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Texas Annotated Subordination, Non-Disturbance and Attornment Agreement

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INTRODUCTION

Though a fixture in transactions involving commercial real estate, Subordination, Non-Disturbance and Attornment ("SNDA") agreements are often overlooked or misunderstood by the parties responsible for their drafting and negotiation. The purpose of this Annotated SNDA (this "Article") is to provide an introduction to SNDAs in Texas, describe some of the most commonly negotiated provisions, and offer an overview of the key issues that lenders, landlords and tenants should consider in negotiations. Ideally, this Article will serve as a tool to practitioners and their clients in preparing both leases and SNDAs. The footnotes provided in this Article draw upon statutes, case law and practical observations with the goal of providing general guidance to promote more efficient leasing and financing transactions.

Overview of SNDAs. SNDAs are typically three-party agreements between a lender, a tenant and a landlord/borrower. The need for an SNDA arises where a borrower seeks to transfer, acquire or refinance property that is leased to one or more tenants. The future rental stream produced from commercial property will serve as the collateral for a lender's loan to either the landlord/borrower or to a third-party purchaser of the property. As a result, a lender will require agreements from the tenant and landlord regarding the rights of the various parties, the relative priorities of the lien and lease interests, and the consequences of foreclosure. This agreement will most often take the form of an SNDA. Tenants look to SNDAs for reassurance that their lease will continue despite a landlord's loan default and a lender's foreclosure. Landlords often view SNDAs as a necessary obstacle to accomplishing its financing goals, aiming to have the document executed as quickly and efficiently as possible.

The Importance of SNDAs. SNDAs allow lenders, landlords and tenants to collectively plan for the worst case scenario—foreclosure. In the event of foreclosure and in the absence of an SNDA, state law will determine whether and under what circumstances a commercial lease is extinguished and what rights and obligations survive foreclosure. There are a number of problems with this arrangement that are readily apparent to most lenders and tenants. First, there is not a significant body of case law interpreting SNDAs, which makes it difficult to anticipate how courts might address various situations and how they might interpret certain SNDA provisions. Second, the laws in each state vary greatly as to the factors that determine lien priority (i.e., recording statutes, "lien theory" and "title theory" foreclosure laws, determination of actual and constructive knowledge and notice requirements). Finally, default state law positions on these issues will, in certain circumstances, make risks difficult to calculate, creating obstacles to financing that cannot be overcome. SNDAs contractually modify lien positions, lease rights and party obligations, providing certainty to lenders and tenants.

Before the SNDA: Leverage, Leases and Loans. Planning for a successful SNDA negotiation must begin long before an SNDA is requested by a lender or tenant. Commercial leases will often include provisions requiring a tenant to execute an SNDA on request, requiring non-disturbance guaranties from lenders, or allowing subordination of the lease or a lien at the option of the lender. While not a focus of this Article, Appendix A contains a sample lease provision that is fairly typical where an SNDA is contemplated at the time of lease execution. A landlord should be aware that any lease provision, especially non-market concessions, could impact future financing opportunities. Further, a landlord/borrower should know at the loan application and commitment stage what types and number of SNDAs will be required in

connection with the contemplated loan transaction. Exposing and addressing potential problems in advance (at the lease and early loan stages) will pave the way for an SNDA that satisfies all parties involved. No two SNDA negotiations will be identical, as the particular goals and bargaining positions of the parties will vary widely. Therefore, just as with any other contract, attorneys must be aware of these factors and remain flexible in negotiations.

The Role of the Landlord. While the key players in the SNDA negotiation are the lender and the tenant, the role of the landlord is often inappropriately minimized or dismissed. Landlords have a vested interest in ensuring that an SNDA is executed. Moreover, it is in the landlord's interest to have the process resolved as quickly and efficiently as possible. In most cases, the landlord/borrower will be responsible for its own attorneys' fees as well as those of the lender. Though many lenders will prefer to negotiate directly with tenants, some will require the landlord to play the role of mediator. Throughout the process, the landlord/borrower can add significant value by opening lines of communication, ensuring that any breakdown is not permanent and keeping the negotiations moving toward execution.

Final Notes. The annotations in this Article are not intended to constitute a legal opinion and are not and cannot be dispositive of every issue or factual circumstance that a practitioner or party will encounter in the negotiation and preparation of an SNDA. As with any general legal form, the practitioner must tailor the agreement to the specific needs of the client and the factual context of the given transaction. Reference is made throughout to several annotated forms, including the Annotated Assignment of Rents, the Annotated Deed of Trust, and the Annotated Guaranty prepared by the attorneys of Winstead PC. These documents have been published and presented on numerous occasions by various Winstead PC attorneys.

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