***Lapatin on the Law***

CLOSING TIME

What we typically explore on these pages are the daily interactions between landlords and their tenants, from finding good ones to evicting bad ones. A different set of issues and concerns comes into play when an apartment building is being bought or sold. Anyone involved in such a transaction should be sure to engage the services of an experienced real estate attorney who can shepherd the transaction successfully to closing. Beyond that, it’s important to understand that rental housing is investment property, and the value of that investment has much to do with the tenants who populate the building.

A purchase and sale agreement will typically give the buyer the right to conduct various “due diligence” activities, including a physical inspection of the property in order to identify defective conditions which might someday entitle tenants to withhold rent. To the extent that the inspection includes looking at individual apartments, remember that such access is allowed only if a landlord is permitted under the terms of a lease to show an apartment to a prospective purchaser. The courts have suggested that the landlord will need to work with the tenant in order to find a mutually acceptable time when the visit can take place. Hopefully a sufficient number of tenants will be willing to let the buyer confirm that the building has been well-maintained.

The purchase and sale agreement will customarily include various warranties and representations which can be relied upon by the buyer. For example, the seller may be asked to verify that:

* An attached schedule provides complete and correct information regarding the names of the tenants, how much rent they pay, when the lease term ends and the status of any security deposits or advance payment of last month’s rent.
* No rent arrearages exist nor are there any other outstanding defaults.
* No tenant has alleged that the landlord has breached the lease.
* No eviction proceedings or other litigation is pending.

One issue which invariably arises is whether these warranties and representations will survive the closing. The seller will want to be relieved from any further liability once title changes hands while the buyer would prefer to keep the seller on the hook if it’s subsequently discovered that the seller’s assurances were misleading. The parties will usually negotiate a limited time period, such as six months, during which the warranties and representations will remain in effect post-closing.

The buyer may wish to approve the reletting of any vacant apartments prior to the closing or may insist that any unrented apartment be spruced up and ready for occupancy.

In addition to a deed conveying title to the property, the parties will normally enter into an agreement at closing assigning all of the existing leases to the buyer. As part of this document, the seller will in most instances remain responsible for any tenant claims relating to the period prior to the sale, while the buyer will assume liability for anything which transpires thereafter. The buyer will want to take physical possession of all tenant files, including original leases and correspondence.

The buyer and seller should each sign notices which will be sent to the tenants in order to let them know that the sale has occurred and that any future rent payments or correspondence should be directed to the new owner. If a tenant has paid a security deposit or last month’s rent in advance, the notice must also include provisions assuring the tenant that the new owner will properly account for the money. If any escrowed security deposit is being transferred to a new bank, the tenants should be so informed, including the name and location of the bank and the relevant account number.

What happens if rents are delinquent at the time of closing? The purchase and sale agreement is likely to contain a clause obligating the buyer to use reasonable efforts to collect the amount due for the seller’s benefit. Any collection costs incurred by the buyer would be deducted and the buyer may also take the position that any funds received from the tenant should first be applied to rents accruing after the closing. The seller sometimes retains the right to pursue the tenants for whatever they owe, but since the seller no longer owns the property, an eviction can no longer be threatened.

There may occasionally be situations in which an eviction action is already pending at the time of closing. In a recent court decision, *Fannie Mae v. Branch*, the Massachusetts Supreme Judicial Court indicated that the buyer would be able to intervene in the case, which could then be continued to completion. The original plaintiff, i.e., the seller, would have to remain in the suit to the extent that the tenant had previously raised any counterclaim related to the period prior to closing.

The resolution of disputes between a seller and a buyer will depend primarily upon the wording of the purchase and sale agreement, meaning that nothing should be taken for granted by either party. These agreements are long and complex and tend to be aggressively negotiated. Be aware of the pressure points and make sure that you have a capable attorney in your corner.

Philip S. Lapatin