

## W E L C O M E

*A message from*  
Aaron Abraham and  
David J. Pfeffer



*Aaron Abraham*



*David J. Pfeffer*

Welcome to the inaugural issue of *The TKD Construction Advisor*, one of several special publications for our clients and colleagues in the construction and real estate industries. We brought our practice here to Tarter Krinsky & Drogin because of the exceptional opportunities that this firm offers to combine access to best-in-class legal service providers and provide a full-service platform for our clients in the cost-effective manner that today's demanding marketplace requires.

This newsletter allows us to share some of the firm's thoughts and insights into current trends in the construction, development and general real estate industries. As we all know, the last twelve months have seen drastic changes in the marketplace for every player in

the construction industry, perhaps none more so than developers and owners of commercial real estate. As a firm, we have adapted to these changes and have been able to counsel our clients on strategies to navigate successfully in today's economy. The articles in this issue of the *Construction Advisor* highlight some of the new ways in which players in the construction and real estate industries can protect themselves in today's challenging marketplace, as well as how to capitalize on the unique opportunities that this marketplace provides.

We hope you find the articles informative and useful, and we welcome your comments and suggestions. If you have a specific topic that you would like to see addressed in a future issue of the *Construction Advisor*, we would be pleased to hear from you.

Best,

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## THREE STRATEGIES FOR DEALING WITH BALKING PURCHASERS

*By Edward Farrell*



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In today's residential real estate market, balking purchasers are a major challenge for developers. Many purchasers are seeking to renegotiate purchase agreements, and others are attempting to extricate themselves from validly binding contractual obligations by filing lawsuits or formal complaints with the Office of the Attorney General. Purchasers are disputing the terms of new transactions as well as those that were "in contract" before the economy declined.

Some purchasers seek relief based on irrelevant factors such as the state of the economy, while others thoroughly scour the unit, purchase agreement and offering plan in an attempt to discover a single detail that deviates from the original plans. Many purchasers are even willing to simply walk away from their down payment in order to avoid closing.

Developers have several tools to counter these increasingly common and harmful tactics and achieve their primary objectives of avoiding costly disputes, capitalizing on their investment and compelling balking purchasers to comply with the agreements they signed. The following three strategies may have a positive impact, and can be used both before signing new purchase agreements and during renegotiations of existing purchase agreements.

### 1. Request a Higher Down Payment

A down payment equal to 10% of the purchase price has been an industry standard in residential real estate transactions for many years. The rationale for this percentage is twofold: to require a substantial investment that will deter a purchaser

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from simply walking away from the purchase agreement and to adequately compensate the seller if the purchaser willfully defaults. Neither is the case in today's real estate market because many purchasers have been willing to forfeit their down payments and 10% of the purchase price does not provide adequate compensation to a developer. Therefore, developers should consider requesting a 15% down payment. This will result in more purchase agreements proceeding to closing since purchasers may be unwilling to forfeit this higher amount.

Courts have held that a seller may retain a down payment that exceeds 10% of the purchase price absent evidence of overreaching, fraud, illegality or mutual mistakes. This increased down payment may be structured in installments with 10% payable at signing and an additional 5% due six months later.

Even if a purchase agreement has been signed, it is not too late to capitalize on this strategy. When a purchaser seeks to renegotiate, any concessions made should be contingent on the purchaser's increasing the down payment. For example, if a purchaser requests an extension of the closing date, a developer can require that the purchaser pay an additional 5% of the purchase price in exchange for the extension.

### **2. Require Purchasers to Pay All Legal Fees**

In light of the steep increase in frivolous but expensive lawsuits and dispute resolution applications filed with the Attorney General by purchasers attempting to terminate purchase agreements, it is more important than ever for developers to insulate themselves from unanticipated legal fees. All offering plans and purchase agreements should

provide that a purchaser is required to pay all legal fees and costs incurred by a developer in defending any litigation or dispute. If purchasers are obligated to pay these costs, they may be less likely to file lawsuits or other legal procedures, especially in cases where they are unlikely to prevail.

This provision can also be added to a purchase agreement during a renegotiation. Since a renegotiation is often initiated by the purchaser, a developer can take advantage of the purchaser's weak legal position by making the requested changes only if the purchaser agrees to include additional safeguards like this one.

### **3. Seek Specific Performance**

Most purchase agreements limit a seller to the remedy of retaining the down payment if a purchaser willfully defaults. It would be prudent to also include the right to seek specific performance for

a purchaser default. Many purchasers who are simply walking away from their contractual obligations have the financial ability to complete the transaction but are simply choosing not to. With the remedy of specific performance available, a developer could potentially compel a purchaser to complete the transaction in spite of the purchaser's unwillingness. This remedy will also reduce the number of requests to renegotiate a purchase agreement since the threat of walking away from the transaction will be removed.

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# AVOIDING & DOCUMENTING CONSTRUCTION CLAIMS

By David J. Pfeffer and Michael R. Wood



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Today's marketplace presents new challenges to both owners and contractors during the construction process. To an owner, potential delays and complications in the completion of a project and management of an asset are, more than ever, something to be avoided at all costs. Likewise, to a contractor, the potential for owner defaults, delays in payment, and a fluctuating value of any security for that payment make it equally important to manage credit effectively.

The most important steps that both parties to a construction project can take to mitigate these risks, at least to some degree, are to know their contracts, implement procedures to administer those contracts effectively, and document their progress – good or bad – on the project.

## Knowing Your Contract

For all their project expertise, project personnel often make assumptions or generalizations about the contracts they are working under. On all projects, but especially on large or complex ones, contract provisions have been specifically drafted to meet the owner's or designer's goals or visions for the project. Applying lessons learned on a previous project, under a different contract, can very well result in more lessons being learned – at a significant expense.

Project personnel need to expect that contract language regarding a contractor's entitlement to compensation, extensions of time for changes to the work, unforeseen site conditions, or for any of the other myriad issues that arise on a daily basis, can – and will – vary from project to project.

Take, for example, a simplified situation of a general contractor building a mixed-use condominium in New York City. Needing a foundation, the general contractor solicits proposals from and subcontracts with a foundation contractor. The foundation contractor excludes from his proposals any obligation to remove or remediate contaminated materials found during his excavation.

Since he has encountered contaminated materials on other projects, the general contractor's project manager is able to demonstrate the existence of an unforeseen site condition and negotiate a change order with the owner. However, on this project, the owner has contracted away any responsibility

for contamination. If the project manager is not aware of this obligation under his contract with the owner or his subcontract with the foundation subcontractor, the general contractor will be at a significant disadvantage when it comes time to resolve the contamination claims.

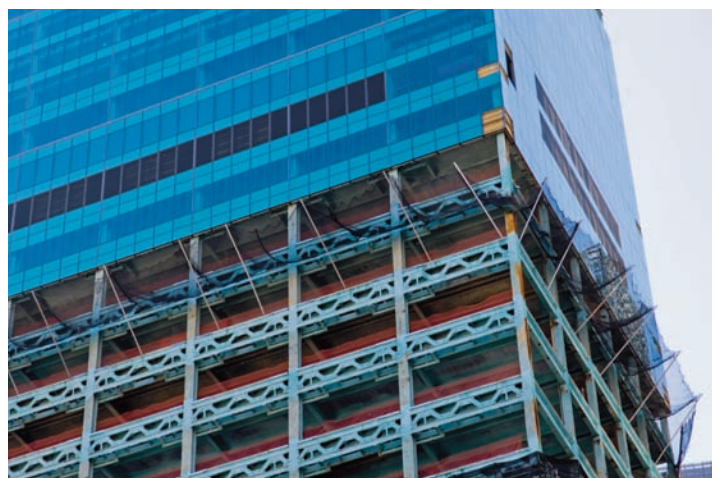
The general contractor's project manager will be left to negotiate for this work at the last minute – when the work becomes critical to his progress on the project. Although the general contractor bargained long ago to remove the contaminated materials from the site, the project manager's lack of understanding as to his contractual obligations will leave him at a significant disadvantage when forced to negotiate with the end provider of that service.

All too often, parties assume that they fully understand their obligations under the multiple agreements in place on a construction project without actually reading those agreements.

## Effectively Administering Agreements

The most effective method of administering multiple agreements on a project is to address commonly encountered provisions before they become the center of a dispute. A project team that takes the time to be proactive and establish a manual of policies and instructions for field and project level personnel to rely upon during the project is steps ahead of the project team that has to retreat to the home office to deal with each of the inevitable unknowns in the construction process. To that end, most projects would be well-served if each project team assembled a book or binder of such policies and instructions.

Without such a procedure for claims identification and prosecution, a foreman who discovers an unidentified utility



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service line during a renovation project might note his discovery in a daily log, but otherwise not take action, and seriously damage his employer's entitlement to recover any compensation for additional costs or time associated with working around the line. Likewise, an owner's project manager who is unfamiliar with the relationships and procedures contained in his contracts with his contractor or construction manager and with his design professional might fail to understand his obligations when he learns of potential conflicts between drawings and specifications from his designer.

Conversely, the project team that can turn to a set of easy-to-understand policies for managing conflicts in contract documents, delays, changes to the project and any other issues is in an infinitely more advantageous position to address, document and prosecute a claim. A project manual that provides the forms, letters and flowcharts needed to address and document situations on a real-time basis will put project personnel in a position to be even more proactive.

### Documenting Claims

To the extent that a claim is not resolved at the project level, it can not be disputed that the better documented a party's claim is, the more likely the chances of success.

A party attempting to argue its entitlement to compensation or an

extension of time needs to rest that entitlement upon some documentary evidence. Once a claim leaves the people who see the project on a daily basis and might be aware of the more subjective elements of the claim (e.g., were the marble counter tops supplied of the same quality that was promised?), the most reliable basis for negotiating or litigating the claim is the documentation in the project file.

For those who are working for or advising an owner, contractor, design professional or any other organization involved in a construction project, the best practice can be to have the project team compile and record the real-time cost implications of potential claims. It will always be extremely complicated – and expensive – to hire an expert to try to recreate the impact a claim will have. The organization that has policies in place for the people most familiar

with the nuts and bolts of the project to identify issues on a daily basis will be at a significant advantage when claims are being resolved or litigated.

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