



Turning to Fall

September 29, 2022

'You Can't Always Get What You Want' – Exercising an Option

On March 21, 2022, the Court of Special Appeals of Maryland (the "Court") decided in *Peterbilt of Baltimore LLC v. Capitol Gateway Properties, LLC*^[1] that provisions of an option to purchase (the "Option") pursuant to the tenant's lease are conditions precedent, which must be satisfied to exercise such Option.

Peterbilt of Baltimore LLC ("Peterbilt") entered into a lease agreement with Capitol Gateway Properties, LLC ("Capitol Gateway"), as landlord, on January 13, 2014 (the "Lease"). The Lease of the real property located at 8300 Ardwick Ardmore Road, Landover, Maryland (the "Property") was for an initial term of ten years. In exchange for Peterbilt's agreement to pay above market rent for the Property, Capitol Gateway agreed to include the Option to buy the Property after the first and second five-year terms. On January 22, 2019, Peterbilt sent Capitol Gateway written notice that it sought to exercise the Option. Peterbilt's notice triggered a multistep process to determine the purchase price of the Property (the "Option Procedures").^[2]

Under the Option Procedures, the purchase price was required to be the fair market value (the "FMV") of the Property as of the date Peterbilt exercised the Option. If Peterbilt and Capitol Gateway could not agree upon the FMV, the parties were required to obtain certified real estate appraisers, advise one another of their respective appraiser's information, and provide the opposing party a copy of such appraiser's report once issued. If the difference in the two appraised values was greater than ten percent, the respective appraisers were required to meet and agree upon the FMV. If the appraisers could not agree on the FMV, they would have to jointly agree on the appointment of a third appraiser.^[3]

Peterbilt had applied for financing to acquire the Property in the amount of the lesser of \$6,000,000 or 80% of the appraised value.^[4] As such, the potential lender hired an appraiser (the "Peterbilt Appraiser") in connection with the application, who appraised the Property at \$2,800,000. Peterbilt notified Capitol Gateway of such appraisal on February 26, 2019. Capitol Gateway notified Peterbilt of its appraiser (the "Capitol Gateway Appraiser") on March 7, 2019, and the Capitol Gateway Appraiser delivered an appraisal of \$4,530,000 to Peterbilt on May 7, 2019.^[5] As the difference in appraisals was greater than ten percent, the Capitol Gateway Appraiser contacted the Peterbilt Appraiser to meet and discuss their valuations, but the meeting never occurred. The Peterbilt Appraiser refused to comply with the Option Procedures because he was engaged by the potential lender, rather than specifically engaged by Peterbilt. For the same reason, Capitol Gateway contended it was not required to appoint a third appraiser because Peterbilt had already failed to satisfy the Option Procedures in not hiring its own appraiser.^[6]

The Court held that the Circuit Court for Talbot County did not err in finding the Option Procedures were conditions precedent to the exercise of the Option, as opposed to covenants, which would have allowed Peterbilt the opportunity to cure. The Court reasoned that the Option Procedures were material terms of the Lease, and where a step was not completed by one party, performance by the other party would not arise.^[7] The Circuit Court concluded that the Lease required the parties to obtain an appraiser who would go further than solely appraising the Property, but, rather, would communicate the appraisal value to the opposing party, confer with the other appraiser if their values were not within ten percent, and jointly appoint a third appraiser if the original appraisers could not agree on the FMV.^[8]

Peterbilt failed to retain an appraiser who would comply with the Option Procedures; thus, Capitol Gateway was not required to perform under the Option by naming a third appraiser.^[9] Furthermore, because the Option Procedures constituted conditions precedent to the exercise of the Option, the Court upheld the circuit court's finding that Peterbilt's noncompliance was not a breach of contract. Accordingly, Peterbilt was not entitled to cure and Capitol Gateway was not entitled to attorney's fees.^[10]

Successful exercise of an option requires unequivocal compliance with the terms of such option. Strict adherence to the specific provisions of a purchase option is necessary to effectuate the option; thus, drafting of option provisions should be carefully considered. This is another example, albeit not relied upon by the Court, of the doctrine of *strictissimi juris* or “strict construction.” This doctrine generally provides that a court will apply strict construction of a contract and especially a lease when it affects the alienation of property. Courts are loathe to divest parties of real property, and consequently will strictly construe provisions which purport to alienate property or constitute restraints on the alienation of property. Since a lease is both a contract and a conveyance, courts typically will apply this rule of strict construction.

[1] *Peterbilt of Baltimore LLC v. Capitol Gateway Properties, LLC*, 2022 WL 833362 (Md. Ct. Spec. App. Mar. 21, 2022) (unreported).

[2] *Peterbilt v. Capitol Gateway Properties*, 2022 WL 833362, at 1.

[3] *Id.*

[4] *Id.* at 2.

[5] *Id.* at 3.

[6] *Peterbilt v. Capitol Gateway Properties*, 2022 WL 833362, at 4.

[7] *Peterbilt v. Capitol Gateway Properties*, 2022 WL 833362, at 10-11.

[8] *Id.* at 7.

[9] *Id.* at 8.

[10] *Id.* at 12-13.