



Mortgage break-up fees - by Thomas Kearns

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Is a \$2 million break-up fee in a term sheet for a \$250 million mortgage “grossly excessive” and “not customary in the industry?”

We may soon find out as a result of a lawsuit brought in New York under New York law against Avison Young involving the former JC Penney headquarters in Plano, Tx. The suit was brought by Dreien Opportunity Partners LLC against Avison and is before judge Paul Oetken in the Southern District of New York. The facts recited here appear in an opinion issued September 30th, 2019, rejecting in large part Avison’s motion to dismiss.

Avison Young was hired by the purchaser to arrange \$460 million in financing for the purchase of the property. Avison Young obtained term sheets from two lenders to make up the total needed:

One from Och-Ziff for \$250 million; and
One from Cindat for \$80 million.

The Och-Ziff term sheet provided that, “In the event that [purchaser] obtains a loan for the property from anyone other than an affiliate of [Och-Ziff] prior to December 31st, 2016, the [purchaser] must pay a break-up fee to [Och-Ziff] in the amount of \$2 million.”

Three weeks later, Cindat elected not to proceed with its share of the financing and the purchaser was forced to go to a different financing source. It appears that the break-up fee was payable even if Och-Ziff didn’t close due to Cindat’s withdrawal. The opinion is silent as to the relationship between Och-Ziff and Cindat.

After closing, Och-Ziff sued the purchaser for the break-up fee and the purchaser sued Avison Young for professional negligence. The purchaser alleges that Avison Young failed to advise the purchaser that the break-up fee was “not customary in the industry,” “was grossly excessive,” and “should not have been included in the agreement.” Surprisingly, the opinion does not spend much time on why a sophisticated purchaser who signed a term sheet with a break-up fee should be relieved of the obligation. The court recites: “... [the] complaint states that Avison Young failed to provide Dreien with multiple options for each component of the capital stack...and did not, therefore, provide Dreien with any alternatives to Och-Ziff...”

The opinion held that the complaint should not be dismissed at this early pleading stage.

A trial may ensue and Avison Young may be reaching out to experts to testify as to the practice and reasonability of break-up fees in mortgage transactions and that in the circumstances of this case the break-up fee was appropriate.

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