

Chutes and Ladders of Real Estate Transactions: Avoiding Pitfalls in Drafting Commercial Documents



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When the subject turns to the details of any of our recent real estate trials, other attorneys as well as clients are routinely surprised by what question of fact or law has turned out to be a key element of the case. Many times, the deciding issue in a real estate case is the drafting of the underlying commercial real estate documents. For this reason, it is extremely important for drafting attorneys to always bear in mind the specter of litigation. The following discussion identifies a representative cross-section of timely topics that we see ripen (or spoil) into litigation repeatedly.

I. Drafting Precision

Your best defense in real estate litigation is good offense. Precise drafting on the front end can save a lot of headaches in litigation. A significant number of contract disputes turn on matters of the contract's construction including the definition of a particular word or phrase, the placement of a clause within a sentence, or even the placement of a punctuation mark. It is important to note that most, if not all, of these disputes could have been avoided at the time of the contract's drafting with a few "simple" changes to the document. The changes are only "simple," however, if the attorney has done his or her due diligence on the pitfalls of drafting, including the dangers of both indefiniteness and ambiguity.

A. The Danger of Indefiniteness

As the Georgia Court of Appeals consistently has held, the test of an enforceable contract is "whether it is expressed in language sufficiently plain and explicit to convey what the parties agreed upon."¹ The time and subject matter of the agreement must be clear from the language used in the contract. Language that is indefinite, uncertain, or vague may render the contractual provision, or even the entire contract, unenforceable.

¹ Farmer v. Argenta, 174 Ga. App. 682, 683 (1985).

“[I]ndefiniteness in subject matter so extreme as not to present anything upon which the contract may operate in a definite manner renders the contract void.”²

For example, in AMB Property, L.P. v. MTS, Inc., the Court of Appeals held unenforceable a renewal provision setting the new rental rate as “the greater of (1) the base rent for the last year of the original term or (2) *the then existing market rental rate for comparable shopping centers.*”³ Rather than merely striking the vague language and enforcing the remainder of the provision, the Court held that the reference to the “market rental rate” was such an integral part of the renewal provision that no portion of the provision should be enforced.⁴

In Farmer v. Argenta, the Court of Appeals went one step further when addressing the enforceability of the following stipulation in a real estate sales contract: “30 days after closing seller will pay buyer rent in the amount of the mortgage payment, taxes and insurance included if escrowed in an amount not to exceed \$300.00 per month *as long as necessary until seller finds another home.*”⁵ The Court determined that the phrase “as long as necessary until seller finds another home” was too indefinite to be enforced, and further held that the indefinite term was so material to the sales agreement that its indefiniteness rendered the entire contract unenforceable.⁶ Georgia courts can either strike an invalid term or find that the invalid provision renders the entire contract void.⁷ In making this determination, the court will consider the intent of the parties as evidenced by the terms of the agreement. “If it appears that the contract

² Lemming v. Morgan, 228 Ga. App. 763 (1997) (citations omitted).

³ 250 Ga. App. 513, 513 (2001) (emphasis added).

⁴ Id.

⁵ 174 Ga. App. at 682 (emphasis added).

⁶ Id. at 684.

⁷ Id.

was to take the whole or none, then the contract would be entire.”⁸ For example, if it appears that the parties intended to sell an entire piece of land through a purchase and sale agreement, then an invalid term could render the entire contract void.⁹

B. The Danger of Ambiguity

Even if a provision does not contain terms too indefinite, uncertain, or vague to enforce, a term or phrase of the contract may be capable of more than one reasonable interpretation, thereby creating ambiguity. In Georgia, the threshold question for the court in matters of contract interpretation is whether or not the language of a disputed contractual provision is ambiguous.¹⁰ “Ambiguity exists when a contract is uncertain of meaning, duplicitous, and indistinct; or when a word or phrase may be fairly understood in more than one way.”¹¹ The court first considers the language contained in the “four corners” of the document when deciding whether a provision is ambiguous.¹² If the court determines that the contract language is unambiguous, the contract is enforced as plainly written.

If, after considering the language of the “four corners” of the agreement, the court finds that there is still the potential for ambiguity, then the court applies the rules of construction. The Georgia Code sets out some of the rules of construction employed by the court. These rules of construction provide that: parol evidence may be used to interpret a contract; words generally bear their usual meaning unless they are words of art or technical words; business custom may be considered when universally accepted;

⁸ Peach Consolidated Prop. v. Carter, 278 Ga. App. 273 (2006).

⁹ Id.

¹⁰ See Brannen/Goddard Co., et al. v. PNC Realty Holding Corp. of Georgia, 238 Ga. App. 387, 389 (1999).

¹¹ Sheridan v. Crown Capital Corp., 251 Ga. App. 314, 315 (2001).

¹² Id.

terms should be read to give effect to the entire contract; the contract should be read against the party that prepared the agreement; the rules of grammar usually govern; handwritten terms are given more effect than printed terms; grants by implication are not favored; and time is generally not of the essence.¹³ If, after applying the rules of construction, there is still ambiguity in the contract, the court will submit the issue to a jury to resolve the ambiguity.

Even if the parties intended the provision to mean something different than what is stated in the contract, the court will apply the terms of the contract if they are not contradicted by other terms, and capable of only one reasonable interpretation.¹⁴ In Bronner Bros. Mfg., Inc. v. Russell, the Court of Appeals addressed an employment contract provision setting a salesman's base salary at \$25,000 plus "*2% on all orders generated other than personally initiated* by [the salesman]."¹⁵ Because the provision, as stated, allowed the salesman a two percent commission on all orders other than those personally initiated by him, the employer asked the court to insert a comma after the word "personally." The court found that such an insertion, "in addition to arbitrarily rewriting the contract, would create nonsense, and make ambiguous what was not."¹⁶ The Court conceded that the provision was "not a brilliant specimen of draftsmanship," but ultimately held that it was not ambiguous. Therefore, the Court refused to consider the existing evidence that the parties had never intended for the salesman to get a two percent commission on sales that were not his own.¹⁷

¹³ O.C.G.A. § 13-2-2.

¹⁴ Twin Oaks Assoc. v. DeKalb Venture, Ltd., 190 Ga. App. 854, 855 (1989); First Data POS, Inc. v. Willis, 273 Ga. 792, 794 (2001).

¹⁵ 196 Ga. App. 832, 833 (1990).

¹⁶ Id.

¹⁷ Id. at 834.

When considering a contract provision, a court properly may determine that a seemingly clear and unambiguous provision is in fact ambiguous because of the existence of a conflicting provision within the contract. For example, in Coker v. Coker, the Court of Appeals determined that an otherwise clear right-of-first-refusal provision was ambiguous because it conflicted with other contractual provisions.¹⁸ While the right-of-first refusal provision contemplated third party offers for the entire property, other relevant contractual provisions contemplated third party offers for mere portions of the property.¹⁹ Consequently, the Court read into the right-of-first refusal provision the parties' intent to include offers for only a portion of the property.

If the Court determines that a provision is potentially ambiguous, then the court turns to the rules of construction in order to determine the parties' intent in drafting the provision.²⁰ In Western Pacific Mut. Ins. Co. v. Davies, the Court considered how to interpret the word "failure."²¹ Where a disputed term or phrase is not otherwise defined by the contract, a court will give the words their ordinary meaning as defined by dictionaries.²² Therefore, the Court turned to the dictionary definition of "failure" to determine the ordinary and customary meaning of a home warranty provision under which coverage was triggered by a "failure of...structural components."²³ Because the dictionary indicated that "failure" could mean anything from "not succeeding in doing or becoming," to "lost power or strength," the Court held that it was for a jury to decide

¹⁸ 265 Ga. App. 720 (2004).

¹⁹ Id. at 721.

²⁰ Swisshelm v. Department of Human Resources, 253 Ga. App. 816, 817 (2002) ("The cardinal rule of construction is to ascertain the intention of the parties.").

²¹ 267 Ga. App. 675, 676, (2004).

²² Kerr-McGee Corp. v. Georgia Cas. & Sur. Co., 256 Ga. App. 458, 459 (2002).

²³ Davies, 267 Ga. App. at 676.

whether there had been a “failure” sufficient to trigger coverage.²⁴ Grammar and precision of language are never more important than when a court reviews only what the words say, without explanation or context from the litigants.

Note that in an effort to avoid ambiguity, it is important to define all capitalized terms and ensure that the title of the documents or labeling of the provisions therein are indicative of the intent of the parties. Also, it is important to remember that the actions of the parties can be considered by a court in resolving ambiguity. In Richard Bowers & Co. v. Clairmont Place, there was a dispute as to whether Clairmont, the owner of a commercial property, was required to comply with a provision in a Leasing Commission Agreement entered into by one of its predecessors to pay a broker’s commission.²⁵ It was undisputed that Clairmont assumed the Leasing Commission Agreement as part of its purchase. The Leasing Commission Agreement provided, in pertinent part, for payment of commissions equal to “five percent (5%) of the monthly rental paid by Tenant under this Lease” by owner to broker.²⁶ Subsequent to the execution of the underlying lease but prior to Clairmont’s acquisition of the subject property, the tenant on the subject property changed.²⁷

Although Clairmont paid the 5% commission to the broker for a period of time, Clairmont later ceased paying the commission and the broker sued for the commissions owed.²⁸ The trial court denied the broker’s motion for summary judgment finding, in part, that the subsequent tenant was not the “Tenant” for purposes of the Leasing Commission Agreement and, therefore, Clairmont did not owe the commissions. The

²⁴ Id. at 678.

²⁵ 324 Ga. App. 673, 673 (2013).

²⁶ Id. at 674.

²⁷ Id.

²⁸ Id. at 675.

trial court issued a certificate of immediate review.²⁹ The Court of Appeals granted the broker's application for interlocutory review and the broker appealed. The Court of Appeals determined that the lack of clarity regarding the meaning of "Tenant" created an ambiguity within the Leasing Commission Agreement.³⁰ Looking to the four corners of the contract, the Court noted that "Tenant" was not a defined term in the Agreement; and while the word "Tenant" was capitalized, the agreement contained several capitalized words that were not defined.³¹ Importantly, the Court also looked to the actions of the parties to resolve the ambiguity in the contract.³² In this case, Clairmont paid the commissions for years notwithstanding the fact that the tenant had changed. Concluding that the trial court erred in denying summary judgment, the Court found that under the parties' construction of the Leasing Commission Agreement, as shown by their actions and conduct, the subsequent tenant could be and was a "Tenant" for purposes of the Leasing Commission Agreement.³³ Also, in addressing another issue, the Court noted that the title of a document can also be evidence of the intent of the parties.³⁴

C. Other Examples and Case Studies

1. Contract Ambiguity 1

"In the event that Seller sells or contracts to sell the Property to any buyer introduced to the Property by Broker within 90 days after the expiration of the Listing Period, then Seller shall pay the commission referenced above

²⁹ Id. at 676.

³⁰ Id. at 677.

³¹ Id.

³² Id. at 678.

³³ Id.

³⁴ Id. at 679.

to Broker at the closing of the sale or exchange of the Property.” – Court found ambiguous as to what had to occur within 90 days of the listing period expiration date for the commission to be due.³⁵

2. *Contract Ambiguity 2*

Real property sold with the stipulation that “all Equipment having to do with the cattle operation still belongs to the seller.” Property then sold to third party “together with all fixtures, landscaping, improvements, and appurtenances.” – Court found ambiguous because it did not identify the equipment to remain with seller.³⁶

3. *Contract Ambiguity 3*

Purchase and sale agreement stated “transaction shall be closed on June 6, 2002, or on such other date as may be agreed to by the parties in writing, provided, however, that: (1) in the event the loan described herein is unable to be closed on or before said date; or (2) Seller fails to satisfy valid title objections, Buyer or Seller may, by notice to the other party (which notice must be received on or before the closing date), extend the Agreement’s closing date up to seven (7) days from the above-stated closing date.” – Contract was ambiguous as to the process for extending the closing date if it was a cash sale as opposed to a loan.³⁷

4. *Contract Ambiguity 4*

Special Stipulation No. 1 to the sales agreement provided: “Real Estate Commission of \$28,210.00 to be paid to [Prudential] on or before June 1,

³⁵ Snipes, et al. v. Marcene P. Powell & Associates, Inc., 273 Ga. App. 814, 815-16 (2005).

³⁶ Barrett, et al. v. Britt, et al., 319 Ga. App. 118, 122 (2012).

³⁷ Rolan, et al. v. Glass, 305 Ga. App. 217, 220-21(2010).

2002, by sellers.” – Court noted that the provision failed to provide for a refund if the sale failed to close on stated date unlike other provisions to the agreement; because a genuine issue of fact existed for jury determination the trial court erred in granting summary judgment.³⁸

II. Merger Clauses and the Merger Doctrine

A. Merger Clauses

Also referred to as an “entire agreement” clause, a merger clause is a statement in a contract that generally provides that “this contract constitutes the sole and entire agreement between the parties and no modification hereto shall be binding unless attached hereto and signed by each party.”

Generally, a merger clause bars reliance on any alleged misrepresentations not contained in the contract itself.³⁹ A seller is protected from a claim of fraud or misrepresentation based upon statements made prior to the agreement.⁴⁰ Put another way, the merger clause is like a disclaimer stating that the written contract “completely and comprehensively represents the parties’ agreement.”⁴¹ This, however, does not completely bar all fraud claims. A purchaser can sue for fraud based on the contract itself; she could rescind the contract and sue for fraud, or she could affirm the contract and sue in tort for fraudulent concealment.

³⁸ Krogh, et al. v. Pargar, LLC, 277 Ga. App. 35, 38-39 (2005).

³⁹ Ainsworth v. Perrault, 254 Ga. App. 470, 474 (2002).

⁴⁰ Harkins v. Channell, 274 Ga. App. 478 (2005).

⁴¹ Ainsworth, 254 Ga. App. at 472.

1. *Fraud Claims Based on Misrepresentations in the Contract*

A merger clause cannot bar a fraud claim based on representations contained in the contract itself.⁴² “Generally, false representations that induce the party to enter into the contract are merged through the contract merger language, but [when] the same misrepresentations were made as part of the contract, there [is] no merger.”⁴³ Thus, in Conway v. Romarion, the purchaser brought a claim against the sellers asserting that the sellers had concealed extensive damage to the property.⁴⁴ The Court held that the merger clause would not prevent a fraud claim for any statements made in the contract. The Court opined that if the disclosure statement was incorporated into the contract, the purchaser’s fraud claim would not be barred by the merger clause.⁴⁵

2. *Rescission*

After discovering fraud, the purchaser can rescind the contract and sue in tort. In this case, the buyer offered to restore the benefits received under the contract and sued to recover the purchase price and any additional damages resulting from the fraud.⁴⁶ A party is not bound by the merger clause in asserting a claim for rescission. If a purchaser wishes to rescind the contract, she must be careful to do so immediately, through proper notice, and *prior to filing a lawsuit*.⁴⁷ Otherwise, the Court may find that she affirmed the contract. For example, in Authentic Architectural Millworks, Inc. v. SCM Group USA, Inc., the Court found that the purchaser affirmed the contract when

⁴² Conway v. Romarion, 252 Ga. App. 528, 532 (2002).

⁴³ Worsham v. Provident Co., Inc., 249 F.Supp.2d 1325, 1332 (2002)(citations omitted).

⁴⁴ 252 Ga. App. 528, 532 (2002).

⁴⁵ Id.

⁴⁶ Worsham, 249 F.Supp.2d at 1331.

⁴⁷ Novare Group, Inc. v. Sarif, 290 Ga. 186, 188 (2011).

she failed to seek rescission in her initial pleadings with the court.⁴⁸ Similarly, a purchaser who initially asked the court to reform the contract prior to claiming rescission was found to affirm the contract and had to proceed under its terms.⁴⁹ Once a purchaser affirms the contract, she is forever barred from asserting a claim in tort for fraud in the inducement.⁵⁰

3. *Fraudulent Concealment*

The buyer could also elect to affirm the contract and sue for fraudulent concealment, claiming her damages are the difference between the value of the property sold to her with the damage and the value of the property absent the damage.⁵¹ When a buyer affirms the contract, the buyer is bound by the terms of the contract and subject to any defenses that the seller may make based upon the contract.⁵² Thus, generally when a buyer affirms a contract and sues for misrepresentations made by the seller, the seller will argue that the merger clause in the contract precludes the buyer from claiming she relied on misrepresentations made outside the contract.⁵³ This does not, however, prevent the buyer from alleging that the seller actively or passively concealed damages or defects in the purchased property.⁵⁴ In that case, the merger clause would not be a defense to the suit.⁵⁵

⁴⁸ 262 Ga. App. 826 (2003).

⁴⁹ Harkins v. Channell, 274 Ga. App. 478 (2005).

⁵⁰ Ainsworth, 254 Ga. App. at 470.

⁵¹ Browning v. Stocks, 265 Ga. App. 803, 803 (2004).

⁵² Id. at 806.

⁵³ Id.; see also Ainsworth, 254 Ga. App. at 472.

⁵⁴ Condon v. Kunse, 208 Ga. App. 856 (1993).

⁵⁵ Id.

For example, in Browning v. Stocks, the purchaser affirmed the contract and brought a suit against the seller for fraudulently concealing damage to the property.⁵⁶ The evidence established that there was extensive damage to parts of the property that took at least two years to accumulate. The damage was not discovered by the buyer's inspector because the holes had been filled with putty and fresh paint.⁵⁷ The seller attempted to argue that the merger doctrine was a defense to the claim. The court clarified that the merger clause in the contract was not a defense to the purchaser's fraudulent concealment claim.⁵⁸

B. The Merger Doctrine

The general law of survival of terms and conditions is that those found in the sales contract do not survive the closing unless specifically reserved or unless they are not performed by delivery and acceptance of the deed.⁵⁹ Ultimately, “[t]he application of the doctrine of merger depends upon the intention of the parties.”⁶⁰ If a contract contains a survival clause and the closing statement shows that the parties intended that certain terms (e.g., Reps and Warranties) survive the agreement, then they will do so.⁶¹

III. Guaranty/Waiver Language Regarding Deficiency

A. O.C.G.A. § 44-14-161

Georgia's confirmation statute requires a creditor to obtain an order confirming a foreclosure sale of real property before pursuing a judgment against a borrower.⁶²

⁵⁶ Browning v. Stocks, 265 Ga. App. 803, 806 (2004).

⁵⁷ Id. at 804-805.

⁵⁸ Id.

⁵⁹ Savage v. KGE Associates Ltd. Partnership, 260 Ga. App. 770, 774-775 (2003).

⁶⁰ Toys 'R' Us, Inc. v. Atlanta Economic Development Corp., 195 Ga. App. 195, 198 (1990).

⁶¹ Savage, 260 Ga. App. at 774-775.

⁶² O.C.G.A. § 44-14-161.

Georgia Courts have consistently held over the last eighty-five years that no action may be taken to obtain a deficiency judgment unless the person instituting the foreclosure proceeding obtains judicial confirmation of the sale.⁶³

B. Can Borrower or Guarantor Waive the Confirmation Requirement by Virtue of Waiver Clauses in Loan Documents?

In HWA Properties, Inc. v. Community & Southern Bank, the Court held that the following language was sufficient to waive the lender's obligation to confirm foreclosure prior to seeking a deficiency against the guarantor:

[The guarantor] expressly agrees that [he] shall be and remain liable, to the fullest extent permitted by applicable law, **for any deficiency remaining after foreclosure of any mortgage or security interest securing Indebtedness, whether or not the liability of Borrower or any other obligor for such deficiency is discharged pursuant to statute or judicial decision.** [Guarantor] shall remain obligated, to the fullest extent permitted by law, to pay such amounts as though the Borrower's obligations had not been discharged.⁶⁴

In Community & South Bank v. DCB Investments, LLC, the Court held that the guarantor waived the lender's obligation to confirm when the guarantor specifically agreed to be liable for "any deficiency remaining after foreclosure of any mortgage or security interest securing Indebtedness, whether or not the liability of Borrower or any other obligor for such deficiency is discharged pursuant to statute or judicial decision."⁶⁵

However, at least two trial courts have distinguished the above quoted language from instances where the guarantor did not specifically agree to be liable for any deficiency remaining after foreclosure. In Atlanta Capital Bank v. Songy, in the Superior Court of Fulton County, Judge Wright determined that the waiver found in the HWA

⁶³ Windland v. FDIC, 151 Ga. App. 742 (1979); Commercial Exchange Bank v. Johnson, 197 Ga. App. 529, 530 (1990).

⁶⁴ 322 Ga. App. 877, 886-87 (2013).

⁶⁵ 328 GA. App. 605, 612 (2014).

Properties guaranty was distinguishable from the waiver in Songy because the HWA Properties guaranty included a specific agreement to be liable for any deficiency remaining after foreclosure whereas no specific agreement existed in the guaranty before Judge Wright in Songy.⁶⁶ The Superior Court of Cobb County likewise refused to apply the HWA Properties holding to similar facts. In First Citizens Bank and Trust Company, Inc. v. Panahi, Judge Hamby held that, unlike the HWA Properties guaranty, the guaranty at issue “[did] not contain language that constitute[d] a specific affirmation of liability on behalf of the guarantors in the event that the creditor fail[ed] to confirm a foreclosure sale.”⁶⁷

In light of the uncertainty on the issue of a borrower or guarantor’s ability to waive the confirmation requirement, the Northern District of Georgia has certified the following questions to the Georgia Supreme Court:

- 1) Is a lender’s compliance with the requirements contained in O.C.G.A. 44-14-161 a condition precedent to the lender’s ability to pursue a borrower and/or guarantor for a deficiency after a foreclosure has been conducted?
- 2) If so, can borrowers or guarantors waive the condition precedent requirements of such statute by virtue of waiver clauses in loan documents?⁶⁸

It will definitely be interesting to see how the Georgia Supreme Court answers the certified questions. In the meantime, if it is the intent of the parties involved in your

⁶⁶ See Appendix A.

⁶⁷ See Appendix B.

⁶⁸ PNC Bank, N.A. v. Smith, Case No. 11:14-CV-0336A-ELR, Order at *4 (N.D. Ga. June 3, 2015).

transaction to allow the lender to seek a deficiency judgment from a borrower or guarantor before or without confirmation, you should make sure the language is at least as specific as the language found in the HWA Properties and DCB Properties.

IV. Common Sense Drafting Reminders

A. Be Careful When Using Form Documents and Boilerplate Provisions.

All attorneys who handle commercial real estate transactions have their “go by” or “standard” documents such as a form commercial sales or loan agreement. However, sometimes, the attorney’s use of the form document results in transaction-specific, key terms being accidentally omitted by the drafting attorney. For example, if the transaction contemplates the sale of a business along with the commercial real estate, the “form” commercial sales agreement likely would not include issues critical to the sale of the business such as a non-compete provision for the seller and principal owner. Be sure to review even your “boilerplate” or “miscellaneous” provisions for each transaction as these are not one-size-fits-all propositions. For example, you would not want to include a “time is of essence” clause for a transaction where timely performance is not required or cannot be assured. Analyze each specific transaction to determine which, if any, non-standard provisions must be added to your form documents for that particular transaction.

B. Review All Title Documentation Thoroughly – and then Review Again – and then Have Someone Else Review.

Title to commercial property is generally more complex than title to a residential property. Most commercial property is subject to easements, restrictions, regulations, etc. You cannot properly draft the requisite commercial provisions without

understanding and digesting the implications of title issues with the underlying real estate.

C. Have a Formal Escrow Agreement or at Least a Detailed Escrow Provision.

You would be surprised at how often the attorney responsible for drafting the commercial real estate documents fails to draft a formal escrow agreement or fails to include an escrow provision in the loan documentation. As the drafting attorney (or the individual or firm responsible for holding the escrowed funds), you WANT a formal document or provision clearly establishing the role of the escrow agent or attorney. The formal agreement or provision generally will help to minimize exposure should the transaction not be completed, especially if the provision provides that the escrow agent or attorney can simply interplead the funds to a specific court upon notice of a dispute by one of the parties.

V. Conclusion

While the aforementioned insight better prepares parties and their real estate lawyers to avoid litigation, or at least evaluate the issues associated with various contract terms, thankfully for the authors, litigation is inevitable and ubiquitous. When you find yourself mired in the pit, call a litigator to drop you a ladder.