

**Presented:  
DBA REAL PROPERTY SECTION MEETING**

November 12, 2007  
Dallas, Texas

**Subordination, Nondisturbance and Attornment  
Agreements**

*by*

Keenan Kolendo  
Haynes and Boone, LLP  
901 Main Street, Suite 3100  
Dallas, Texas 75202  
keenan.kolendo@haynesboone.com

**SUBORDINATION, NONDISTURBANCE AND ATTORNMENT AGREEMENTS<sup>1</sup>**

**TABLE OF CONTENTS**

- I. SCOPE AND INTRODUCTION ..... 1
- II. FORECLOSURE OF THE FEE - ITS EFFECT ON THE LEASE ..... 1
  - A. Lease Superior to Mortgage..... 1
  - B. Mortgage Superior to Lease..... 3
- III. RULES FOR DETERMINING PRIORITY ..... 5
  - A. Inception of Mortgage Lien Priority ..... 5
  - B. Inception of Lease Priority..... 5
  - C. Subrogation and its Effect On Priority..... 6
- IV. SUBORDINATION, NON-DISTURBANCE AND ATTORNMENT AGREEMENTS.. 8
  - A. Definition ..... 8
  - B. Elements..... 8
    - 1. Subordination..... 8
    - 2. Non-Disturbance ..... 8
    - 3. Attornment ..... 8
- V. DRAFTING AND NEGOTIATING CONSIDERATIONS..... 9
  - A. Common SNDA Provisions Requested by Lenders and Possible Tenant Responses ..... 10
  - B. SNDA Provisions Tenants May Request and Possible Lender Responses..... 13
- VI. LENDER’S LEASE REVIEW CHECKLIST ..... 16

---

<sup>1</sup> This outline is built and based upon an original outline prepared (*circa* more than a few years ago) by Robert McCulloch, Haynes and Boone, LLP, who should receive all credit for the insight and ideas found in this outline.

## **SUBORDINATION, NONDISTURBANCE AND ATTORNMENT AGREEMENTS**

### **I. SCOPE AND INTRODUCTION.**

A purchaser acquiring rental property at a foreclosure sale faces certain risks associated with tenants who are leasing all or part of the collateral. The purchaser may have unknowingly or unwillingly assumed the prior landlord's obligations. The purchaser may be liable for damages arising out of the prior landlord's conduct. The purchaser may be bound by lease amendments of which the purchaser has no notice, including amendments creating substantial monetary obligations or expanding or contracting the size of the leased premises, and even amendments decreasing the rental or changing the term of the lease. The purchaser may even encounter personal liability for the landlord's wrongful acts.

Similarly, any tenant preparing to occupy space needs to consider the effect a landlord's mortgage default may have on the tenancy, including the possibility that through the loan default and without any notice to the tenant, the landlord's interest in the property can be sold and the lease terminated—a sobering prospect, no doubt, to a tenant who may have invested a fortune in the premises and may have fully performed each of his obligations under the lease.

The Subordination, Nondisturbance and Attornment Agreement (or “*SNDA*”) is the common way of addressing these risks. First, this outline addresses the effect of a foreclosure on a lease and how the result differs depending on whether the lease is superior to the mortgage (this outline makes no distinction between a mortgage or deed of trust and uses the term “mortgage” to refer to either type of lien). Second, this outline briefly covers the rules for determining the relative priorities of a lease and a mortgage on the property. Third, the discussion focuses on using the SNDA as a means of mitigating the risks associated with default and foreclosure. Finally, this outline addresses typical SNDA provisions and points to consider in drafting and negotiating leases and SNDAs.

### **II. FORECLOSURE OF THE FEE - ITS EFFECT ON THE LEASE.**

As a general rule, the effect of a foreclosure on a lease will typically hinge on whether the lease is superior to the mortgage. As discussed below, however, there may be some steps the lender can take unilaterally that will influence the effect of the foreclosure on the lease.

#### **A. Lease Superior to Mortgage.**

If a lease is superior to the mortgage, a foreclosure of the mortgage will not affect the lease. The purchaser at foreclosure is simply substituted for the former landlord. In that situation, the purchaser's concerns are virtually the same as the concerns a potential purchaser might have in a voluntary transaction. Unlike a voluntary transaction, however, the purchaser at foreclosure cannot depend on a willing landlord to obtain estoppel letters, provide copies of lease documents and files and enable the prospective purchaser to interview the tenants. Therefore, the purchaser at foreclosure may have difficulty assessing the risks associated with stepping into the prior landlord's shoes. These risks include, but are not limited to, the following unknown variables: the terms of the lease, whether there are any unresolved disputes between the landlord

and tenant (particularly claims by the tenant against the landlord that might lead to rental offsets or monetary claims against the new landlord), whether the tenant is in possession and paying rent, or whether the tenant has accepted the landlord's performance regarding premises improvements, repairs, maintenance or other obligation performable before the foreclosure. In the absence of satisfactory answers to these questions, the lender or any other prospective purchaser should be aware that substantial risks exist that may not be known until after the foreclosure. In this situation, if the lease is superior to the mortgage, the purchaser will acquire the interest of the former landlord subject to whatever lease terms, claims, offsets and liabilities that may exist between the tenant and the former landlord at the time of foreclosure. If the purchaser at foreclosure assumes the lease, expressly or by operation of law, then the purchaser generally steps into whatever liabilities the former landlord had to the tenant as of the date of the foreclosure.

In *F. Groos and Co. v. Chittim, et. al.*, 100 S.W.1006 (Tex. Civ. App. 1907, no writ), the court stated the following regarding the effect of foreclosure on a lease having priority over the mortgage:

[I]f the lease is anterior to the mortgage, the possession of the tenant being notice of his rights thereunder, his leasehold estate and his right thereto are not affected by foreclosure of the mortgage. A change of landlords is only effected. Instead of being the tenant of the mortgagor, [the tenant] becomes the tenant of the mortgagee, or of him who by the foreclosure has acquired the reversion. He [the tenant] has every right against his new landlord that he had under the lease against the original lessor and he who acquired the reversion at the foreclosure has every right against him [the tenant] that the lessor had under the lease. The one who acquired the reversion stands in the shoes of the mortgagor. The lessee stands in his own, just as he did before. If, before the foreclosure, the lessor was entitled to receive from the lessee the rents and profits occurring under the lease, after the foreclosure the one who acquired thereunder the reversionary estate is likewise entitled to receive them. *And it would seem a logical sequence that, if the original lessor were not entitled to receive from the tenant the rents and profits accruing under the lease, he who acquired his title under the foreclosure proceedings would not, ordinarily, be.* *Id.* at 1010 (emphasis added).

In *Ontiveros v. MBank Houston, N.A.*, 751 F. Supp. 128 (S.D. Tex. 1990), the court provides an excellent analysis of the potential pitfalls existing for a lender foreclosing a lien that is subordinate to the lease. Ontiveros was the tenant in possession under a lease that predated the mortgage. Apparently, there was no other agreement between the tenant and the lender. Subsequent to the date of the mortgage, the landlord and the tenant modified their lease to settle a dispute and, among other agreements, the landlord agreed to pay the tenant an improvement allowance of \$125,000 on October 1, 1985. In July, 1985, the lender foreclosed and notified the tenant to make all rent payments to it. The tenant made rent payments for July, August and September, 1985. On October 1, 1985, the lender failed to pay the tenant the \$125,000 due under the lease amendment, and the tenant sued. The court's following holdings are helpful teachings regarding the relationship of a foreclosing lender and a tenant whose lease predates the mortgage:

- a. The lease was superior to the mortgage. *Id.* at 130.
- b. The fact the lease was not recorded was irrelevant to the determination of priority. The lender was on constructive notice of the rights of the tenant due to the tenant's possession of the premises. Further, the tenant's possession charged the lender with knowledge of the terms of the lease. *Id.* at 130.
- c. The mortgage was inferior to the lease modification, even though it occurred subsequent to the mortgage. "A mortgagee with knowledge that a third party possesses the mortgaged property must inquire into the terms of the original lease and bind the mortgagor not to alter the lease to protect its interests." *Id.* at 130-131.
- d. By demanding and accepting rent, the lender ratified the lease and assumed the landlord's liabilities under it. *Id.* at 131.
- e. The lender's failure to pay the \$125,000 caused the tenant to be unable to complete its renovation which rendered the premises unsuitable for the tenant's purposes. The landlord's breach effectively evicted the tenant, and the tenant was not liable for rent after the eviction occurred. *Id.* at 131.

*Ontiveros* teaches us that, absent a contractual arrangement between the lender and the tenant, if a lease is superior to a mortgage, the purchaser at foreclosure acquires the property subject to the lease and to any and all claims, offsets and defenses that may exist under the lease against the previous landlord. Further, by accepting rent from the tenant, the landlord assumes the lease and becomes personally liable for the claims that may exist against the landlord. *See also M.G. Building Materials, Ltd. v. C&K Materials Co., Inc.*, No. 04-04-00173-CV, 2004 WL 2715912 (Tex. App.—San Antonio, 2004) (holding that a superior lease is not extinguished by foreclosure).

## **B. Mortgage Superior to Lease.**

If the mortgage is superior to the lease, then a non-judicial foreclosure, without more, will generally terminate the lease. However, if the tenant remains in possession and the landlord accepts rental payments, then at some point, the parties' conduct will be considered to have bound them to the terms of the terminated lease. A number of Texas courts have considered this situation and have provided guidance as to the relationship of the tenant and the new purchaser—what conduct is necessary to create a new tenancy relationship and the terms of that new relationship.

In *United General Insurance Agency of Midland, Inc. v. American National Insurance Company*, 740 S.W.2d 885 (Tex. App.—El Paso 1987, no writ), the court considered the effect of a non-judicial foreclosure on a lease subsequent and inferior to the foreclosed mortgage. The

tenant remained in possession and sought a declaratory judgment construing the relative rights and obligations of the tenant and the mortgagee (who had purchased the mortgaged property at the foreclosure sale). The trial court held for the mortgagee and ruled that the mortgagee had the unilateral election, following foreclosure, either to deem the lease terminated or to hold the tenant to the terms of the lease. On appeal, the court of appeals held that the non-judicial foreclosure had the effect of terminating the lease, unless the mortgagee and the tenant both expressly or impliedly agreed to continue the lease. *Id.* at 886-87.

In *ICM Mortgage Corporation v. Jacob*, 902 S.W.2d 527 (Tex. App.—El Paso 1994, writ denied), the court attempted to clarify its holding in *United General* by requiring affirmative action manifesting consent to the creation of a lease. The court explained that foreclosure terminates an inferior lease. *Id.* at 531-532. Any landlord-tenant relationship between the tenant and a purchaser at foreclosure of a superior mortgage is a new, independent landlord-tenant relationship (rather than continuation of the old lease/relationship), the terms of which, however, may be modeled implicitly on the tenant's lease with the prior owner. *Id.* at 532-533. The court stated that its use of the word "continue" to describe the existence of a post-foreclosure landlord-tenant relationship in its *United General* opinion (i.e., to continue a lease after foreclosure) did not imply that a foreclosing purchaser's failure to take action to terminate the *Jacob* appellee's lease established (or, in the vernacular, "continued") a landlord-tenant relationship. The court found "irrelevant" the argument that the mortgagee failed to take action to terminate the lease in question and gave instructions that the lessee "sit tight" until it obtained clear title to the property. The court explained:

Our focus (in *United General*) was the necessity for both parties to have affirmatively manifested consent to a new lease agreement, not to the extent to which either had failed to object to the mere continuation of a previous agreement. To the extent we implied a different focus, we now disavow it. *Id.* at 533.

This rule is consistent with the effect of foreclosure on other interests in real property: Subject to the effect of the expressed or implied agreement of the parties, foreclosure normally cuts off interests in real estate that are subordinate to the mortgage. *See also Callewart v. KPT, Inc.*, No. 05-95-01454-CV, 1996 WL 616436 (Tex. App.—Dallas, 1996, n.w.h.) (agreeing with the court in *Jacob* and reiterating the general rule that upon foreclosure, a tenant's lease is terminated).

The parties do not, however, have to expressly articulate affirmative consent to a landlord-tenant relationship. The parties' conduct subsequent to foreclosure can effect an implied agreement to create a tenancy. *Peterson v. NCNB Texas National Bank*, 838 S.W.2d 263 (Tex. App.—Dallas 1992, no writ), is a prime illustration. NCNB foreclosed on leased property pursuant to a mortgage that was superior to the lease. A few days after the foreclosure, NCNB sent the tenant a notice advising of the change of ownership and directing the tenant to make future rental payments directly to NCNB. The tenant subsequently made two regular rental payments to NCNB. Approximately two months after the foreclosure, NCNB sent the tenant a second, more formal letter in which NCNB expressly recognized the lease and sent a form requesting the tenant formally to confirm the continued existence of the lease. The tenant did not sign the agreement NCNB tendered but made two more rental payments. Thereafter, the tenant

defaulted under the lease, and NCNB sued the tenant for unpaid rent. The tenant's defense was that the lease was subordinate to the deed of trust lien and therefore terminated upon foreclosure. In opposition, NCNB contended that though the tenant had not signed a formal confirmation of the lease, the tenant should be deemed to have affirmed the lease because the tenant remained in possession of the premises and paid rent for four months after receiving knowledge of the foreclosure. The court held in favor of NCNB, stating “[t]he payment of rent with full knowledge of the foreclosure sale and the failure to take timely action to disaffirm the lease is sufficient evidence, as a matter of law, to show that [the tenant] affirmed the lease.” *Id.* at 267.

### III. **RULES FOR DETERMINING PRIORITY.**

Given the dramatic difference in effect between foreclosure on a lease that is subordinate and foreclosure on a lease that is superior to the mortgage, it is important to know how to determine the priority between the lease and the mortgage.

#### A. **Inception of Mortgage Lien Priority.**

Generally speaking, a mortgage lien will take priority over any lease granted subsequent to the date the mortgage is properly recorded. Even without actual knowledge of a mortgage, all persons are charged with knowledge of a properly recorded instrument. Section 13.002 of the Texas Property Code provides that “[a]n instrument that is properly recorded in the proper county is notice to all persons of the existence of the instrument.” (Vernon 2004). (Note, however, that pursuant to Section 13.001(a), “[a] conveyance of real property or an interest in real property or a mortgage or deed of trust is void as to a creditor or to a subsequent purchaser for a valuable consideration without notice unless the instrument has been acknowledged, sworn to, or proved and filed for record as required by law.” (Vernon 2004).)

#### B. **Inception of Lease Priority.**

A lease’s relative priority will be established on the earlier to occur of the date the tenant takes possession of the premises or the date the lease or a memorandum of the lease is properly recorded. A tenant’s possession of the leased premises is notice to the world of the tenant’s interest and imposes a need on subsequent third parties, such as mortgagees, to inquire as to the terms of the lease, even when the lease is not recorded.<sup>2</sup> *Liedeker v. Grossman et al.*, 206 S.W.2d 232 (Tex. 1947); “*Moore*” *Burger, Inc. v. Phillips Petroleum Co.*, 492 S.W.2d 934 at 939 (Tex. 1972). Thus, in Texas, unlike some other jurisdictions, recording a memorandum of lease is not required to establish the priority of a leasehold interest unless the parties desire to establish a priority date prior to the date of the tenant’s first occupancy (as in the case of a ground lease or build to suit lease in which the tenant’s possession of the premises may not be apparent).

---

<sup>2</sup> Exceptions to this rule exist, including without limitation: (i) instances where the type of possession is not sufficient to put a prospective purchaser on inquiry of a tenant’s interest in the property [see *Jackson v. DeGuerin*, 77 S.W.2d 1041 at 1042 (Tex. 1935)]; and (ii) instances where the party in possession of the property has secretive claims that would not have been discovered by a purchaser exercising reasonable diligence [see *Dallas Trust & Savings Bank v. Pickett*, 59 S.W.2d 1090 at 1093-1094 (Tex. Civ. App. Waco 1933), writ dismissed].

C. **Subrogation and its Effect On Priority.**

A real estate development often begins with a land loan providing funds for the initial acquisition, followed by a construction loan to fund construction of the improvements, followed by a permanent loan placed on the property after it has been leased and tenants are in possession and paying rent. Fortunately for the permanent lender, through the doctrine of subrogation, the priority of the permanent lender's lien will often relate back to a date many years before the date of the new loan.

The doctrine of subrogation is an equitable doctrine that, for purposes relevant to this discussion, allows the inception of a mortgagee's priority to relate back to a date earlier than the date the mortgage was recorded. Under this doctrine, one who advances funds to pay off a prior lien is allowed to stand in the shoes of the prior lien holder. *Blaylock v. Dollar Inns of America, Inc.*, 548 S.W.2d 924 at 933 (Tex. Civ. App.—Tyler 1977, n.w.h.), *rev'd on other grounds*, 576 S.W.2d 794 (Tex. 1978); *Texas Commerce Bank N.A. v. Liberty Bank*, 540 S.W.2d 554 (Tex. Civ. App.—Houston [14th Dist] 1976, no writ); *Providence Institution for Savings v. Sims*, 441 S.W.2d 516 (Tex. 1969). In *Blaylock*, the court held that even absent a writing to that effect, a lender advancing money that is used to pay off a prior lien will be subrogated to the prior lender's rights:

It has long been the law of this state that one who has advanced money with an understanding or under circumstances giving rise to an understanding that his advancement shall be secured by a first lien upon the property is not a mere volunteer and should be subrogated to the prior lien so discharged. *Blaylock*, 548 S.W.2d at 933.

Thus, for purposes of determining the relative priority of a lease and a mortgage, simply determining that the tenant's possession predated a mortgage may not be enough to know with certainty that the lease is superior to the mortgage. Further inquiry is necessary to determine whether a prior mortgage existed on the property and whether the prior mortgage was paid with the proceeds of the indebtedness secured by the subsequent mortgage.

*Med Center Bank v. Fleetwood*, 854 S.W.2d 278 (Tex App.—Austin 1993, writ denied) contains an excellent discussion of the impact of subrogation on the relative priorities of a lease and a mortgage. In 1984, Fleetwood and two other individuals formed a joint venture to construct a shopping center. After the shopping center was completed, but before permanent financing had been obtained, Fleetwood sold his interest in the joint venture for cash and a promissory note (the "Fleetwood Note") secured by a mortgage lien covering the shopping center. The parties also entered into a lease of two adjacent tracts of land whereby Fleetwood was granted a 55% undivided leasehold interest in the adjacent tracts for a term of 99 years. The lease was expressly subordinate to Fleetwood's lien. Subsequently, Nationwide advanced permanent financing to the joint venture for the shopping center. The permanent financing was secured by a mortgage covering the shopping center and one of the adjacent tracts (called "Tract A" in the opinion). Fleetwood expressly subordinated the lien securing the Fleetwood Note to the Nationwide mortgage. The closing of the permanent loan triggered a prepayment obligation under the Fleetwood Note, which the joint venture was unable to pay. After Fleetwood declared

the Fleetwood note to be in default, the joint venture cured the default by obtaining a loan from Med Center Bank. The Med Center loan was secured by a lien covering the shopping center and Tract A. Most of the Med Center loan proceeds were used to pay off the Fleetwood Note. Fleetwood executed a release of the lien that secured the Fleetwood Note. Thereafter, the joint venture defaulted on the Med Center loan and Med Center foreclosed on Tract A by non-judicial foreclosure. Fleetwood then contended that, since his 99-year lease predated the Med Center lien on Tract A, the foreclosure had no effect on the lease.

Since the Fleetwood lease was clearly first in time ahead of the Med Center lien, the question was whether Med Center was subrogated to Fleetwood's lien. The court framed the issue as follows:

[I]f Med Center was not subrogated to the rights under the Fleetwood's lien, its deed of trust, which was perfected later in time, is inferior to Fleetwood's lease interest. However, if Med Center was entitled to be subrogated to the Fleetwood deed of trust, its lien was superior to the lease . . . and its subsequent foreclosure extinguished the lease. *Id.* at 284.

In reaching its decision that Med Center was subrogated to the priority of the Fleetwood lien, the court entered into a thorough discussion of the doctrine of subrogation, stating among other things:

[o]ne who advances money to pay off an incumbrance on realty at the instance of either the owner of the property or the holder of the incumbrance, either on the express understanding, or under circumstances from which an understanding will be implied, that the advance made is to be secured by a first lien on the property, is not a mere volunteer, and in the event the new security is for any reason not a first lien on the property, the holder of such security . . . will be subrogated to the rights of the prior incumbrance under the security held by him, unless the superior or equal equities of others will be prejudiced thereby.... *Id.* at 285 (quoting *Fleetwood v. Med Ctr. Bank*, 786 S.W.2d 550 at 553-554 (Tex. App.—Austin 1990, no writ), internal citations omitted).

In analyzing a particular client's position with regard to the application of principles of subrogation, it is important to remember that in this context, subrogation is an equitable remedy, and its application may be limited if prejudice will result.

The Court in *Fleetwood* considered whether "superior or equal equities" existed that would preclude the application of subrogation principles. The court held that such prejudice did not exist, stating that "absent a showing that subrogation results in additional debt having priority over or parity with the intervening interest, a material change in the terms of the superior interest or other pecuniary loss resulting from the subrogation, there is no prejudice to intervening interest holders." *Id.* at 286.

#### IV. SUBORDINATION, NON-DISTURBANCE AND ATTORNMENT AGREEMENTS.

##### A. Definition.

Through the use of the SNDA, lenders and tenants are able to avoid the analysis and uncertainties incident to determinations of relative priorities of their respective interests in real estate and provide additional agreements that are generally in the best interests of both the lender and the tenant.

As the title of the instrument suggests, the SNDA contains several elements: (a) subordination of the leasehold interest to the mortgage; (b) the lender's agreement of non-disturbance in favor of the tenant and (c) the tenant's agreement of attornment in favor of the lender or other purchaser at a foreclosure sale. Although the foregoing elements are the major components of an SNDA, note that an SNDA may contain other elements as well.

##### B. Elements.

1. Subordination. The holding in *Ontiveros*, 751 F. Supp. at 128, gives a clear example of the reason lenders often require assurance that all leases have been subordinated to their mortgage. In anticipation of the lender's requirements, a standard provision of many leases is a specific subordination provision. In this provision, the tenant expressly subordinates its rights under the lease to the rights of any existing or future lender. Similarly, a subordination provision within an SNDA makes the tenant's rights under the lease subordinate and inferior to the rights of the lender's mortgage.

However, a simple subordination of the leasehold estate, without more, subjects both the mortgagee and the tenant to the risk of termination of the lease upon a foreclosure, a prospect both parties will generally want to avoid. The tenant will generally want to remain in possession of the leased space and the mortgagee will want assurance that it or its purchaser at a foreclosure sale will have the benefit of continued receipt of rental income after the foreclosure sale, provided that the tenant is not in default under the lease.

2. Non-Disturbance. The lender's covenant of non-disturbance in the SNDA is its agreement that, notwithstanding a future foreclosure, the landlord and tenant relationship will continue following the foreclosure, and the tenant's possession of the leased premises will not be disturbed, provided the tenant has complied and continues to comply with the terms of the lease. The lender's agreement of non-disturbance, however, probably does not give the lender what it is seeking: the tenant's reciprocal agreement to recognize the purchaser at the foreclosure sale as the new landlord and to render to that purchaser the benefits to which the former landlord was entitled.

3. Attornment. The concept of attornment dates back to medieval days in which the lord of a feudal estate would grant to another the services of his tenant. As a condition of the grant's effect, the tenant would attorn to the grantee with words such as "Sir, I attorn to you by force of the said grant", or "I become your tenant." Fisher and Goldman, *The Ritual Dance*

*Between Lessee and Lender--Subordination, Nondisturbance and Attornment*, 30 Real Property, Probate and Trust Law Journal 355 (1996).

In the context of today's real estate practice, and in particular this discussion, an attornment agreement is the tenant's agreement to "attorn to" or recognize a purchaser at foreclosure as the new landlord under the lease. The tenant's covenant of attornment is the tenant's agreement to render to the landlord all of the rights and benefits afforded the original landlord under the lease. Thus, in attorning to the purchaser, the tenant agrees that the purchaser is the holder of the landlord's interest in the leasehold estate and is entitled to receive the rental payments and other benefits to which the landlord is entitled under the lease. The SNDA will contain the tenant's agreement to the effect that if a foreclosure or conveyance in lieu of foreclosure occurs, the tenant will recognize the purchaser at the foreclosure sale as the landlord under the lease.

## V. DRAFTING AND NEGOTIATING CONSIDERATIONS.

For the reasons described above, whether you represent the landlord or the tenant, it is important to consider the need for an SNDA during lease negotiations.

From the landlord's perspective, whether or not the property is currently financed, it is critically important to maintain the property's attractiveness to lenders. If the landlord places leases that would be superior to future mortgages, the landlord may severely compromise the landlord's ability to obtain future financing or even to sell the property. The property will be less attractive to lenders because superior leases present all of the problems described in the *Ontiveros* case: potential lender liability for the landlord's pre-foreclosure defaults, the risk the lender will be bound by all lease amendments, including those made after the date of the financing, and the possibility the purchaser at foreclosure will be deemed to have assumed the lease by accepting rental payments. Therefore, the landlord should be sure the landlord's lease form makes the lease automatically subordinate to all existing and future financing of any kind and requires the tenant, upon request, promptly to execute and to deliver a subordination agreement expressly subordinating the lease to any liens. The landlord's lease form should also specify the number of days within which the tenant must sign and return the SNDA.

The tenant should be willing to agree to subordinate the lease to existing or future liens, but the tenant should condition its subordination on the lender's execution and delivery of a non-disturbance agreement in a form reasonably acceptable to the tenant. The tenant should determine if the project is currently subject to financing. If the property is currently financed, the tenant should insist upon obtaining an SNDA within a certain number of days after the date of the lease, or as a condition to the tenant's obligation to pay rent. The tenant should be careful not to assume mistakenly that a simple subordination agreement will be satisfactory. As discussed above, a subordination agreement without the lender's reciprocal non-disturbance agreement does not solve any of the tenant's problems because it will not assure that the lease remains in force or that the tenancy will not be disturbed.

Normally, the SNDA should be signed by the landlord as well as by the tenant and the lender in order to ensure the landlord is bound by whatever agreements concerning the lease are

contained in the SNDA. As with other documents affecting real property, an adequate description of the land and the deed of trust affected by the SNDA must be included. Although the practice is not uniform, best practice is probably to require recording the SNDA in the real property records of the county where the premises are located to ensure that a purchaser at foreclosure will have notice of the provisions of the SNDA and will take title subject to those agreements. If the property is not financed as of the date of the lease, the tenant should consider attaching a form of SNDA to the lease as the agreed form of SNDA the tenant will sign. This practice gives the tenant more negotiating strength in reacting to an unreasonable SNDA form a future lender might tender rather than simply rejecting the lender's unreasonable form. This practice may also save the tenant costs in reviewing and negotiating the SNDA at a later time. Landlords, however, often prefer not to include a form SNDA in the lease, leaving wider latitude to meet future lender's requirements. If the lease includes an agreed form of SNDA, the landlord should try to preserve some flexibility so a future lender's requirements can be accommodated if possible.

**A. Common SNDA Provisions Requested by Lenders and Possible Tenant Responses.**

In addition to the basic agreements mentioned above, the SNDA will generally contain provisions designed to protect the lender and/or the purchaser from risks at foreclosure, including the following:

- a. Lender's Objective— Mitigation of the risk of damage claims due to pre-foreclosure acts or omissions of a prior landlord, including the borrower (including construction defects, breach of repair and maintenance obligations).

Lender's Solution—Include in the SNDA a provision that the purchaser at foreclosure is not subject to damage claims for acts or omissions occurring before the foreclosure.

Possible Tenant Objection—If tenant is damaged by landlord's breach of the lease, it is unfair to cut tenant off from recourse.

Possible Negotiated Result—An SNDA provisions that the tenant's recourse is limited to set-off of tenant's actual direct damages resulting from costs incurred by tenant to cure landlord defaults and recovery of consequential damages is expressly waived.

- b. Lender's Objective—Mitigation of the risk that in advance of foreclosure, the landlord might collect rent in advance for periods following the foreclosure.

Lender's Solution—Include in the SNDA an acknowledgment that the lender is not bound by rental payments for periods following the date of foreclosure.

Possible Tenant Objection—If tenant actually pays rent in good faith, tenant should receive a credit—besides, the lender probably will not notify the tenant of the foreclosure in advance. Further, if the lender wants to protect itself, it has the right to trigger direct payment of rentals to the lender via the assignment of rents, which is a part of the loan documentation.

Possible Negotiated Result—SNDA will provide that the lender is not bound by rental payments for more than one month in advance of due date.

- c. Lender's Objective—Avoidance of the risk of lease amendments to which the lender did not consent.

Lender's Solution—Provide in SNDA that the lender is not bound by any lease amendment to which it is not a party.

Possible Tenant Objection—Until foreclosure, the lender is not a party to the lease, and waiting for the lender to approve lease amendments is too cumbersome and time consuming.

Possible Negotiated Result—An SNDA provision that specific types of amendments shall not be valid unless the lender's prior consent is obtained—such as amendments changing the rental rate, changing the term of the lease or agreements voluntarily terminating lease.

**Note**—If the SNDA is silent on this issue and the lease is subordinate to the lien, a subsequent lease amendment may not be binding on the lender unless consented to by the lender.

- d. Lender's Objective—Negating renewal, expansion or purchase options.

Lender's Solution—Provide in SNDA that upon foreclosure, all renewal, expansion and purchase options are void.

Possible Tenant Objection—These options may be critical to the tenant's business strategy or may represent the result of significant tradeoffs made in negotiating the lease.

Possible Negotiated Result—An SNDA provision that any options to purchase are inapplicable to the foreclosure sale (so the foreclosure, and any deed in lieu of foreclosure, does not trigger tenant's purchase rights), but confirming that any other options either contained in the lease as of the date of the SNDA or subsequently approved by the lender will remain effective.

- e. Lender's Objective—Assurance that tenant will honor assignment of rentals contained in loan documents.

Lender's Solution—Inclusion of an SNDA provision to that effect.

Possible Tenant Objection—Tenant does not want to get caught between two parties each contending it has the right to rent payments. Further, tenant does not want the lender to trigger the assignment of rentals and then not proceed with foreclosure, because this will cut off landlord's access to cash to repair and maintain the leased premises.

Possible Negotiated Result—An SNDA provision which provides for direct payment to lender for an agreed maximum period or a provision that rent shall be paid into escrow. In any event, the SNDA should contain the agreement of the landlord authorizing the tenant to make the payment as agreed, so the tenant can avoid being caught in the middle.

- f. Lender's Objective—Assurance that tenant will not terminate, cancel or surrender the lease prior to the end of the lease term.

Lender's Solution—An SNDA provision prohibiting termination, cancellation or surrender of the lease without lender consent.

Possible Tenant Objection—This prohibition could deny tenant the ability to exercise remedies for landlord's default. Further, even in the absence of default, the tenant wants the flexibility of dealing with the landlord, not the landlord and a loan officer the tenant has never met.

Possible Negotiated Result—Tenant agrees to give lender notice of landlord's default and an opportunity to cure before exercising remedies under the lease; or tenant agrees not to exercise the remedy of lease termination until the lender has been notified and has had an opportunity to cure.

- g. Lender's Objective—Avoidance of burdensome lease provisions identified during lender's due diligence lease review. [Example: indemnification obligations relating to matters not within the lender's control, such as environmental indemnifications.]

Lender's Solution—Require a lease amendment as a condition to closing the loan or as a condition to approving the lease; alternatively, inclusion of an SNDA provision containing contingent lease modifications that are effective only following foreclosure.

Possible Tenant Objection—Tenant is unwilling to permit the lender to pick out certain negotiated lease provisions while leaving others intact, because this changes the negotiated result of the lease.

Possible Negotiated Result—Tenant may be willing to amend the lease to clean up mistakes or inconsistencies identified by the lender. Tenant will probably not be willing to agree to SNDA provisions contingently modifying the lease unless the change is a deal killer or unless the Tenant receives other recourse or remedies.

**B. SNDA Provisions Tenants May Request and Possible Lender Responses.**

The tenant, when presented with a form of SNDA, may want to modify the SNDA to include the following elements:

- a. Tenant's Objective—Assurance the lender has approved the lease, including all expansion and extension options.

Tenant's Solution—Inclusion of lender's express consent to the execution of the lease, including all option terms, and lender's acknowledgment that tenant's exercise of the rights, remedies and options therein contained shall not constitute a default under the mortgage.

Possible Lender Objection—Lender will probably be willing to acknowledge the lease is approved, but unwilling to acknowledge tenant's exercise of certain rights and remedies under the lease will not be a default under the mortgage, as the loan may be dependent upon rental stream from the mortgaged property.

Possible Negotiated Result—An SNDA provision expressly approving the lease.

- b. Tenant Objective—Assurance that if foreclosure does occur, the purchaser at foreclosure will be deemed to have assumed liability for the covenants of the landlord under the lease.

Tenant's Solution—An SNDA provision that the purchaser at foreclosure will be deemed to have assumed liability under the lease and will be obligated to perform the duties of the landlord and provide the services to the tenant that the landlord is required to provide under the lease.

Possible Lender Objection—Lender may want to take the property "subject to" the lease, but without assuming liability.

Possible Negotiated Result—An SNDA provision containing the above assumption language, but limiting the liability of the lender/foreclosure purchaser to its interest in the mortgaged property.

- c. Tenant Objective—Assurance the tenant will be made whole if, prior to foreclosure, the tenant incurs expenses in curing defaults on the part of the landlord.

Tenant's Solution—Elimination of SNDA provisions exculpating the lender or foreclosure purchaser from pre-foreclosure landlord defaults.

Possible Lender Objection—Lender will be absolutely unwilling to give tenant an open ended indemnity for a prior landlord's defaults.

Possible Negotiated Result—An SNDA provision giving tenant set-off rights for pre-foreclosure expenses incurred due to landlord's default, perhaps conditioned on lender having been given notice of default and opportunity to cure.

- d. Tenant Objective—Assurance tenant will continue to receive the benefit of any rental inducements such as free rent, moving expenses, and construction allowances, for which the original landlord is obligated but which may not have been fully discharged as of the date of foreclosure.

Tenant's Solution—Inclusion of an SNDA provision to that effect.

Possible Lender Objection—Lender may be unwilling to become liable for discharge of tenant inducement costs not paid by landlord unless the payment obligation accrues after the date of foreclosure.

Possible Negotiated Result—Establish an escrow in the amount of unpaid tenant inducement costs; inclusion of SNDA provision giving tenant set-off rights up to a capped amount; inclusion of SNDA provision that lease termination is tenant's sole remedy for unsatisfied tenant inducement obligations.

- e. Tenant Objective—Assurance the provisions of the landlord's mortgage regarding condemnation and insurance proceeds do not conflict with the lease. **Note:** Ground lease tenants (most of whom will have built their own building at their own expense) will be very sensitive to anything giving the lender a right to seize insurance proceeds after a casualty event, especially if the lender has the right

to apply the proceeds against the loan rather than hold them to ensure their application to repair/restoration.

Tenant's Solution—Inclusion of an SNDA provision that condemnation and insurance proceeds will be applied as provided in the lease.

Possible Lender Objection—Lender may be unwilling to agree in advance that condemnation and insurance proceeds will not be applied against the unpaid balance of the loan, particularly if other tenants have the right to terminate their leases because of the damage, or if the damage occurs late in the term of the loan and might compromise the ability of the lender to obtain full payment at loan maturity or if the damage is late in the term of the lease.

Possible Negotiated Result—This will depend on property type (single tenant/multi-tenant), the type of lease (ground lease/building lease) and the tenant's negotiating strength.

- f. Tenant Objective—Assurance that lease amendments entered into subsequent to the date of the SNDA will survive a foreclosure.

Tenant Solution—Inclusion of an SNDA provision (i) that tenant's subordination is limited to the lease as it exists and that any subordination of future extensions, modifications, consolidations or renewals are conditioned on the lender's execution of a non-disturbance agreement; or (ii) acknowledging that the SNDA applies to the lease, as it may hereafter be modified, renewed and amended.

Possible Lender objection—Lender will be unwilling to be bound by lease modifications of which the lender has no notice and which may adversely affect the value of the lease or burden the property.

Possible Negotiated Result—An SNDA provision permitting certain lease amendments without lender consent and acknowledging these amendments will be effective after a foreclosure. Lender will likely insist on approval rights over lease amendments that (i) reduce rent, (ii) materially reduce any other monetary obligation of tenant under the lease or (iii) extend or reduce the lease term.

Following this outline is a sample lease review checklist a lender might use. Also attached are two forms of SNDA, one a lender might favor and one a tenant might favor.

## VI. LENDER'S LEASE REVIEW CHECKLIST

The issues listed below are common lease issues of concern to lenders. Lenders will expect the lease and/or the SNDA to resolve these issues in a manner that mitigates the lender's (or foreclosure purchaser's) exposure to liability as a potential future landlord. A borrower's (i.e., landlord's) familiarity with the lender's perspective and probable requirements will add "backbone" to its negotiation posture with tenants and help it resolve most of the issues addressed below during landlord/tenant negotiations. A well drafted lease negotiated with a lender's concerns in mind will help obviate the need to undertake a wholly new round of discussions once the lender is asked to approve the lease. If the landlord is unable to prevail on these issues with the tenant, a fall-back position is to address these issue to the benefit of a foreclosure purchaser within the body of the lease or within the SNDA. If the landlord fails to control the lease negotiations so as to obtain a lease that is immediately acceptable to the lender, then the landlord's ability to finance its project can bog down and momentum for leasing up the project may be lost. Often, a lending line officer has limited authority to negotiate or approve unresolved issues of significance to the lender and the issues are passed to the credit policy area, resulting in a new learning curve and additional delay.

### 1. Lender Liability and Environmental Liability:

YES NO SNDA	(a)	Lender's (and landlord's) liability must always to be limited to the equity interest in the project.
YES NO SNDA	(b)	The landlord and lender must not be liable for any of the following (most of these will need to be addressed in SNDA if not addressed in lease):
YES NO SNDA	(i)	the acts or omissions of the prior landlord;
YES NO SNDA	(ii)	the rights of tenant relative to any offset, defense or counterclaim against the prior landlord;
YES NO SNDA	(iii)	payment of rent more than one month in advance;
YES NO SNDA	(iv)	conflicting lease provisions between tenants (e.g., do rights given to one tenant violate negative covenants the landlord made to another tenant?);
YES NO SNDA	(v)	the erection or completion of improvements;
YES NO SNDA	(vi)	warranties as to use, compliance with zoning, title, etc.
YES NO SNDA	(c)	From the lender's perspective, the landlord should avoid broad representations regarding compliance with laws or covenants regarding initial construction, expansion options, rights of first offer/refusal, and continuing construction and/or repair obligations. The lender will want to limit the obligations for which the lender will be responsible if it steps into the landlord's shoes. The lender may not be able to perform per all of the requirements of the lease.
	(d)	Environmental:
YES NO SNDA	-	(1) Tenant must agree to comply with all applicable laws regarding hazardous substances.
YES NO SNDA	-	(2) Tenant must agree to indemnify landlord for tenant's acts relative to hazardous substances.

Discussion: Even though the lender will want the tenant commitments set out above, the lender will want to avoid approving any reciprocal indemnification obligations in which the landlord would indemnify the tenant for contamination of the remainder of the project because the remainder of the project may be in the hands of other tenants. Possible fall-back position—Landlord liable for environmental contamination of common areas occurring after the date of the lease and arising through the conduct of its own employees or contractors.

**2. Casualty or Condemnation :**

YES NO SNDA (a) "Mandatory re-build" clauses wherein the landlord is obligated to rebuild following a major casualty should not be allowed unless the landlord can "opt out" of rebuilding.

Discussion: The tenant's position will be that the cost of insurance is a pass-through under the lease and it is totally unreasonable for the landlord to have the option to either rebuild or to keep the insurance proceeds and terminate the lease.

YES NO SNDA (b) The lease should provide for landlord control of insurance proceeds and should anticipate the lender's right to control and disbursement of insurance/condemnation proceeds in situations where rebuilding is allowed. (The landlord should be aware of the terms of its mortgage on the issue of casualty and condemnation proceeds. Generally, the lender's mortgage will entitle the lender to receive and hold insurance proceeds and unless otherwise agreed, will generally entitle the lender to apply proceeds against the debt.)

YES NO SNDA (c) The lease must allow adequate time for restoration to occur must be allowed before a tenant can exercise a termination right; the landlord or a third party must be the one determining how long rebuilding will take.

YES NO SNDA (d) The landlord must make sure casualty and condemnation language is consistent across different leases in the same project to the extent necessary to avoid having to rebuild one tenant while another tenant is allowed to terminate.

Discussion: In a lease in which the landlord has the right/obligation to rebuild, abatement of rent during the time from the casualty to the completion of restoration is generally reasonable and appropriate. Be aware of the manner in which abatement works under the particular lease terms. In determining the time period within which repairs must be accomplished, consider measuring the time from receipt of insurance proceeds. It can take longer to negotiate and adjust the payment of insurance proceeds than it will take to rebuild.

**3. Notices/Landlord Defaults/Self-Help:**

Must comply with the laws of the state where the project is located based on review by local counsel.

YES NO SNDA (a) Tenant must send notice to lender concurrent with the notice sent to landlord.

YES NO SNDA (b) Lender should have the same amount of time in order to cure the default as is given to the landlord plus the amount of time it takes for lender to become entitled under the mortgage to remedy the default, but at least some minimum finite period of time (e.g., the longer of the time given the landlord or 30 days).

Discussion: As a practical matter, if the loan is performing, it is unlikely the lender will undertake cure of a landlord default, but the lender will want to be aware of the situation and be in a position to insist that the landlord take action.

YES NO SNDA (c) General tenant rights to terminate a lease upon any type of landlord default must be avoided. Tenant remedies in many states are limited by common law to landlord defaults which result in "constructive eviction" of the tenant (something the tenant has to prove in court).

YES NO SNDA (d) Setoff Rights and Self-Help:  
(1) Broad rights of setoff must be avoided except for monetary defaults by landlord; setoff rights must never be allowed against a purchaser at foreclosure which arise from prior ownership.  
(2) Tenant should agree to perform any work under any self-help clause in a "good and workmanlike manner" and must indemnify landlord for any liability resulting from tenant's actions.  
(3) Tenant's self-help rights must exclude 1) buildings or space other than the "premises;" 2) systems or their operations (HVAC, roof, elevators, plumbing, etc.) which are not exclusively related to the "premises"; or, 3) actions affecting any other tenant in the project.  
(4) Landlord cannot be liable for services failures beyond landlord's control; however, rent may be abated and tenant can be allowed to terminate a lease due to a services failure which continues beyond some finite period of time.

**4. Other Provisions:**

(a) Assignment and Subletting:  
YES NO SNDA (1) Original tenant must always remain obligated for performance of all obligations under the lease.

YES NO SNDA (2) The use of the premises by any assignee or sublessee should tie back to the use clause in the lease (i.e. a sublessee restricted to the same use as the original tenant). Use of the premises by any tenant must be restricted so that it (i) does not conflict with any "exclusive use" or

- "prohibited use" in any lease in the project (all leases should prohibit certain bingo parlors, strip joint, etc...); or
- ii) have the potential to result in ill effects to other tenants in the project (e.g., increasing elevator or traffic loads, etc.)
- YES NO SNDA (3) Landlord should be able to qualify the assignee/sublessee as to creditworthiness, character, nature of business, etc.
- YES NO SNDA (b) Cotenancy: [i.e., a clause in which a tenant's obligations under the lease are dependent upon the continuation of one or more other tenants in the project]. These are very common in anchored shopping centers.
- (1) Cotenancy clauses should be avoided if at all possible.
- (2) Such clauses are standard in regional mall anchor leases.
- Discussion: Often the traffic anticipated to be generated by an anchor tenant will be the key reason why a developer will be able to successfully lure other retailers into a new center. The co-tenancy clause is the tenant's means of placing onto the developer the risk that the actual leasing may not match the promises made by the developer. Certainly, the retailer counting on traffic from an anchor does not get the benefit of his bargain if, instead of being next door to a retailer generating hundreds of customer trips a day, the retailer is next door to an empty, boarded up space. If cotenancy rights are granted to a tenant, then the cotenancy right should match a similar operating covenant of the anchor tenant. Retailers are as reluctant to give covenants to operate as landlords are reluctant to give cotenancy clauses.
- YES NO SNDA (c) Right-to-Go Dark Clauses: (i.e., a clause permitting the tenant to vacate the premises without termination of the lease).
- Landlord must be able to regain control of the space after some finite period of time (ideally as short as possible).
- Discussion: While most lease forms provide that "abandonment" or vacation of the premises is a default under the lease, "going dark" in an office project is generally less harmful to the landlord than in the case of a retail center. Boarded up or dark windows in a retail center, regardless of the payment of rent by the tenant, may cast a blight upon the vacant space that is likely to affect the neighboring tenants.
- YES NO SNDA (d) Force Majeure:
- Except for rental payments, all leases must allow the landlord additional time for performance of obligations under the lease after occurrence of force majeure events.
- Discussion: Force Majeure should not be a sticking point in lease negotiations. Often the issue of reciprocal force majeure provisions arises. Be sure the force majeure clause does not apply to monetary obligations.

**5. Special Provisions:**

- YES NO SNDA (a) Right of First Refusal to Purchase Project:  
(1) What is the applicable purchase price?  
Discussion: The purchase price must be sufficient to make the lender whole. The tenant will probably also want to assure that the purchase price is sufficient to pay the mortgage in full. Query: What happens on the exercise of a purchase option on a subordinated lease in which the tenant's option price is less than the debt? Does the tenant step into the shoes of the landlord and hold the property subject to the unpaid debt? Is the result different if the lease is superior to the mortgage?  
(2) In the case of a right of first refusal, a fast turnaround is needed from the tenant, say 15 days.  
Discussion: In no case should a right of first refusal apply to a foreclosure sale. Once a tenant does exercise a right of first refusal, the tenant must be obligated to close within a finite time frame (as short as possible).
- YES NO SNDA (b) Tenant's Right to Protest Taxes; Tenant's Rights to Participate in Resolution of Other Issues Involving Third Parties:  
(1) Large credit tenants may insist on a right to protest taxes.  
(2) Landlord may permit tenant to protest taxes provided:  
i) No tax lien is allowed to be foreclosed;  
ii) The tenant indemnifies landlord for any loss or liability resulting from such protest;  
iii) Landlord should have the right to require a cash deposit or a bond and the right to pay the tax on or after an outside date in order to assure that the lien will not be foreclosed.  
Discussion: The right in favor of one or more tenants to protest taxes in a multi-tenant project may not be workable unless the rights are coordinated or unless the tenants occupy separate tax parcels within project.
- YES NO SNDA (c) Special Retail Clauses:  
- All special clauses (i.e. operating clauses, co-tenancy, exclusive use rights, prohibited uses) must be identified to make sure they work consistently. Note the implications of such clauses on a tenant's rights to assign or sublease.
- YES NO SNDA (d) Building Identity Clauses [i.e., a right in favor of a tenant to name the building or project]:  
- These must be personal to the named tenant only (i.e. not to any sublessee) and must operate only for a finite period or only as long as same minimum number of square feet are occupied and operations of the tenant for intended purposes continues therein.
- YES NO SNDA (e) Impossible OR Unusual Provisions:

- The lender must make sure it will be able to perform all of the landlord's covenants if it has to step into the landlord's shoes.
- Any unusual provisions (e.g. "favored nations" clauses, requirement to consent to any refinancing of the project, etc.) analyzed for their effect upon the landlord's liability, the exit strategy for the loan, the economics of the project, etc.

**6. Tenant/Lender Agreements:**

- |             |     |  |
|-------------|-----|--|
| YES NO SNDA | (a) | The lease must require the tenants to furnish estoppels upon landlord's request. The lease clause should establish a definite time limit on the tenant's obligation to respond. Keep in mind the possible effect on a sale or financing transaction if the tenant has an extended time for response.   |
| YES NO SNDA | (b) | The SNDA can be used to make lease modifications without requiring full scale lease modifications. <u>The landlord should have a clause in each newly negotiated lease stating that the lease is subject to lender approval. This prevents the landlord from being in the unfortunate position of being committed to a signed lease that the landlord will not approve and that the tenant will not agree to release. Leases for which the lender does not want to provide an SNDA must be subordinate to lender's mortgage so the lender is not exposed to the outstanding liabilities and obligations of the prior landlord.</u> |
| YES NO SNDA | (c) | The standard lease form must subordinate the tenant's interest in the lease to all existing and future mortgages and should not require the landlord to obtain an SNDA.  |

Discussion: In specific instances, an obligation on the part of the landlord to obtain an SNDA may be appropriate; however, this provision should be included only when the tenant requires it and only in cases in which the lender would be willing to provide it. In any event, the landlord should have an "out", as by a termination of the lease (termination may be automatic or upon the election of the tenant) without further liability occurring within twenty (20) days after lease signing if the lease has not been approved by the lender and an SNDA executed and delivered by the lender. In any event, any right of termination in favor of the tenant due to non-delivery of the SNDA should have a time limit and should expire if the tenant does not exercise the termination right timely.

## EXHIBIT "A"

### SUBORDINATION, NONDISTURBANCE AND ATTORNMENT AGREEMENT

**NOTICE:** THIS SUBORDINATION, NONDISTURBANCE AND ATTORNMENT AGREEMENT RESULTS IN YOUR LEASEHOLD ESTATE BECOMING SUBJECT TO AND OF LOWER PRIORITY THAN THE LIEN OF SOME OTHER OR LATER SECURITY INSTRUMENT.

This Subordination, Nondisturbance and Attornment Agreement ("**Agreement**") is entered into as of the \_\_\_\_ day of \_\_\_\_\_, 200\_\_, by and among \_\_\_\_\_ ("**Tenant**"), \_\_\_\_\_ ("**Borrower**") and \_\_\_\_\_ ("**Bank**").

#### **Factual Background**

A. Borrower is the owner of certain real property located in the City of \_\_\_\_\_, County of \_\_\_\_\_, State of Texas, (IF APPLICABLE) [commonly known as \_\_\_\_\_,] and more particularly described in the attached Exhibit A. As used here, the term "**Property**" means that real property, together with all improvements (the "**Improvements**") located on it.

B. Bank has (CHOOSE ONE) [agreed to make/made] a loan to Borrower in the principal amount of \$\_\_\_\_\_ (the "**Loan**"), as provided in a (CHOOSE ONE) [construction/standing/land] loan agreement dated \_\_\_\_\_, 20\_\_ (the "**Loan Agreement**"). The Loan is or is to be evidenced by a promissory note (the "**Note**") which is or is to be secured by a deed of trust encumbering the Property (the "**Deed of Trust**"). The Loan Agreement, the Note, the Deed of Trust, and all other documents and instruments identified in the Loan Agreement as "Loan Documents," including this Agreement, shall be collectively referred to here as the "**Loan Documents**."

C. Tenant and Borrower (as Landlord) entered into a lease dated \_\_\_\_\_, 20\_\_ (the "**Lease**"), under which Borrower leased to Tenant a portion of the Improvements located within the Property, (IF APPLICABLE) [commonly known as \_\_\_\_\_,] and more particularly described in the Lease (the "**Premises**").

D. Bank is willing to make or continue the Loan to Borrower, provided that Tenant agrees, among other things, to subordinate Tenant's rights under the Lease to the lien or charge of the Loan Documents and to attorn to Bank on the terms and conditions of this Agreement. Tenant is willing to agree to such subordination and attornment and other conditions, provided that Bank agrees not to disturb Tenant's possession under the Lease, all as set forth more fully below.

#### **Agreement**

Therefore, the parties agree as follows:

1. **Subordination**. The Loan Documents, and all supplements, amendments, modifications, renewals, replacements and extensions of and to them, shall unconditionally be and remain at all times a lien or charge on the Property prior and superior to the Lease, to the leasehold estate created by it, and to all rights and privileges of Tenant under it. The Lease and leasehold estate, together with all rights and privileges of Tenant under the Lease, are hereby unconditionally subjected and made subordinate to the lien or charge of the Loan Documents in favor of Bank. Tenant consents to Borrower's and Bank's

entering into the Deed of Trust and the other Loan Documents. Tenant further declares, agrees and acknowledges that, in making disbursements under the Loan Documents, Bank has no obligation or duty to, nor has Bank represented that it will, see to the application of such proceeds by the person or persons to whom they are disbursed by Bank, and any application or use of such proceeds for purposes other than those provided for in the Loan Documents shall not defeat the subordination made in this Agreement, in whole or in part.

2. Definitions of "Transfer of the Property" and "Purchaser." As used here, the term "***Transfer of the Property***" means any transfer of Borrower's interest in the Property by foreclosure, trustee's sale or other action or proceeding for the enforcement of the Deed of Trust or by deed in lieu thereof. The term "***Purchaser***," as used here, means any transferee, including Bank, of the interest of Borrower as a result of any such Transfer of the Property, and also includes any and all successors and assigns, including Bank, of such transferee.

3. Nondisturbance. So long as Tenant is not in default in the performance of the terms, provisions and conditions contained in the Lease and so long as Tenant observes the provisions of this Agreement:

(a) Tenant shall not be named or joined in any foreclosure, trustee's sale or other proceeding to enforce the Deed of Trust unless the joinder is required by law in order to perfect such foreclosure, trustee's sale or other proceeding;

(b) The enforcement of the Deed of Trust shall not terminate the Lease or disturb Tenant in the possession and use of the Premises; and

(c) The leasehold estate granted by the Lease shall not be affected in any manner by any Transfer of the Property or any other proceeding instituted or action taken under or in connection with the Deed of Trust, or by Bank's taking possession of the Property or the Premises in accordance with any provision of the Deed of Trust; provided that Bank, if it becomes the Purchaser or if it takes possession under the Deed of Trust, and any other Purchaser shall not:

(i) be liable for any damages or other relief attributable to any act or omission of any prior landlord under the Lease (including Borrower);

(ii) be liable for any damages or other relief attributable to any latent or patent defects in construction with respect to any portion of the Property;

(iii) be liable for any consequential damages attributable to any act or omission of Purchaser;

(iv) be liable for any damage or other relief attributable to any breach of any representation or warranty contained in the Lease by Purchaser or any prior landlord under the Lease;

(v) be subject to any offsets or defense not specifically provided for in the Lease and which Tenant may have against any prior landlord under the Lease; or

(vi) be bound by any prepayment by Tenant of more than one month's installment of rent or for any security deposit not actually delivered to Purchaser or by any modification or amendment of or to the Lease unless the prepayment, amendment or

modification shall have been approved in writing by Bank or by any subsequent beneficiary under the Deed of Trust.

4. Attornment. If any Transfer of the Property should occur, and if Tenant is not in default under the Lease, Purchaser shall be bound to Tenant and Tenant shall be bound to Purchaser under all of the terms, covenants and conditions of the Lease (IF APPLICABLE) [(except as provided in Section 6 below)] for the balance of the Lease term and any extensions or renewals of it which may then or later be in effect under any validly exercised extension or renewal option contained in the Lease, all with the same force and effect as if Purchaser had been the original landlord under the Lease. Tenant does hereby attorn to Purchaser, including Bank if it should become the Purchaser, as the landlord under the Lease. This attornment shall be effective and self-operative without the execution of any further instruments, upon Purchaser's succeeding to the interest of the landlord under the Lease.

5. Tenant's Waiver of Option Rights. In the event of any Transfer of the Property, Tenant specifically waives any right, whether arising out of the Lease or otherwise, to exercise any option which remains unexercised at the time of such transfer, to:

(a) purchase the Premises or the Property, or any interest or portion in or of either of them; or

(b) expand into other space in the Improvements. The foregoing waiver does not apply to any option to extend or renew the Lease term which is set forth in the Lease as of the date of this Agreement; Tenant does not waive any right to exercise any such option following a Transfer of the Property. If, after the date of this Agreement, Tenant acquires any purchase option, option to expand into other space in the Improvements, or option to extend or renew the term of the Lease, Tenant agrees that such option shall be subject and subordinate to the lien or charge of the Loan Documents and shall be null and void upon any Transfer of the Property.

(INSERT SECTION 6 IF THE LEASE IS TO BE MODIFIED OR IF PORTIONS OF THE LEASE WILL BE INEFFECTIVE UPON BANK FORECLOSURE. RENUMBER SUBSEQUENT SECTIONS IF NECESSARY.)

[6. Modification of Lease Following Transfer. Tenant acknowledges that as landlord, Bank or another Purchaser would have different interests and concerns than those of Borrower and that certain provisions of the Lease would be burdensome for Bank or such Purchaser following a Transfer of the Property. Accordingly, Tenant agrees that if the Property should be so transferred, the Lease as between Tenant and Purchaser shall be amended as set forth in the attached Exhibit B. Upon Bank's written request following any such Transfer of the Property, Tenant agrees to execute a new lease of the Premises with Purchaser for the remaining term of the Lease, upon the same terms and conditions as are set forth in the Lease between Borrower and Tenant, except as modified in accordance with Exhibit B.]

7. Default By Borrower. In the event of a default by Borrower in its performance of the terms, provisions and conditions of the Loan Documents, Borrower directs Tenant and Tenant agrees to recognize the assignment of rents made by Borrower to Bank in the Deed of Trust, and to pay to Bank as assignee all rents due under the Lease, upon Tenant's receipt of written notice from Bank that Borrower is in default under the terms of the Loan Documents. Borrower hereby authorizes Tenant to accept such direction from Bank and waives all claims against Tenant for any sums so paid at Bank's direction. Such payments of rents by Tenant to Bank by reason of that assignment and of Borrower's default shall continue until the first to occur of the following:

(a) No further rent is due or payable under the Lease;

(b) Bank gives Tenant notice that the default of Borrower under the Loan Documents has been cured and instructs Tenant that the rents shall thereafter be payable to Borrower; or

(c) A Transfer of the Property occurs and Purchaser gives Tenant notice of such transfer. Purchaser shall thereupon succeed to the interest of Borrower under the Lease as provided in Sections 3 and 4 above, after which time the rents and other benefits of Borrower under the Lease shall be payable to Purchaser as the owner of them.

8. Limitation on Bank's Performance. Nothing in this Agreement shall be deemed or construed to be an agreement by Bank to perform any covenant of Borrower as landlord under the Lease unless and until Bank obtains title to the Property as Purchaser or obtains possession of the Property under the terms of the Deed of Trust, and then only during the time when Bank holds title to the Property.

9. Tenant's Covenants. Tenant agrees that during the term of the Lease, without Bank's prior written consent, Tenant shall not:

(a) pay any rent or additional rent more than one month in advance to any landlord (including Borrower); or

(b) cancel, terminate or surrender the Lease, except at the normal expiration of the Lease term; or

(c) enter into any amendment, modification or other agreement relating to the Lease; or

(d) assign or sublet any portion of the Lease or the Premises, except as expressly provided in the Lease.

10. No Merger. Borrower, Tenant and Bank agree that unless Bank shall otherwise consent in writing, Borrower's estate in and to the Property and the leasehold estate created by the Lease shall not merge, but shall remain separate and distinct, notwithstanding the union of such estates either in Borrower or Tenant or any third party by purchase, assignment or otherwise.

11. Notices of Default; Material Notices. Tenant, from and after the date of this Agreement, shall send a copy of any notice of default or similar statement under the Lease to Bank at the same time such notice or statement is sent to Borrower under the Lease. Borrower and Tenant shall send copies of all material notices given under the Lease to Bank. Such notices shall be delivered to Bank in the manner and at the addresses set forth below.

12. Limitation on Liability. Regardless of anything in the Lease or this Agreement to the contrary, no Purchaser who acquires title to the Property shall have any obligation or liability beyond its interest in the Property. Tenant shall look exclusively to Purchaser's interest in the Property for payment and discharge of any of Purchaser's obligations under this Agreement or under the Lease. Tenant shall not collect or attempt to collect any judgment based upon such obligations out of any other assets of Purchaser. By executing this Agreement, Borrower specifically acknowledges and agrees that nothing contained in this Section shall impair, affect, lessen, abrogate or otherwise modify the obligations of Borrower to Tenant under the Lease.

13. Tenant's Estoppel Certificate.

(a) Tenant's Option Rights. Tenant has no right or option of any nature whatsoever, whether arising out of the Lease or otherwise, to purchase the Premises or the Property, or any interest or portion in or of either of them, to expand into other space in the Improvements or to extend or renew the term of the Lease, except as described in the attached Exhibit C.

(b) True and Complete Lease. Tenant represents and warrants to Bank that Exhibit D accurately identifies all amendments, supplements, side letters and other agreements and memoranda pertaining to the Lease, the leasehold and/or the Premises.

(c) No Default. As of the date of this Agreement, Tenant represents and warrants that there exist no events of default, or events that with notice or the passage of time or both would be events of default, under the Lease, on either the Tenant's part or the Borrower's, nor is there any right of offset (including audit or accounting rights which might otherwise give rise to a claim or an offset for rents paid under the Lease) against any of Tenant's obligations under the Lease, except as described in the attached Exhibit E. The Lease is in full force and effect as of the date of this Agreement.

(d) Reliance. Tenant acknowledges that Bank is relying on the representations, certifications and undertakings made by Tenant in this Agreement in extending credit to Borrower.

(e) Further Certificates. Within ten (10) days after Bank's request, Tenant shall deliver to Bank and to any person designated by Bank, estoppel certificates executed by Tenant, certifying (if such is the case) that the Lease is in full force and effect, that there are no defenses or offsets outstanding under the Lease (or stating those claimed by Tenant, as the case may be) and such other information about Tenant or the Lease as Bank may reasonably request.

(f) Nondisturbance Agreement. This Agreement satisfies any condition or requirement in the Lease relating to the granting of a nondisturbance agreement from Bank.

14. Bank's Rights to Cure Default. In the event of any act or omission by Borrower which would give Tenant the right to terminate the Lease or to claim a partial or total eviction, Tenant shall not exercise any such right or make any such claim until it has given Bank written notice of such act or omission and has given Bank either thirty (30) days to cure the default, if the default is monetary, or a reasonable time for Bank to obtain possession of the Property and cure the default, if the default is non-monetary. Nothing in this Agreement shall, however, be construed as a promise or undertaking by Bank to cure any default of Borrower's.

15. Notices. All notices given under this Agreement shall be in writing and shall be given by personal delivery, overnight receipted courier, or by registered or certified United States mail, postage prepaid, sent to the party at its address appearing below. Notices shall be effective upon receipt or when proper delivery is refused. Addresses for notices may be changed by any party by notice to all other parties in accordance with this Section. Service of any notice on any one Borrower shall be effective service on Borrower for all purposes.

To Bank: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

To Borrower: \_\_\_\_\_  
\_\_\_\_\_

To Tenant:

---

---

---

---

16. Arbitration. Any controversy or claim between or among the parties which arises out of or relates to this Agreement, including any claim based on or arising from an alleged tort, shall be determined by arbitration as provided in the Loan Documents.

17. Attorneys' Fees. If any lawsuit, reference or arbitration is commenced which arises out of or relates to this Agreement, the prevailing party shall be entitled to recover from each other party such sums as the court, referee or arbitrator may adjudge to be reasonable attorneys' fees in the action, reference or arbitration, including the allocated costs for services of in-house counsel, in addition to costs and expenses otherwise allowed by law.

18. Miscellaneous Provisions. This Agreement shall inure to the benefit of and be binding upon the parties and their respective successors and assigns. This Agreement is governed by the laws of the State of Texas, without regard to the choice of law rules of that State. As used here, the word "include(s)" means "include(s), without limitation," and the word "including" means "including, but not limited to." Bank may but shall not be obligated to record this Agreement, at Bank's sole discretion.

19. Integration. This Agreement integrates all of the terms and conditions of the parties' agreement regarding the subjection and subordination of the Lease and the leasehold estate created by it, together with all rights and privileges of Tenant under it, to the lien or charge of the Loan Documents. This Agreement supersedes and cancels all oral negotiations and prior and other writings with respect to such subjection and subordination (only to such extent, however, as would affect the priority between the Lease and the Loan Documents), including any provisions of the Lease which provide for the subjection or subordination of the Lease and the leasehold estate thereby created to a deed or deeds of trust or to a mortgage or mortgages. This Agreement is intended by the parties as the final expression of the agreement, and as the complete and exclusive statement of the terms agreed to by the parties, with respect to such subordination and subjection, to the extent specified in the foregoing sentence. If there is any conflict between the terms, conditions and provisions of this Agreement and those of any other agreement or instrument, including any of the Loan Documents, the terms, conditions and provisions of the Loan Documents shall prevail. This Agreement may not be modified or amended except by a written agreement signed by the parties or their respective successors in interest.

THIS WRITTEN AGREEMENT REPRESENTS THE FINAL AGREEMENT AMONG THE PARTIES RELATING TO THE SUBJECT MATTER THEREOF AND MAY NOT BE CONTRADICTED BY EVIDENCE OF PRIOR, CONTEMPORANEOUS OR SUBSEQUENT ORAL AGREEMENTS OF THE PARTIES. THERE ARE NO UNWRITTEN ORAL AGREEMENTS AMONG THE PARTIES.

NOTICE: THIS AGREEMENT CONTAINS A PROVISION WHICH ALLOWS THE PERSON OBLIGATED ON YOUR LEASE TO OBTAIN A LOAN, A PORTION OF WHICH MAY BE EXPENDED FOR PURPOSES OTHER THAN IMPROVEMENT OF THE PROPERTY.

**[Remainder of page intentionally left blank, signature pages follow.]**

TENANT: \_\_\_\_\_  
a \_\_\_\_\_,

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

BORROWER: \_\_\_\_\_  
a \_\_\_\_\_,

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

BANK: \_\_\_\_\_  
a \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

**EXHIBITS:**

- Exhibit A - Property Description
- Exhibit B - Schedule of Modified Lease Terms
- Exhibit C - Purchase, Expansion, First Refusal, Extension and Renewal Options
- Exhibit D - Schedule of Amendments, Supplements, Side Letters and Other Agreements and Memoranda Pertaining to Lease
- Exhibit E - Existing Defaults or Offsets under Lease



**EXHIBIT "B"**

**SUBORDINATION, NON-DISTURBANCE AND  
ATTORNMENMENT AGREEMENT ("SNDA")**

THIS AGREEMENT is made as of the \_\_\_\_\_ day of \_\_\_\_\_, 20\_\_, between \_\_\_\_\_, a \_\_\_\_\_, with offices at \_\_\_\_\_, its Sublessees or Assigns, (hereinafter referred to as "*Lessee*"), and \_\_\_\_\_, a \_\_\_\_\_, with offices at \_\_\_\_\_ ("*Mortgagee*").

**WITNESSETH:**

WHEREAS, Mortgagee is the holder of a certain \_\_\_\_\_, dated \_\_\_\_\_, and recorded \_\_\_\_\_, in Real Property Records of \_\_\_\_\_ County, Texas ("*Mortgage*"), covering the Shopping Center and/or Leased Premises situated in the City of \_\_\_\_\_, County of \_\_\_\_\_, State of Texas (hereinafter referred to as the "*Premises*"); and

WHEREAS, Lessee leased from \_\_\_\_\_ ("*Lessor*") \_\_\_\_\_ square feet in the Premises pursuant to that certain lease dated \_\_\_\_\_, \_\_\_\_\_ ("*Lease*"), between Lessor and Lessee; and

WHEREAS, Lessee desires that the Lease shall not terminate, but rather shall remain in full force and effect in accordance with its terms in the event the Mortgage is foreclosed or any foreclosure sale of the mortgaged Premises is made or any transfer therein in lieu of foreclosure is made and Mortgagee desires that Lessee subordinate its interest in the Lease to the Mortgage.

WHEREAS, Lessor will deliver a copy of the Lease and any amendments to Mortgagee, the receipt of which is hereby acknowledged,

NOW, THEREFORE, in consideration of the premises and other good and valuable consideration in hand paid, the parties hereto agree as follows:

1. Mortgagee hereby consents and approves the Lease, amendments and the terms thereof, including the options to extend the term as set forth in the Lease, and covenants and agrees that the exercise by Lessee of rights, remedies and options therein contained shall not constitute a default under the Mortgage.

2. The Lease is, and shall remain, subject and subordinate to the lien of the Mortgage and to any extensions, modifications, consolidations or renewals thereof; provided that as to any such extensions, modifications, consolidations or renewals thereof, a non-disturbance agreement in the form of this agreement is executed and delivered by the holder of the Mortgage as so extended, modified, consolidated or renewed.

3. So long as Lessee is not in default in the performance of any terms, covenants and conditions to be performed on its part under the Lease beyond any applicable cure period, then in such event:

(a) Lessee shall not be joined as a party defendant in any foreclosure proceeding which may be instituted by Mortgagee;

(b) Lessee's leasehold estate under the Lease shall not be terminated, barred, cut off, or otherwise disturbed by reason of any default under the Mortgage or any foreclosure proceeding instituted by Mortgagee.

4. If Mortgagee shall succeed to the interest of Lessor in and to the Lease, whether through possession, foreclosure proceeding, or delivery of a deed in lieu of foreclosure, Lessee shall attorn to and recognize Mortgagee or any other purchaser at a foreclosure sale as Lessee's landlord under the Lease, and shall promptly execute and deliver an attornment agreement in the form of this agreement to evidence such attornment. Upon and after such attornment, the Lease shall continue in full force and effect as a direct lease between Mortgagee or such purchaser and Lessee upon all of the terms, conditions and covenants as are set forth in the Lease, except that Mortgagee or such purchaser shall after such attornment:

(a) Be liable for any previous act or omission of any previous landlord arising directly from such landlord's responsibilities and duties pursuant to the Lease; provided, Mortgagee or such purchaser has received appropriate notice of such default, and has an opportunity to cure (having no obligation to so cure) same, all pursuant to the terms and conditions of the Lease,

(b) Be subject to any offset or counterclaim which Lessee might be entitled to assert against any previous landlord, including deductions from rent arising pursuant to the Lease; provided, Mortgagee or such purchaser has received appropriate notice of such default, and has an opportunity to cure (having no obligation to so cure) same, all pursuant to the terms and conditions of the Lease;

(c) Not be bound by any previous prepayment of more than one month's fixed rent, unless such prepayment shall have been expressly approved in writing by Mortgagee;

(d) Be bound by any modification of the Lease unless excepted in subparagraph (e) below.

(e) Not be bound by any modification of the Lease made after the date of this agreement without its written consent which would (i) reduce fixed annual rent, or (ii) materially reduce any other monetary obligation of Lessee under the Lease.

5. This Agreement shall be binding upon and shall inure to the benefit of the parties hereto, and their respective successors and assigns.

6. At any time before the rights of the Lessor shall have been forfeited or adversely affected because of any default on its part, or within the time permitted the Lessor to cure any default under the Lease as there provided, Mortgagee may, at its option, pay any taxes and assessments, make any repairs and improvements, make any deposits or do any other act or thing required of the Lessor by the terms of the Lease, and all payments so made and all things so done and performed by Mortgagee shall be as effective to prevent the rights of the Lessor from being forfeited or adversely affected because of any default under this Lease as the same would have been if done and performed by the Lessor.

7. Any required notices to Mortgagee, shall be in writing and shall be given by registered or certified mail, return receipt requested, postage prepaid, at the address of Mortgagee as hereinabove set forth or at such other address as Mortgagee may designate by notice.

8. Any notices or communications given to Lessee under this agreement shall be in writing and shall be given by registered or certified mail, return receipt requested, postage pre-paid, at the address of Lessee hereinabove set forth, also to the attention of \_\_\_\_\_, at \_\_\_\_\_, or at such other address as Lessee may designate by notice. During the period of any postal strike or other interference with the mail, personal delivery shall be substituted for registered or certified mail. No default notice given by Lessee under the Lease shall be effective as against Mortgagee unless a duplicate copy thereof has been given to Mortgagee.

9. This agreement shall bind and inure to the benefit of and be binding upon and enforceable by the parties hereto and their respective successors and assigns.

10. This agreement contains the entire agreement between the parties and cannot be changed, modified, waived or canceled except by an agreement in writing executed by the party against whom enforcement of such modification, change, waiver or cancellation is sought.

11. This agreement and the covenants herein contained are intended to run with and bind all lands affected hereby.

IN WITNESS WHEREOF, this agreement has been duly executed by the parties hereto.

**[Remainder of page intentionally left blank, signature page follows.]**

