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REPORT

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TRACKING NEVADA'S BIG DEALS

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MASTERING THE ART OF COMMERCIAL
REAL ESTATE NEGOTIATIONS

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Contracts

Mastering the Art of Commercial Real Estate Negotiations

Some have said that contract negotiation is an art. A well negotiated contract should encompass the full expectations of both parties. When all goes well, all parties are pleased with the contract terms, each performs as outlined, the deal closes without incident, and they achieve their goals.

"If it's done right, you have a good document that's reasonable, realistic and easily executed," said Brad Schnepf, president of Marnell Properties, a Las Vegas-based commercial real estate development and management company.

According to experts, to achieve such a contract, specific strategies can be employed and pitfalls avoided.

About The Contract

Each commercial real estate development contract—whether it be between a buyer and seller, a land owner and a developer, a developer and a general contractor or other parties—contains two inter-twined components, the business side and the legal side. The business side of the transaction constitutes the who, what, where, when and how of the deal according to Andrew Gabriel, a commercial and corporate real es-

tate law attorney and partner with McDonald Carano Wilson in Las Vegas. "It's a road map of how you get from Point A to Point B," he adds "It contains the whole picture from start to finish."

The legal aspect pertains to and details issues surrounding the business deal. Some of the necessary legal points are the amount, timing and processing of any deposits; termination; the timing and scope of due diligence and closing; default provisions; indemnity; warranties; risk shifting clauses; contingencies to closing; and terms that govern the outcome for a failed transaction, said Bradley Boodt, a commercial real estate and business attorney and a partner with Holland & Hart in Las Vegas.

The lawyers' job is to anticipate what could go wrong with a deal and protect their clients from that. Consequently, it's essential the client's representation understand the specifics of each business potentially represented in the deal, said Bruce Leslie, a real estate attorney and partner with Armstrong Teasdale in Las Vegas.

In today's world, a one-page contract is unheard of and the complexity of the business transaction being defined determines the length of the contract.

The Typical Process

"The contracting process often begins with two parties, say a property seller and buyer for example, discussing a potential deal and creating what's called a term sheet, letter of intent or memo of understanding—a simple, non-binding expression of the bare bones transaction they're interested in achieving," Gabriel said.

Subsequently, an attorney engaged by one of the sides then drafts a contract based on the points outlined in the initial understanding. Negotiation then comes into play.

Negotiating can take place within a day or can take up to years. Once, and if, the parties finally agree to the contract terms, they both sign the document, making it viable.

The Do's And Don'ts

When a contract isn't negotiated properly, issues arise midstream that then must be addressed, Schnepf said. Specific points must be re-negotiated, if possible, and if not, the deal may have to be canceled.

To avoid such scenarios, consider the following expert advice for negotiating commercial real estate development contracts:

Legal Counsel

Don't sign an agreement, even one that's non-binding, before having your lawyer fully review it first. This is a common pitfall that can result in undesirable consequences. "We might see things in the letter of intent that aren't exactly clear, and if we have to translate that into a contract, it's helpful to flesh that out at an early stage," Gabriel said.

Additionally, always use an attorney with whom you have a good relationship. "You need to listen to your counsel," Schnepf advised. "Have them explain to you what the [contract] implications are. Talk through the risks and come to an area that you're comfortable with. It's a collaborative effort."

Team Approach

Don't negotiate alone. Along with an attorney, have a team with whom you can discuss and brainstorm the contract. This group can include any third parties interested in the transaction outcome.

Just be careful that everyone is on the same page during negotiations. "While a team can be important to making sure that a particular component of a deal is being handled by the best person, in negotiations, speaking with one voice is usually best," said Greg Gilbert, a commercial real estate and construction attorney and a partner in the Las Vegas of Holland & Hart.

Ears Open

"Follow the old adage: 'Listen twice as much as you talk,'" Schnepf recommended. Hear and understand the other party's situation and objectives to see if they align with your own so you then can, if necessary, try and accommodate those without negatively affecting your own position. For example, one party may need to obtain a particular zoning prior to the closing date. The other side needs to understand why that's critical before determining whether or not they can agree to it. "Once there's a mutual understanding of a concern, more times than not you can work through it to the benefit of both parties," Schnepf said.

Egos Aside

When face-to-face with the other party, know when to back off and have a professional, like your lawyer, take over. This may be necessary if, for example, your negotiating style or personality seems to be offending the other party. Egos must be set aside.

Keep it Real

Be honest, avoid exaggeration and be consistent, to avoid eventually ending up in litigation. "Focus on top goals and be creative about ways to resolve sticking points that arise during negotiations," Boodt said.

Be realistic about the value of the specific real estate. Don't let emotional ties to a particular piece of property or development cloud your belief of what it's worth.

Do Your Homework

Have all the necessary information before making decisions about the deal or contract. This includes industry knowledge, property value and development costs, any specifics related to the deal you want to make. Learn about the other side and assess what is likely important deal points to them.

"It's important to show the other side that you've done your homework and are serious," said Gilbert. "It is always best to know the answers before you ask the questions, if possible."

Avoid the Pressure

Don't be pressured into making a critical decision if you're uncomfortable doing so. Have an "out" prepared in advance. For example, say you need to take the decision to your executive board, to allow yourself sufficient time to mull over the issue.

Take the time to thoroughly read the final contract, looking for ambiguous provisions. The language should be as precise as possible to avoid future problems. "If the decisions are going to be good ones, a thorough analysis of the transaction has to occur first," Gilbert said.

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Ask for the World

When outlining what you want in the contract, be aggressive and ask for more than you need or want or less than you want to give, to have room to back off. For instance, when proposing a sale price, start with one that's higher than what you'd accept. "Most people will not propose their final point that they're willing to accept," Gabriel said.

Stay Focused

Don't belabor minor or unimportant points. "That has a way of poisoning the deal rather than making the deal come together," Leslie said.

Also remember, don't underestimate or embarrass anyone on the other side. Don't get trapped into thinking you're smarter than the other side and, therefore, the contract terms aren't important.

Have a Plan B

Don't depend on the particular transaction taking place. "If you get to the point where you have to have it, you're in a much weaker negotiating position," Schnepf said. "If you are desperate, you can't show it." Never be afraid to walk away from a potential deal. If you're unsure about the other party's ability to perform, for example, the deal probably shouldn't happen.

Time is Money

When a potential deal is on the table, respond in a reasonable timeframe. "Time kills deals," Schnepf said. "The other party could very well lose interest and move on because they can't stand to wait for you any longer."

"While not all commercial real estate development contracts result in a successful transaction, the vast majority do," Gabriel said. "In most cases, things go along just fine," he added.

A good contract will allow both parties to feel like they are winning from the deal.

By Doresa Banning

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