

The Art of Real Estate Negotiations

Joshua Stein

The essence of negotiation is persuasion, not confrontation.

IN EVERY REAL ESTATE NEGOTIATION, a “Negotiator” needs to figure out how to sell, persuade, neutralize, or in some other way satisfy someone else—“The Other Side.” Often the Negotiator must satisfy a whole roomful of Other Sides, each with its own agenda: a lender, a tenant, an equity investor, another equity investor, other participants. Sometimes one party

needs the deal as much as the other. Other times one party holds all the cards, or thinks it does. (For ease of exposition, this chapter assumes a negotiation between two parties: “Our Side,” represented by the “Negotiator”; and “The Other Side,” represented by its “Representative.”)

Whether the negotiation involves a lease, a workout, a purchase, or financing of a multi-

Joshua Stein is a real estate and finance partner in the New York City office of Latham & Watkins and a member of the American College of Real Estate Lawyers. He chairs the Practising Law Institute’s annual seminar on commercial real estate finance and co-chairs the New York State Bar Association Commercial Leasing Committee. This article is reprinted from Mr. Stein’s recent ALI-ABA Book *A Practical Guide To Real Estate Practice*. To order that book call 1-800-CLE-NEWS and ask for Customer Service or visit ALI-ABA’s web page at www.alai-aba.org. (An earlier version of this article appeared in *Real Estate Review*.) Copyright © 2001 Joshua Stein (joshua.stein@lw.com or www.real-estate-law.com).

state portfolio, or even a contract for the sale of a house, the Negotiator's goal is always the same: to convince The Other Side to go along with Our Side, on terms that work for Our Side. Negotiators have many names for that process, including "making a deal," "selling," "horse trading," "getting to yes," and "manipulating." But negotiating always boils down to understanding The Other Side's psychology and agenda, and persuading The Other Side to accept the Negotiator's view of the solution.

WHO REPRESENTS THE OTHER SIDE? •

The experienced Negotiator begins by asking exactly who represents The Other Side. Does the representative have authority to make a deal? Or have the real decision makers merely sent someone whose job is to extract a first round of concessions, but who has authority, in turn, to make only negligible concessions? This ploy allows someone higher up to step in to finish the job and, possibly, to take back some of the first representative's concessions.

If The Other Side's Representative's hands are tied, Our Side would be foolish to send someone with the authority to trade away points, make concessions, and get the deal done. Our Side's Negotiator would do what he or she has the authority to do, while the Representative might concede little, reserving much for further discussion.

Even if the low-level Representative does in fact have authority to try to make a deal—subject to confirmation and approval by a senior person—Our Side may suffer simply because of The Other Side's internal organizational dynamics.

The Other Side's Representative may make a deal that is perfectly reasonable, logical, and appropriate under the circumstances. When a subordinate makes a deal and explains it to his or her superiors, however, those superiors often need to show that they are tough and responsi-

ble, and that they can add value to a transaction. (Otherwise, why does the organization need them?)

Therefore, The Other Side's executive (second-guesser) might scrutinize and question the proposed deal much more critically than if he or she had been on the firing line initially. Indeed, the senior person might well have made the same deal on the same terms and deemed it perfectly good under the circumstances.

For these reasons, a Negotiator should try to have The Other Side send to the negotiation the highest-level Representative who can reasonably be requested. And the Negotiator should try to assure that the authority levels of negotiators on both sides are reasonably well balanced (or tipped in Our Side's favor).

THE NEGOTIATING TIMETABLE • If both parties want to close a deal quickly, they should probably bring in their higher level negotiators at the outset, and in other ways try to do everything possible to move the process along.

If Our Side is in no hurry but believes The Other Side needs a quick deal, Our Side may want to slow the process by starting the exchanges with low-authority negotiators. The Negotiator would work through each issue deliberately and carefully, taking his or her time about setting up meetings, not expediting the process. The Negotiator might suspend negotiations while the attorneys redraft, then study the redrafts carefully to assure they are as complete and correct as possible before circulating them for review and discussion.

This approach might set the stage for a time crunch that may ultimately work in the Negotiator's favor.

A time crunch can also sometimes explode in the face of the side dragging its feet. The more unstable and tense a situation, the less anyone can predict and control it. The Negotiator may

think that instability and tension give Our Side an advantage, but he or she could be missing a crucial piece of information about the deal or about The Other Side's options that changes everything.

Whether and how to set up instability and tension is a delicate strategic decision, more art than science.

PERSONAL RELATIONSHIPS AMONG NEGOTIATORS • As early as possible in negotiations, the Negotiator should get to know the people on The Other Side as individuals. He or she may want to ask about their families, their roles in their company, their hobbies and interests, and what is going on in their lives. The Negotiator should build friendly relationships to the extent possible.

Most people want to please and help their friends. Good feelings among the negotiators make the rough and tumble of negotiating smoother and more pleasant and may produce better results for everyone. At a minimum, good interpersonal relationships may lead both parties to skip the posturing and gratuitous confrontation, so common in many negotiations, that can waste time, create ill will, and even frustrate transactions.

Good negotiators make "small talk" with the opposing side(s). When the formal meeting recesses, though, they discuss anything except the business at hand. They don't talk shop. They avoid any topic remotely close to the subject of the negotiation, such as similar transactions that they recently closed.

Casual remarks, if relevant to the transaction or any similar transaction, can suggest concerns, issues, or ideas about the transaction that The Other Side might otherwise not have raised and that Our Side may prefer not to face. So skilled negotiators talk about weather, family, golf, baseball, music, concerts, or anything else

as long as it is irrelevant to the business agenda—unless they make a deliberate strategic determination that small talk is the right way to present or resolve an issue.

Working Together

The Negotiator should try to develop a sense of shared achievement, treating the participants as partners who are working hard to get to a reasonable middle ground. When the two sides reach a compromise, both sides "own" the outcome.

Once the parties have agreed about substantive issues, a Negotiator will treat the differences as history, emphasizing instead the mechanics and logistics of how the parties will document and close their new agreement.

The more the parties talk about logistics, process, and timing, the more they cement their shared commitment to the resolution reached. This reduces the likelihood that The Other Side will reopen issues. It also produces positive momentum and a state of mind that moves the process along.

Positive momentum and positive states of mind often peak shortly after the parties have achieved, recognized, and confirmed a breakthrough. This may be the right time for the Negotiator to raise any troublesome or awkward issues that remain.

During the negotiations, the parties may have agreed to set aside temporarily certain sticky secondary issues. A successful Negotiator must not let these issues fester. If they are not resolved, the judgment that they are secondary may turn out to be wrong. They may instead turn out to be fundamental, particularly if the parties finally focus on them at the last minute. If these issues will not get resolved, the parties might save time, money, and effort by recognizing the deadlock early and moving to a com-

pletely different approach or to a completely different transaction.

REACHING A COMPROMISE • The mechanics of compromise may be as important as the concessions themselves. Once a Negotiator suggests, even in the most tentative and hypothetical terms, a possible framework for compromise, he or she has just compromised. Nine times out of 10 it cannot be taken back. So before a Negotiator tries to break through on a major issue, he or she must be careful about what is said and when. A Negotiator should not suggest a framework for compromise unless Our Side is ready to live with it.

As the flip side of this proposition, a Negotiator can sometimes get what Our Side wants just by suggesting a palatable way to break a deadlock. The Other Side may be so relieved at having a concrete proposal to think about that they will embrace it in large part just because it is there.

Similarly (again both good and bad depending on the Negotiator's agenda), once Our Side suggests a number—a price, a delivery date, whatever—the Negotiator can assume The Other Side will seize that number and never let go. If that is the result the Negotiator wants, terrific. But if the Negotiator wanted flexibility, he or she just lost it. The Negotiator will never be able to improve Our Side's position by making a subsequent proposal more favorable to Our Side.

Until he or she is ready to commit, any detail that the Negotiator offers can put him or her at a disadvantage. The more details the Negotiator gives, the more opportunities The Other Side has to find problems, or to accept the details that they like while negotiating away, or ignoring, the details they don't.

Therefore, a Negotiator should be mysterious when he or she can, not giving too many details

until confident that the idea is ready for the harsh light of the stage. The Negotiator needs to confirm that Our Side can live with every aspect of the proposal.

The quintessential example of the advantages of mystery may be Richard Nixon's "secret plan" for peace in Vietnam. It was an effective, credible campaign ploy in part because the candidate said so little. Had he given details, the debate would have turned to those details. The details, and objections to them, would have overwhelmed the idea of a "plan" and perhaps Nixon's candidacy. (Of course, the merits of the "secret plan"—and its effectiveness in negotiations with the North Vietnamese—represent a different discussion entirely. I mention it only as it relates to the role of details in presenting a proposal.)

MAKING A PROPOSAL • If The Other Side demands details, the Negotiator should use the Other Side's interest as an opportunity to draw them into helping structure a proposal as if it were their own. The Negotiator should solicit the Representative's comments, ideas, and thoughts and use them in his or her proposal to the extent possible. The Negotiator should help The Other Side to develop a sense that they share ownership of the proposal.

How the Negotiator presents a new idea or a new proposal can be extremely important. If the idea or proposal is revolutionary or difficult to explain, it should often be presented "one on one" to an appropriate individual, not to a larger group. If the Negotiator presents a major new idea in a large meeting, each person on The Other Side may vie against his or her colleagues to try to find problems. The fact that peers are watching may make everyone tough and inflexible.

If the Negotiator presents the proposal "one on one," however, he or she can better control

the Representative's reaction and how the Negotiator responds to it. The Negotiator can often better sell the idea this way.

RESPONDING TO A PROPOSAL • Knowing how to respond to The Other Side's proposals is at least as important as knowing how to set up and present a proposal.

Once in a while, the Negotiator can respond with a simple "no," or its first cousin, "our organization has a policy against that," or the bureaucrat's first argument against everything: "If we did it for you, we'd have to do it for everyone."

This tiresome trio of responses, never very compelling to begin with, has become even less so in today's era of quick business deals and nimble organizations. It hardly demonstrates a Negotiator's desire to reach an agreement. Business organizations have learned that they must be flexible or they will lose business to their competitors. As a leading former student at the London School of Economics, Mick Jagger, put it: "If you can't rock me, somebody will."

For the most part, a Negotiator can't "just say no" any more. The opposing party expects responses that are flexible, logical, and rational. If the answer is "no," it requires a rational explanation. That process may itself resolve the impasse.

An Instructive Example

In a recent transaction, a developer was selling a partnership interest in a development still in the early approvals stage, an unfinanceable asset. The purchaser was short of cash, but the seller insisted on cash at closing. These incompatible positions seemed to lead inevitably to deadlock.

Seeking a solution, the purchaser asked the seller to explain why he so adamantly insisted

Once in a while, the Negotiator can respond with a simple "no," or its first cousin, "our organization has a policy against that," or the bureaucrat's first argument against everything: "If we did it for you, we'd have to do it for everyone."

on receiving immediate cash, beyond the normal explanation that everyone always needs more cash.

The seller explained that he had an unsecured bank loan he was no longer able to carry. The bank was pressing him into a corner, where he would soon face personal bankruptcy. He intended to use the cash sale proceeds to repay the loan.

Working together, the parties crafted a "win-win" solution that had not occurred to the seller. The purchaser offered to assume the seller's bank debt and to convince the bank to release the seller from that debt. The seller would be out from under. The purchaser would conserve cash without having to arrange a new loan. All the parties won. Even the bank won, by exchanging a borrower with the seller's weak financial statement for a new, more solvent borrower.

The parties reached their compromise because the purchaser forced the seller to explain rationally why he needed cash so badly at the closing.

COMPROMISES AND CONCESSIONS •

The following are a few more thoughts about the mechanics of achieving compromises and handling concessions.

Rationality Can Produce Solutions

At its best, the “rational” approach to negotiations, as demonstrated in the above example, can lead The Other Side to suggest the very solution that Our Side might have suggested. Had Our Side’s Negotiator offered the same solution, The Other Side might have questioned it and tried to compromise it away. Because it is The Other Side’s proposal rather than Our Side’s, though, no “selling” is necessary. Our Side’s major challenge may be figuring out how to gracefully accept The Other Side’s proposal—with due deliberation and skepticism—without being overly gleeful about it.

Don’t Give It Away

Once the parties are into negotiations, both sides usually want to eliminate uncertainty and to resolve issues quickly. The Negotiator should not let this sense of urgency lead him or her to concede issues without getting something in exchange.

Whether the Negotiator concedes an issue because it is the only rational solution, as in the example above, or because The Other Side has proposed a reasonable compromise, every concession should if possible be part of a package where Our Side gives something—ideally something Our Side planned to give up anyway—but gets something at the same time. The value of a concession is at its highest just before it is actually made. As soon as the Negotiator makes a concession or telegraphs that he or she intends to, it becomes yesterday’s news and no longer can buy anything.

Threats

A threat is stronger before it is acted upon than after. The possibility that one party might

do something can create leverage. Once the threat is carried out (selling the property to, or obtaining the loan from, someone else), it is no longer a weapon. But a negotiator who makes threats, without acting on them, reduces the credibility of all future threats. Therefore, the best threat is an unstated one, or one communicated ambiguously through “back channels.”

Starting Positions

If the Negotiator wants or needs something from the transaction, he should ask for it. Strong negotiators are never timid. They don’t negotiate internally with themselves before they put their proposal on the table. The worst that can happen to a request is that The Other Side says no. If the Negotiator asks for too much, the Other Side will not hesitate to say so. The Negotiator can then trade away the excessive demand for something else. But if the Negotiator never asks at all, Our Side will never get what it needs.

Humility

A Negotiator making a proposal should not plead for it, or present it to The Other Side as if it were some kind of humble application. The Negotiator raises an issue because Our Side expects it to be dealt with and resolved, and because Our Side expects to achieve what it needs. If the Negotiator goes on the defensive when a discussion begins, he or she will probably stay there.

Accepting Concessions

Finally, in accepting The Other Side’s concessions, the Negotiator needs to think about how that acceptance will be perceived. If The Negotiator accepts a proposal too quickly, without serious thought, The Other Side may conclude that it gave away too much (and will eventually figure out a way to get it back). The same result may follow if Our Side somehow expresses appreciation for The Other Side’s concession.

In each case, Our Side violates an important principle of negotiations: both parties need to feel they have had a constructive process of give and take, producing a reasonable outcome in which neither is a victim or victor. Any suggestion that the result unreasonably favors one party or the other may lead the "losers" to think they gave away more than they had to.

THE IMPORTANCE OF TIMING • Timing is always crucial in negotiations. Some particularly sensitive issues of timing:

New Issues

The Negotiator should plan when and how to raise new issues and how to put them on the agenda. If he or she overloads the negotiating table at the beginning, the Negotiator may slow or even stop the process. He or she may want to start out with issues that will be easy to resolve, thus creating positive momentum.

Sometimes the Negotiator enters a meeting not quite prepared. Our Side may have been dilatory and not have decided exactly what position to take on some issues. If the Negotiator raises an issue without asking for something specific, Our Side is unlikely to end up with the result it needs.

If the Negotiator is not yet ready to present an issue, he or she should leave it off the agenda for the time being. Of course, the Negotiator must leave the door open so The Other Side understands that additional issues may remain. Otherwise, the mere passage of time will automatically put the Negotiator on the defensive when Our Side has finally decided what we want and how to ask for it.

The Other Side's Mood

The Negotiator should pay attention to The Other Side's mood. If The Other Side is in an angry and difficult mood, or has voiced or sug-

gested questions about Our Side's commitment to the transaction or negotiating positions, Our Side should avoid raising new issues that might create trouble. Save those issues for later.

Conversely, if Our Side has just won some issues, the "momentum" may favor raising more issues right now because The Other Side is in a concessionary frame of mind.

Controlling the Agenda

If the Negotiator finds he or she is losing on an issue, he or she may want to take it off the table for now, and defer the debate. The Negotiator can say he or she needs more information, or needs to discuss the issue with someone, or needs time to look into it more. The Negotiator should provide a decent reason to defer an issue. He or she can raise the issue again when better prepared, or when he or she has developed better arguments or found something to trade for it.

Sometimes the Negotiator will want to save one or two major issues for the very end of the negotiations, so the Negotiator can present them as "the final issue(s)" of the negotiation. If, at that point, The Other Side is committed to the deal and is enthusiastic about being close to the end of discussions, they may be predisposed to accept the Negotiator's position on "the final issue," whatever it is. But the Negotiator must be sure to present this "final issue" in a way that does not make The Other Side think it is merely a "final grab."

THE DOCUMENTS • Whatever agreement the parties reach will be reflected in a set of documents. The development of those documents is an important corollary to the negotiations themselves. It will often receive a great deal of attention as the negotiations work their way through to conclusion. Negotiators should keep several principles in mind as they move from discussions to documents.

Rarely will a problem or an issue go away because the attorneys do a great job on the documents or “come up with something” that adequately addresses everyone’s needs. In most cases, if the parties have not truly resolved the problem, it will simply reappear in the next draft.

Control of the Documents

Many believe Our Side should try to control the documents. By controlling the documents, Our Side can decide exactly how to present issues and compromises and to some degree control the negotiations. Care and diligence by The Other Side can, however, make up for these advantages. Our Side can then be left with the logistical burden, distraction, and expense of coordinating documents and taking the blame for delays, instead of focusing on substance and results. Therefore Our Side may want to be strategic about the documents, maintaining control of only the fundamental documents while graciously allowing The Other Side to handle the rest.

Incorporate Positions

To the extent that Our Side controls the documents, Our Side should incorporate its positions into those documents as early as possible. A position already in a document achieves a degree of momentum. Anyone who challenges that position is challenging the progress of the

documents and the transaction. And the challenger bears the burden of having to explain why he or she didn’t raise the issue earlier in the process. In contrast, if Our Side identifies an issue in a document as “To be discussed,” then Our Side admits that Our Side does not quite know what it wants. This approach undercuts whatever Our Side might eventually decide to request. It also assures The Other Side will focus on Our Side’s position with special care once Our Side finally decides what it wants.

Know the Existing Documents

Before the Negotiator raises any issue, he or she should know how existing documentation already deals with it. If the Negotiator wants Our Side to be free to transfer a partnership interest or a lease, he or she must know how the current documents restrict transfer. If the existing restrictions are negligible, the discussion may lead The Other Side to want to tighten them. The Negotiator might have achieved a better result by saying nothing at all.

Ambiguity Is Not Always Bad

Some negotiators believe they should eliminate any ambiguity or uncertainty in the documents, a process that any smart attorney can continue almost without limit. Sometimes, however, Our Side may prefer to live with the ambiguity that exists rather than to deal with the consequences of a full discussion of the issue. If resolution of the ambiguity will probably lead to a negotiation that Our Side will probably lose, the ambiguity in the existing documents may beat the certainty of an inferior resolution. Any such judgment represents a business decision, though. If you are the attorney who decides to live with an ambiguity, you want to assure that no one can say, after the fact, that it arose merely because you were careless. This may require some written record of how the decision was reached.

Documents Don't Resolve Issues or Problems

Rarely will a problem or an issue go away because the attorneys do a great job on the documents or "come up with something" that adequately addresses everyone's needs. In most cases, if the parties have not truly resolved the problem, it will simply reappear in the next draft. Careful negotiators, particularly if they are under time pressure, will not fall into the trap of thinking otherwise.

Trading Substantive for Speculative Rights

A careful Negotiator will avoid trading away an issue for a concession from The Other Side that may offer benefits unlikely to be realized, or that for other reasons ultimately may not work, such as "a share of the profits" or "whatever security or assurances you want" or "an option to unwind." Measures like these often turn out to be impossible to resolve and work out. Once the parties try to document them, they create an endless panoply of issues until the parties finally give up. If Our Side gives up

something real in exchange for one of these chimerical measures, Our Side may give up "something" in exchange for "nothing."

DISREGARD THIS ARTICLE • As a final thought, negotiators must be ready to ignore any or all of the ideas and principles outlined above. Successful maneuvering at the negotiation table depends largely on instinct and a sense of people, the situation, and its larger context.

Although the principles outlined here have worked well for the author, a negotiator must respond to issues and proposals creatively and instinctively. This can sometimes require deliberately breaking the rules to achieve a result. But before a negotiator can deliberately break the rules, he or she should understand them. Most of the great artists of history had to master academic studies before they ventured into their own brand of "creativity" and achieved their signature styles.

To purchase the online version of this article, go to www.ali-aba.org and click on "Articles and Forms Online"

PRACTICE CHECKLIST FOR

The Art of Real Estate Negotiations

In every real estate negotiation, a "Negotiator" needs to figure out how to sell, persuade, neutralize, or in some other way satisfy someone else—"The Other Side." How can you, as the Negotiator, accomplish this goal?

- Begin with the parties:
- Try to have the Other Side represented by someone with authority to negotiate, not a junior who can get but not give, and whose every giving will be second-guessed;

- Determine whether speed or a slower pace of negotiations will benefit Our Side; and
- Develop a good personal relationship with the Other Side. Make small talk to create a friendly environment.

As the negotiation progresses:

- Offer only compromises you are ready to accept. Once made, such suggestions can rarely be taken back;
- When the Other Side makes demands, use those demands to craft a proposal for which the Other Side feels ownership; and
- Present new ideas strategically.

•At the compromise and concession stage:

- Be rational—it is a fast way to create solutions;
- When you concede, get something in return;
- Threats have their uses, but indirect threats may be safer and more effective;
- Assert your positions confidently. Don't apologize for them or pre-negotiate them before you present them; and
- Accepting a concession too quickly may cause the other side to conclude that it has given too much away.

•Plan the timing of your negotiations:

- Plan when to raise new issues;
- Gauge the Other Side's mood, and raise issues accordingly;
- If an issue is going the wrong way, take it off the table "for further study" and return to it later; and
- Consider leaving some of the trickier issues till last, when the momentum of the negotiation and the Other Side's desire to close the deal may help resolve them in your favor.

•How the documents interact with the negotiations:

- Controlling the documents often lets you control the agenda and win some issues. But it also burdens you with the administrative tasks and distraction of document drafting and redrafting;
- If you control the documents, incorporate your positions into them at the earliest possible moment;
- Know the documents and how they deal with an issue before you raise it;
- Consider the possible benefits of ambiguity;
- Documents don't solve problems. Problems that are papered over will come back to haunt you; and
- In drafting the documents, don't trade substantive for speculative rights.

• Finally, be prepared to ignore any of these guidelines for negotiation when it makes sense—but do it intentionally.