

PRE-NEGOTIATION OR PRE-WORKOUT AGREEMENTS

By Steven M. Alden and John M. Nolan

As one of our panelists succinctly asked, “If it’s called a pre-negotiation agreement, why does it take so long to negotiate?” Indeed, the pre-negotiation agreement should not require any negotiation. Attached are two Annexes -- Annex 1 is a “standard” Pre-Negotiation Agreement drafted by Lender’s Counsel. Annex 2 is a Discussions Agreement which accomplishes the primary purpose of the pre-negotiation agreement and should require little or no negotiation prior to signing. (The language in bold face type in italics contained in the Annexes is language which may prove controversial and is therefore not always included.)

Standard Provisions

A pre-negotiation agreement should include several standard provisions which readily evidence the purpose of the pre-negotiation agreement.

1. **Discussions.** The parties – the borrower, the lender and the guarantor – plan to meet and conduct discussions about the loan and the loan documents, in the hope of resolving and settling issues which have arisen. No party shall incur any liability by reason of these discussions, and participating in the discussions shall not constitute or be deemed to be a waiver of any rights.
2. **Non-Binding.** All discussions will be non-binding. The parties will be bound only by agreements in writing signed by all parties.
3. **Not Admissible.** The discussions may not be used or quoted in any legal proceeding and are not admissible as evidence.
4. **Termination.** Any party may terminate the discussions at any time.
5. **Voluntary.** All parties have voluntarily agreed to conduct discussions on these terms, and no party has been coerced into participating.
6. **Governing Law.** The law of a designated State, which may or may not be the State where the real estate is located, governs the pre-negotiation agreement.
7. **Loan Documents.** It is also common to add that the only obligations of the parties are those set forth in the Loan Documents and the Loan Documents are in full force and effect. Even this seemingly innocuous addition can, however, become controversial and it is not always included.
8. **No Waiver.** Lenders are often anxious about signing any agreement with a defaulting borrower. Accordingly, they seek to add a no waiver paragraph providing that the pre-negotiation agreement and the discussions do not effect a waiver or forbearance or constitute an agreement by the lender to delay the exercise of its rights or

remedies or to amend or otherwise affect the rights or obligations of any party under any of the loan documents.

Additional Lender Provisions

Lenders typically request additional provisions, including

1. **Confirmation of Debt.** A statement by the borrower and guarantor confirming the outstanding amount of the debt and listing the instruments evidencing, securing and guaranteeing the indebtedness.
2. **Acknowledgement of Default.** An acknowledgment that the loan is in default and specifically identifying the monetary defaults.
3. **No Defenses.** A statement by the borrower that it has no defenses, offsets or counterclaims to its obligations under the loan documents and a waiver of any defenses, offsets or claims that may exist. If the borrower is unwilling to waive any defenses or claims, the lender will typically ask the borrower to identify any such defenses or claims. If the lender has completed its due diligence and “perfection check”, it may have discovered issues it would like to clean up. Unfortunately for the lender, these issues may have to wait for the next step -- the forbearance agreement.
4. **Compensation.** Lenders sometimes require compensation – at least reimbursement of lender’s counsel fees and expenses – for participating in the discussions. We have, however, participated in discussions where the borrower absolutely refuses to pay lender’s counsel fees.

Additional Borrower Provisions

Borrowers may request additional provisions, including

1. **Standstill; Forbearance.** The borrower may seek some relief or temporary forbearance on current payments while the parties are holding discussions. If the lender agrees to a standstill, it should be mutual and the lender should include a carveout for the pursuit of relief in the event of threatened or actual damage or injury to or waste of the collateral security.
2. **Access to Property Receipts.** The borrower may seek some release of funds from the lockbox or cash management agreement while the parties are holding discussions.
3. **Communication with Third Parties.** All parties may request the right to communicate with third parties, e. g. loan purchasers, equity providers and additional guarantors, while the discussions are proceeding.

Conclusion

The primary purpose of the pre-negotiation agreement is to foster an open, protected dialogue among the parties. This is accomplished by establishing a simple principle – that the parties’ discussions are not binding, not discoverable and not admissible, and will not be used against any party.

[BANK LETTERHEAD]

[DATE]

NEGOTIATION LETTER

[VIA HAND DELIVERY] [VIA FEDERAL EXPRESS]

ADDRESS FOR BORROWER

Attention: _____

[VIA HAND DELIVERY] [VIA FEDERAL EXPRESS]

ADDRESS FOR GUARANTOR

Attention: _____

Re: _____ ("Lender") loan (the "Loan") to _____ ("Borrower") concerning the property located at _____, as more particularly described in that certain **[PICK ONE] [Loan Agreement between Borrower and Lender dated _____ (the "Loan Agreement")]; initially capitalized terms used herein but not defined have the meanings set forth in the Loan Agreement] [Deed of Trust executed by Borrower in favor of Lender dated _____ (the "Deed of Trust")]; initially capitalized terms used herein but not defined have the meanings set forth in the Deed of Trust]**

Ladies and Gentlemen:

The parties desire to initiate communications (the "Communications") about (a) the rights and obligations under the documents evidencing, securing or otherwise pertaining to the Loan (the "Loan Documents") and (b) a possible modification, amendment, forbearance, additional collateral pledge or other resolution of current Loan issues (a "Resolution"). To facilitate and to induce Lender to commence Communications, the parties hereby agree that the following terms and conditions govern the Communications:

1. No party is under any obligation to agree to any Resolution. Any party may terminate Communications at any time, for any reason or no reason, in its sole discretion, with no liability. No party shall have any rights or liabilities, either express or implied, on account of (a) the commencement, continuation, or termination of Communications or (b) any oral understanding, unless and until the parties have (in their sole and absolute discretion) approved, signed, and exchanged a written agreement specifically addressing a Resolution, and all required consents have been obtained (an "Agreement"). This letter does not reflect an intention to