



# What Do We Do Now? Finding Strategies to Cope with the Pandemic

Tuesday, April 7, 2020  
1:00 p.m. to 2:00 p.m. Eastern

Panelists:

Alexandra Cole, **Perkins Coie LLP**, Chicago, IL

Lee Weintraub, **Becker & Poliakoff**, Fort Lauderdale, FL

Manny Farach, **McGlinchey Stafford PLLC**, Fort Lauderdale, FL

Gisela Munoz, **Katz Barron**, Coral Gables, FL

Matthew Schiller, **Murphy Schiller & Wilkes LLP**, Newark, NJ

## PRACTICAL TIPS FOR COMMUNICATING WITH:

1. Landlords
2. Tenants
3. Lenders
4. Property Managers

# HOW DO I?

## 1. Proceed with a Closing?

- record documents
- obtain signatures
- access a notary

## 2. How do I close down my facility?

- compliance with WARN Act
- am I an “essential business” and if I am not, what activities can I continue to do?

# THE USE OF CONDITIONS PRECEDENT AND MAC CLAUSES BY BUYERS IN PURCHASE AND SALE AGREEMENTS

**Conditions Precedent generally,  
and a no Material Adverse Change (“MAC”) condition specifically,  
may give a Buyer:**

- The right not to close (extension vs. termination – to be discussed further later);
- The right to a refund of the deposit if terminating.

# CONDITIONS PRECEDENT GENERALLY

## **A Condition Precedent to Closing is:**

- “an event not certain to occur, which must occur, unless it’s nonoccurrence is excused [i.e., waived], before performance under a contract becomes due.”  
RESTATEMENT (SECOND) OF CONTRACTS, § 224.
- If a condition precedent is unsatisfied, a party’s performance is relieved.

## CONDITIONS PRECEDENT GENERALLY (cont.)

### IMPLIED VS. EXPRESS CONDITIONS:

#### 1. Implied Conditions:

- (a) Less likely to be applicable to real estate PSAs, but should be noted.
- (b) At least three ways to infer.
- (c) An implied condition must be “substantially” satisfied by the obligor.

## CONDITIONS PRECEDENT GENERALLY (cont.)

### IMPLIED VS. EXPRESS CONDITIONS:

#### 2. Express Conditions:

- (a) When the scheduled closing date arrives, what does the language say are the consequences of an unsatisfied condition?
- Extension vs. immediate termination
  - Termination option vs. automatic termination
  - Return of deposit upon termination
- (b) An express condition must be “strictly” satisfied by the obligor.

## CONDITIONS PRECEDENT GENERALLY, NO MAC CONDITION

- Review your PSA's conditions precedent to see if any are unsatisfied due to COVID-19 pandemic or the resulting circumstances.
- Review your PSA for a No Material Adverse Change condition, which is the specific condition we're going to review next.
  - Contract specific
  - Subjective
  - Likely difficult to establish



# MATERIAL ADVERSE CHANGE OR MAC

1. “Material” =
  - (a) not temporary, and
  - (b) must significantly affect the party’s ability to perform its obligations under the contract.

## MATERIAL ADVERSE CHANGE OR MAC (cont.)

2. The next question is: **a MAC on what?**
  - (a) On the Property? On the physical condition of the Property? On the physical, financial, or legal condition of the Property? On the ability to finance the Property or to develop/entitle or market/sell the Property? On the condition of the Buyer?
  - (b) A MAC on conditions of the Property are most likely, but does COVID-19 have a MAC on the Property if COVID-19 affects the entire world?
  - (c) Are there any carve-outs to the MAC condition drafted into the contract? E.g., “except for changes in general economic conditions” or conditions affecting the entire industry?

## MATERIAL ADVERSE CHANGE OR MAC (cont.)

- Material Adverse Change may be too difficult to prove in existing contracts.
- Suggestion has been made to include a MAC in future contracts:
  - COVID-19 specific provision
  - Extension option
  - Termination option vs. automatic termination
  - Deposit refund upon termination

## CORONA'S IMPACT ON CONSTRUCTION

- Need to determine extent to which construction projects remain open in your state
  - Is new construction permitted to commence?
- Effect of closure of building departments
- Labor concerns
  - Consider issuing safe passage letters
  - Increase in worker's compensation claims if contracted on-site
  - Accelerated migration of labor out of the industry
- Not likely covered by insurance

## CORONA'S IMPACT ON CONSTRUCTION (cont.)

- Force majeure
  - Was cessation of work caused by natural causes or government action?
  - Breadth of enforcement differs by state
  - AIA contract permits contractor termination if work is stopped for thirty consecutive days
    - Loan documents may establish conditions of termination
    - Should consult with surety first
- Consider contractual notice requirements
  - Knowledge of condition has already occurred

## CORONA'S IMPACT ON CONSTRUCTION (cont.)

- Secure equipment and materials now in case ongoing construction is shut down
- Supply chain management
  - Many supplies come from China and other foreign countries
  - Line up alternative material sources as fallback
  - International suppliers may be difficult to pursue for damages if they don't perform
  - Lead times for delivery are increased
  - Suppliers are changing contract terms and requiring cash payments on delivery

## CORONA'S IMPACT ON CONSTRUCTION (cont.)

- Reduced efficiency in construction home office operations
  - Everybody is working remotely now
- Good news is this will likely lead to improved processes for the future

# Coronavirus Aid, Relief, and Economic Security (CARES) Act & It's Impact on the Real Estate Industry

- Senate unanimously passed (96-0) on March 25, 2020.
- Passed House of Representatives by voice vote and President Trump signed into law on March 27, 2020.
- SBA Interim Final Rule announced the evening of April 2, 2020
- Final regulations anticipated by April 26, 2020

## **Where's the beef?**

- Provides stimulus to individuals, businesses and hospitals due to the economic distress resulting from COVID-19 pandemic
- Creates a \$349 billion loan program for small businesses, 501(c)(3)s and medical practices
- Allocates \$500 billion to assist businesses, states and municipalities.
- Allocates \$130 billion in relief to medical and hospital industries.



## CARES ACT: Impact on Real Estate Industry (cont.)

### Overview of Paycheck Protection Program

- \$350 billion in funding for banks to issue zero-fee loans of up to \$10 million to make 7(a) loans small businesses on or before June 30, 2020
- Loans can be utilized to include:
  - Payroll support (including paid sick or medical leave)
  - Employee salaries and benefits
  - Rent and utilities
  - Interest payments on mortgages
  - Interest payment on other debt incurred prior to February 15, 2020
- Loans may be forgivable up to 100% of the principal amount borrower
- Do not require collateral or guaranties
- **NOTE:** SBA's Interim Final Rules issued April 2, 2020 made (1) financial businesses primarily engaged in the business of lending & (2) certain passive companies owned by developers & landlords ineligible for PPP loans.

# Impact of CARE Act on Real Estate Industry

- **Landlords and Investors:** No direct relief!
- **Retailers and Small Businesses:**
  - Is the relief sufficient?
  - How much will CARES Act actually curtail layoffs and allow businesses to cover short term expenses?
  - How many businesses will survive?
- **Lenders:**
  - How are lenders responding to influx of SBA applications and regulations?
  - Impact on CMBS market and mortgage servicers
- **Construction Industry:**
  - \$43 billion in aid available to assist construction industry under CARE Act.
- **Real Estate brokers and agents:**
  - Unemployment insurance to independent contractors, which would include most brokers.

# BANKRUPTCY

- Good luck with stay relief motions if you are a lender because the amount of the loan, the value of the property (net cap v. cost of construction) and the project all weigh in favor of the borrower.
- Plus, equitable factors control and this downturn wasn't the fault of the borrowers.

## VALUATIONS ARE NOW IN THE AIR

- Good luck getting an accurate valuation as appraisals are based on the ROI and the net cap rate and future income and who knows what those are worth these days
- Past sale valuations will gain little credibility with bankruptcy judges
- No one knows what the tenants are doing these days
- Put that all together and the chance of getting a creditor-friendly valuation for your stay relief motion or otherwise are slim.

## OWNERS VS. LENDERS

- Some in the business community are losing sight of the fact that while owners are getting squeezed by stay relief and valuation issues, lenders are getting squeezed too
- The traditional sources of basis spread (loans and deposits) are close to non-existent now and borrowers are going to have trouble repaying their loans
- Lenders are borrowers too so they themselves have loans to repay. In short, lenders are going to be between a rock and a hard place.

## **BOTTOM LINE: BANKRUPTCY COURTS WILL BE DEBTOR FRIENDLY**

Think of this period of time as Timbers (United Savings Association of Texas v. Timbers of Inwood Forest Associates, Ltd., 484 U.S. 365 (108 S.Ct. 626, 98 L.Ed.2d 740) on steroids

Bankruptcy courts are going to give debtors a chance and there will be a slow-walk to foreclosures and liquidations

Bankruptcy courts are courts of equity and this mess is not the result of the fault of the debtors; these were situations beyond the control of the debtors. Giving debtors a chance is equity in the eyes of the bankruptcy courts, and the argument can be made, is good for the nation as a whole.

## INDUSTRIES AFFECTED

- There are the obvious ones (travel, hospitality, energy, real estate) but some that don't immediately come to mind
- "Social distancing" may actually bring about the much-hyped "retail apocalypse" as shoppers now have a very good reason to not go to the malls and the pressure on landlords will be extreme both from the rents side and also from the building side (think of costs of commodities, of construction, etc.).

## STRATEGY: “I TOLD YOU SO”

- Despite the best-written contracts and best-underwritten loans, there is little way to combat a world-wide pandemic and economic slowdown in bankruptcy court
- Bankruptcy judges will be favorable to borrowers and the best creditors can hope for at this point is to employ a “give ‘em enough rope” strategy of arguing for stay relief (or other relief) early in the case, and if the debtor does not come through, then diplomatically remind the court that debtor promised everything would be fine in 60 days and the case has actually gone backwards



## USEFUL LINKS

1. [www.beckercovid19.com](http://www.beckercovid19.com)
2. <https://www.nolo.com/legal-encyclopedia/emergency-bans-on-evictions-and-other-tenant-protections-related-to-coronavirus.html>
3. <https://www.alta.org/advocacy/online-notarization.cfm>
4. <https://www.murphyllp.com/news>
5. <https://www.perkinscoie.com/coronavirus>
6. <https://www.covid19businessguidance.com/category/real-estate-and-land-use/>