ground coming out of the pandemic, or one with a Forbearance Agreement that may still allow a tenant some latitude in the timing or amount of payments. Usually, this will be accomplished with an escrow agreement defining the terms upon which a portion of Seller's proceeds will be paid back to Buyer to cover certain tenant obligations. These guaranty-type escrows will typically be of limited duration.	Buyers will typically allow that amounts attributable to a period before Closing belong to the Seller, but will not obligate themselves to collect any such amounts. Buyers will resist giving Sellers any post-Closing right to collect past due amounts, on the basis that such efforts weaken their tenant base. The details of any post-Closing escrow agreement to enhance must be meticulously drawn to avoid failing to address future situations or actions that cause conflicting claims to hang up the amounts held due to unanticipated circumstances. Clear, objective conditions to disbursement are essential.

An example of a Pandemic Delay provision:

Section ___. Pandemic. Seller and Purchaser acknowledge that, as of the Effective Date, public health emergencies have been declared throughout the United States, the State of _____, and city of _____, _____ in connection with the Coronavirus (COVID-19) pandemic (the "Emergency Orders") that may cause unexpected impacts to real estate transactions, including but not limited to the imposition of travel restrictions, mandatory isolations, governmental and business closures, delays in Purchaser's inspections and Government Approvals as set forth in this Agreement, and potential closure of offices and institutions required to fund, close and record real estate transactions (collectively, the "COVID Restrictions"). Notwithstanding the Emergency Orders, Purchaser and Seller intend to commence and continue in good faith with performance of their respective obligations under this Agreement. Should either Seller or Purchaser not be able to perform any obligation or meet a contingency within the prescribed time period for such performance due to the COVID Restrictions (an "Affected Time Period"), the Affected Time Period shall be tolled and extended on a day to day basis for a period equal to the time that the COVID Restrictions prevent such party's performance or contingency provided that written notice is delivered to the other party detailing the specific facts and circumstances giving rise to the Affected Time Period, together with regular on-going updates to the other party

continuing through such time period as the COVID Restrictions no longer prevents the subject performance or contingency[***insert if hard end date needed:***; provided, however, that in no event shall the Affected Time Period exceed ___ {days}{months}from the {Effective Date}].

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