

The Strengths of Rights of First Refusal

June 30, 2022

On March 30, 2022, the New York State Supreme Court, New York County (the “Court”) decided in *Times Square JV LLC v. Walber Broadway LLC*^[1] that a ground lease-tenant that is in default under the ground lease for failure to pay the landlord rent does not per se invalidate the tenant’s right of first refusal under the lease to purchase from landlord the land on which the leased premises is situated.

The Crowne Plaza Hotel in Times Square, located at 1605 Broadway, New York, New York (the “Hotel”) was originally constructed in 1987^[2]. The Hotel, a flagship of the InterContinental Hotels Group’s Crowne Plaza brand, contains 795 hotel rooms and is located in a building that is approximately 843,000 square feet of mixed-use property. The entire building was built on a parcel of land that is approximately 41,000 square feet in the aggregate, of which the portion of land the Hotel was situated totaled approximately 11,000 square feet (the “Premises”) and was owned by Walber Broadway LLC, a New York limited liability company (the “Landlord”). Times Square JV LLC, a Delaware limited liability company (the “Tenant”) owned a fee interest in the remainder of said land, which totaled approximately 30,000 square feet.^[3] Tenant’s and Landlord’s rights and obligations vis-à-vis the Premises were governed by that certain lease agreement, dated March 1, 1987, between Landlord, as successor-landlord, and Tenant, as successor-tenant^[4] (the “Lease”).

Under the Lease, Tenant had a right of first refusal (“ROFR”) to purchase the Premises if Landlord decided to offer the Premises for sale^[5]. That is, if Landlord decided to market the Premises, then Landlord was required under the Lease to notify Tenant by delivering to Tenant a proposed purchase and sale agreement with the terms under which Landlord would be willing to sell the Premises (such notice, the “ROFR Notice”). If Tenant agreed to the terms of the ROFR Notice, then Tenant would exercise its ROFR by delivering to Landlord the executed purchase and sale agreement within 15 business days from the date of such ROFR Notice and concurrently paying Landlord the applicable purchase price deposit^[6].

In 2018, Tenant and its affiliated-operating company (the “Hotel Lessee”) entered into a mortgage loan agreement with certain lenders (collectively, the “Mortgage Lender”), pursuant to which Tenant and Hotel Lessee received a loan in the amount of up to \$80,000,000.00 (the “Mortgage Loan”). Separately, the Tenant’s and Hotel Lessee’s respective parent entities (collectively, the “Mezz Borrower”) entered into a mezzanine loan agreement with certain mezzanine lenders (collectively, the “Mezz Lender”), pursuant to which Mezz Borrower received a mezzanine loan of up to \$80,000,000.00 (the “Mezz Loan”) secured by, among other things, a pledge agreement that gave Mezz Lender a security interest in and lien on all of Mezz Borrower’s rights and options in Tenant. Under said mezzanine loan agreement, a default by Tenant and Hotel Lessee under the Mortgage Loan constituted an immediate event of default under the Mezz Loan.

In March 2020, local and federal COVID-19 mandates ceased all Hotel operations, which in turn resulted in the Hotel generating no revenue. Proclaiming to have suffered financial hardship resulting from such COVID-19 shutdowns, Tenant ceased paying rent to Landlord as of December 2020 and thereby defaulted under the Lease for failing to pay amounts then due and owing thereunder. Furthermore, in June 2020, Tenant and Hotel Lessee failed to pay Mortgage Lender the full principal amount then due and owing under the Mortgage Loan on its maturity date. Such default under the Mortgage Loan automatically triggered a default under the Mezz Loan, which resulted in Mezz Lender exercising its right to control Tenant pursuant to the mezzanine loan agreement.

Subsequently, Landlord entered into an agreement with 1601 Broadway LLC, a Delaware limited liability company (“1601 Broadway”) for the purchase and sale of the Premises on August 25, 2021. On August 26, 2021, Landlord delivered to Tenant a ROFR Notice, together with a proposed purchase and sale agreement (“PSA”), and offered Tenant the opportunity to purchase the Premises for \$121,000,000.00, payable as a \$30,000,000.00 deposit due at contract signing with the remainder due at closing^[7]. On September 1, 2021, Tenant delivered to Landlord the executed PSA and wired the required contract deposit in accordance with the ROFR Notice. On September 3, 2021,

Landlord informed Tenant in writing that Tenant's acceptance of the ROFR Notice was purportedly invalid because of Tenant's ostensible failure to disclose its corporate structure and to prove that its signatory was authorized to bind Tenant under the PSA.

On September 16, 2021, Tenant brought an action against Landlord for breach of contract, claiming that Landlord breached its contractual obligations under the Lease by selling the Premises to 1601 Broadway despite Tenant's adequate acceptance of the relevant ROFR Notice. Tenant subsequently motioned for the Court to grant summary judgment.

The Court granted Tenant's summary judgment motion and held that, as a matter of law, Landlord breached the terms of the Lease by effecting the sale of the Premises to 1601 Broadway after Tenant properly exercised its right of first refusal to purchase the Premises in accordance with the Lease. In so deciding, the Court held that, where there was no genuine dispute of any material fact in question and viewing all undisputed facts in a light most favorable to Landlord, Tenant's failure to pay Landlord the Tenant's monetary obligations due under the Lease alone did not bar Tenant from exercising its ROFR in accordance with the Lease and was not dispositive in rendering Tenant's ability to purchase the Premises under the terms of the ROFR Notice, a material issue of fact that would preclude summary judgment.

This case evidences the powerful nature of rights of first refusal, ostensibly enforceable regardless of a material default under the underlying document in which the ROFR is contained.

[1] *Times Square JV LLC v. Walber Broadway LLC*, 655450/2021.

[2] <https://nypost.com/2022/02/16/crowne-plaza-hotel-in-times-square-entangled-in-legal-battle/>.

[3] Amended Verified Complaint dated October 18, 2021, Index No. 655450/2021 (Dkt No. 65).

[4] Tenant was the successor-in-interest to the original tenant, Broadway 48th-49th Street LLC, by that certain Assignment and Assumption of Lease, dated as of March 9, 2020, and Assignment and Assumption of Ground Lease, dated as of November 21, 2006.

[5] Lease § 24.01(a).

[6] Lease § 24.01(a).

[7] Amended Verified Complaint, ¶ 37, p. 13.