



Attorneys at Law

COVID-19 UPDATE

Real Estate and Business Transactions during the COVID-19 Pandemic: Can my transaction still close?

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In an effort to reduce the anticipated spread of the COVID-19 virus, on March 23, 2020, the Governor of the State of Hawaii issued a proclamation that requires all persons in the State to remain at home or at their place of residence starting on March 25 and continuing until April 30, 2020. Earlier proclamations by the Mayors of various counties, including Mayor Kirk Caldwell of the City and County of Honolulu, issued similar work-from-home mandates and closed restaurants, bars, and many other places of business. The resulting shut-down and closure of all but those companies conducting what is defined as Essential Business, is expected to create significant financial hardship for many (if not all) businesses in Hawaii, from retail to manufacturing, restaurants to processing, and industrial to professional services.

Purchase and sale transactions involving real property and/or businesses in Hawaii are typically handled through escrow and title companies like Title Guaranty of Hawaii, Inc., First American Title Company, Old Republic Title and Escrow Company, and Fidelity National Title Company, to name a few. At closing, the title company arranges for the recordation of necessary documents with the State of Hawaii Bureau of Conveyances or Land Court and the escrow company coordinates the payment of the purchase price with the final delivery of closing documents and title. In a COVID-19 world, many are asking whether transactions will still be able to proceed to closing.

The short (and fortunate) answer is “Yes.” However, it is important to understand some things that have changed, how to navigate these changes, and what to expect as you move through a transaction during this period of changes which include government shutdowns, business closures, stay-at-home/work-from-home and quarantining. Here is a look at how a typical real estate and a typical business purchase and sale agreement is expected to work in a COVID-19 world.

REAL ESTATE SALE TRANSACTIONS

1. Contracting. The process of negotiating and executing a real estate purchase and sale agreement, whether for a residential property acquisition or the purchase of a

commercial property, has not changed much. Residential transactions in Hawaii typically use the standard Hawaii Association of Realtors (“HAR”) Purchase Contract form that is completed with the help of a broker and executed via DocuSign or other electronic signature means. The HAR has prepared a COVID-19 addendum to the standard form Purchase Contract which addresses pandemic-related delays and many brokers and attorneys have also prepared similar addenda. Commercial purchase and sale agreements typically include provisions that allow for counterpart signatures and scanned or faxed copies are accepted as originals.

2. Due Diligence. Here is where there are difficulties. Buyers may not be able to physically inspect the properties they intend to purchase. In most cases, home inspectors will be able to arrange for a professional inspection with appropriate social distancing and cleaning. If the family is still in the house, they may not be comfortable with allowing inspectors in their home. Parties may then need to consider alternatives to a physical inspection by buyer prior to closing. Video inspections are one possibility, with seller either preparing a video walk-through of the house and property or going on-line with a buyer and doing a live video walk-through of the property. The parties may also agree to certain parameters for exceptions to a standard “as is” purchase that would, for example, retain a certain amount of the purchase price in escrow after closing to potentially be applied against repair items discovered by a standard inspection conducted as soon as such services are available. This could provide sufficient comfort to a buyer to close a purchase without a physical inspection because the risk of major problems would be offset by certain funds set aside to cover such repairs. Sellers will also need to consider where they would relocate in the event that their home requires termite treatment prior to the closing and their vacating the property.
3. Execution of Documents. One of the primary concerns with the Governor’s mandate was the anticipated unavailability of notary services. The State of Hawaii Attorney General’s Notary Office closed, however, Emergency Rules for Notaries Public were issued that allow for, among other things, notarization by video. The Emergency Rules for Notaries can be found at: <http://ag.hawaii.gov/notaries-public/>. Consistent with the Emergency Rules, escrow companies are arranging drive-through/drive-by notary services and arranging for in-house signings. Lawyers and real estate brokers are helping to deliver and collect documents and arrange for signings consistent with social distancing requirements and stay-at-home orders. However, the process takes more time and coordination than usual. Real estate purchase agreements will need to build in sufficient time to have documents signed, notarized and delivered to the escrow company. If a property is being financed, careful coordination with the lending bank will be required to ensure all of the bank’s requirements can be met and all documents signed prior to the scheduled closing.
4. Recordation of documents. Title companies have stepped in to help resolve title insurance issues caused by delayed filing as a result of the Bureau of Conveyances limiting in-person transactions. Title companies are issuing gap coverage to address

the gap between the date and time of closing and the time of ultimate recordation as noted by the Bureau of Conveyances. Escrow companies, attorneys, and brokers are coordinating with lenders (including seller's lenders to be paid off at closing) to ensure everyone's needs are met at closing.

5. Other issues. If it seems that things are essentially "business as usual" in the real estate transactions world, it is not. There are numerous hurdles to overcome and continuing unknowns that may affect your transaction. Although right now it appears that real property surveyors, appraisers, and residential termite inspectors are continuing to visit properties and provide services, there is no guaranty that this will continue. Real property staking and surveying (even though it is conducted outside) may not be possible, and lenders typically require a survey in connection with the lender's title insurance policy to be issued at closing. Sellers may not be able to move out of the property at closing due to travel restrictions, business closures, and stay-at-home-orders. Termite inspections and treatments may not be possible, and other repairs may not be able to be made prior to closing. Changes in a buyer's financial situation may make it impossible to obtain the financing required to purchase the property. There are potential "fixes" and "work-arounds" for each of these issues, but they will require open and clear communication and cooperation and in many cases the foresight to anticipate these issues and address them directly in your agreement. Your real estate professional should help you consider and address these issues prospectively to avoid surprises as closing approaches.

THE SALE OF A BUSINESS

1. Contracting. As with real estate transactions, the process of negotiating and executing an asset purchase agreement or a stock/membership interest purchase agreement has not changed, although closures, shut-downs, stay-at-home/work-from-home orders and quarantine requirements now require careful consideration of provisions relating to due diligence inspection, as-is acceptance, and post-closing inspection and liability allocation. Parties to contracts for business mergers and sales already in place may wish to consider creative amendments that will address the various business and financial changes resulting from COVID-19 and the government actions taken in response to it, as well as government relief packages like the CARES Act (see discussion in Section 4 below). Parties need to accept the realities of the current COVID-19 world and the future uncertainties this has created. Creative attorneys can then help to negotiate and draft agreements that balance the risks and potential rewards and achieve a meeting of the minds between a buyer and a seller.
2. Due Diligence. Due diligence review of the assets and finances of a business will be challenging in the COVID-19 world. Three things in particular may force parties to postpone closing or cancel a sale. First, buying the assets of a business (and if you are purchasing the stock, you are still looking at the assets) is difficult if you cannot physically inspect the assets. Depending on the nature of the business being sold, there may be equipment, inventory, materials, supplies, real property, fixtures, vehicles, and other assets that may need to be carefully inspected, counted, valued

and approved. Second, it may not be possible to get information and certifications from tax authorities, including but not limited to tax clearance certificates and bulk sales certificates. With physical delivery and in person applications for these documents at the tax offices no longer available, the anticipated wait time to receive these documents is expected to be two weeks or longer. Third, the effects of COVID-19 and the subsequent government actions have significantly affected businesses, forcing many to shut-down completely, to furlough employees, to renegotiate leases and loan payments, and to reassess business plans, budgeting, and profitability. This is a moving target that makes it extremely difficult to value a business as an on-going concern and therefore challenging to reach an agreement as to an appropriate purchase price. Realistic and meaningful due diligence will be also be challenging (and in some cases may not be possible) until some time passes and the parties are able to assess the condition of the business as it comes out of this crisis and resumes operation. For those motivated to proceed, creative and manageable solutions to these challenges exist as long as all parties are prepared to exercise some patience and flexibility.

3. Closing. Most business mergers and acquisitions are handled through attorneys and brokers without the need of setting up a formal escrow with an escrow company. Likewise, the majority of the documents needed to complete a change in the ownership and management of a company can be performed by attorneys acting remotely and filings can be made online with the State of Hawaii Department of Commerce and Consumer Affairs (DCCA). However, filings may still need to be made with the Bureau of Conveyances. As a condition of closing, a loan may need to be paid off and company assets that served as security released. In an asset sale, real property assets will need to be conveyed. In many cases, therefore, you may still need to engage an escrow company to handle at least some aspects of a business sale transaction. Issues with the notarization of documents and recordation of documents discussed in connection with a real property sale above are therefore often equally applicable to the sale of a business. Other closing deliveries and approvals may also be delayed as a result of government offices being closed or backlogged. Parties interested in closing soon may need to consider how to structure deliveries and post-closing obligations to ensure all conveyances are completed in a manner that allows for the continuation of business (as much as that is possible) and the alignment of incentives and rewards. For example, the parties may wish to bifurcate the closing to have portions of the purchase price released upon the delivery by seller of required approvals, releases, tax certificates, etc. The specifics will depend upon the particular business, assets, and deal points.
4. The CARES Act. The current COVID-19 world is challenging for even the most robust of businesses, with only a precious few unaffected or positively affected. On March 27, 2020, Congress passed the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) and shortly thereafter, President Trump signed the CARES Act into law to help rescue the suffering United States economy. Among other things, the CARES Act provides for financial assistance to qualified businesses through loan programs overseen by the Small Business Administration. A discussion

of the Paycheck Protection Program offered as a part of the CARES Act, which program provides funds through government-supported loans to offer a direct incentive to employers to keep their workers on payroll, is detailed in a separate BLRH memo. Parties to a business sale transaction will need to communicate and cooperate to ensure that eligibility requirements are met, applications are timely submitted, and appropriate actions are taken to allow businesses to take advantage of potential financial and other relief available to the business through the CARES Act and other programs.

5. Licenses and Other Issues. In addition to the items and issues discussed above, the conveyance of a business whether by asset or stock/membership interest sale, may require the assignment of certain licenses or permits, or the approval of certain government authorities. For example, the sale of a restaurant or bar will likely involve the transfer or new issuance of a liquor license which will require applications to and approvals from the county liquor commission, the purchase of a contracting business may require notices and approvals from the DCCA's Professional and Vocational Licensing Division, and the sale of a transportation company may require a transfer or new issuance of a Public Utilities Commission license. While these are all issues faced by parties to a business sale transaction at whatever time such a transaction takes place, the ability to obtain these licensing and other approvals, and the time it may take to receive them in this COVID-19 world, need to be carefully considered and addressed by the parties.

The above is far from an exhaustive list of issues and potential problems you may encounter as you look to proceed with your transaction. The specific terms and conditions of each real property and business sale transaction are different, as are the parties' respective situations, financial conditions, and needs. Can a real estate or business sale transaction close even as we struggle to deal with the effects of COVID-19 and all that is being done to combat the spread of the virus? Yes. Will it be an easy and smooth process? That will depend on how prepared you and your team are to deal with the new challenges presented by a COVID-19 world. Advice and assistance from an experienced real estate/business attorney who understands real estate and business transactions in general, and the specific issues arising in such transactions taking place in a COVID-19 world, is the key to a successful transaction.

Craig P. Wagnild is a partner at Bays Lung Rose Holma and serves as chair of the firm's Transactional Law Department. He concentrates his practice in business entities and corporate law, real estate transactions, commercial leasing, real estate development, real estate finance, general business, and international business transactions. Mr. Wagnild also assists clients in structuring and forming limited liability companies and other business entities as well as mergers and acquisitions transactions. He was recognized in *Best Lawyers*® as the 2014 Lawyer of the Year for Business Organizations (including LLCs and Partnerships) and has been repeatedly recognized in the areas of business organizations and real estate law. He is a member of the American Bar Association, the Hawaii State Bar Association, the Japan-America Society of

Hawaii, and the Washington State Bar Association. Mr. Wagnild served as the 2013 president of the Hawaii State Bar Association, and current serves as the Treasurer of the Hawaii State Bar Foundation. He regularly writes and speaks on the topics of real estate and business law.

Bays Lung Rose Holma is a civil litigation and commercial transactions law firm located in Honolulu, Hawaii and specializing in real estate, construction, business law, commercial financing, and employment law. As an identified Essential Business, BLRH attorneys are available to advise and assist clients, including property owners and their property managers, at any time during and throughout the Covid-19 crisis. BLRH can be reached at (808) 523-9000 with calls directed to someone who can assist you, or via e-mail at mail@legalthawaii.com. In addition, a listing of our attorneys along with their telephone numbers and email addresses is available at www.legalthawaii.com.