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Ten Mistakes Buyers Make When Negotiating Letters of Intent in Commercial Real Estate Transactions in Illinois

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In Chicago and throughout Illinois commercial real estate acquisitions, the letter of intent (LOI) often sets the tone for the transaction. A weak LOI often creates two negotiations. First, you negotiate the LOI, then you renegotiate the same issues in the purchase agreement. Conversely, a strong LOI reduces that waste (and expense). Strong LOIs create faster transactions and, even if an attorney is involved, are considerably less expensive than salvaging a weak LOI or proceeding directly to a purchase agreement.

Every commercial real estate LOI should, at a minimum, list the names of the parties, a property description, the purchase price, any earnest money deposit, the due diligence period and the closing date. However, many “off-the-shelf” LOIs include blanket provisions that lack nuance, strongly favor one side, or fail to account for local customs.

The following are several LOI provisions that can increase expenses for a buyer or create headaches later if not properly addressed in the LOI:

1. **Exclusivity**: Exclusivity prevents the seller from negotiating with other buyers. Without an exclusivity provision, the seller is generally free to shop the property to other buyers. Prudent buyers include an exclusivity provision and ensure that exclusivity is included as a binding term.
2. **Closing Costs**: Closing costs are rarely a one-size-fits-all endeavor. Customs vary by location and transaction type. In Illinois, the seller is typically responsible for the base owner’s policy. In Cook County and other Illinois counties, real estate tax prorations need careful attention because tax bills are often paid in arrears. In Chicago, both the buyer and the seller must pay a transfer tax. Similarly, prudent buyers identify the brokers and state who pays them. Miscommunications over closing costs are often heavily negotiated points in a purchase agreement because they directly affect both parties’ transaction costs.
3. **“As Is:”** Many off-the-shelf LOIs include blanket language like “the property is sold as is.” While most commercial properties are sold “as is,” this blanket language fails to capture nuance that can be extensively negotiated in a purchase agreement, such as casualty, condemnation, operating covenants, representations and warranties, or environmental conditions. If an LOI specifies an as-is sale, prudent buyers clarify that representations, warranties, and covenants will be negotiated in the purchase agreement.
4. **Access and Communication**: Diligence lives in the details. The rent roll, leases, deposits, concessions, delinquencies and utility structure can change the economics of the deal. Acquisitions are often faster when specific types of inspections or documentation are identified in the LOI, especially when an acquisition hinges on a particular set of information.
5. **Due Diligence Start Date**: Many commercial real estate LOIs reference a “30-day due diligence period” without saying when the clock begins. A buyer can lose critical due diligence time chasing documents instead of pushing a transaction forward.
6. **Rent Rolls**: Buyers often ask for a rent roll, but they do not say it must be certified or brought current before closing. In multifamily transactions, a current and certified rent roll is a critical closing delivery that can be lost at the LOI stage.

7. **Assignment**: Many commercial real estate LOIs contain a blanket “no assignment” section. However, buyers often form a new acquisition entity before closing. If the buyer plans to syndicate the purchase, bring in a joint venture partner, or use a fund entity, assignment language matters from the start. The LOI should often allow, at minimum, assignment to an affiliate or newly formed entity without the seller’s consent.
8. **Authority to Sign**: The LOI should confirm that the person signing for the seller has authority. A buyer can be left in a tough spot if they’re negotiating with someone who cannot bind the ownership entity.
9. **Non-Binding Terms**: An LOI should clearly state which provisions are binding and which are not. A common structure is to say the purchase obligation is non-binding until both parties sign a definitive purchase agreement, with select provisions binding the parties immediately. Those binding provisions often include confidentiality, exclusivity, access rules and brokerage provisions.
10. **Remedies**: If terms are binding (such as exclusivity, confidentiality, or access provisions), the LOI should say what happens if someone breaches them. For exclusivity, buyers may want injunctive relief, reimbursement of diligence costs, or another stated remedy. Without a remedy, the provision may be difficult to enforce.

Frequently Asked Questions About LOIs

- **How do I draft a strong LOI for a commercial real estate purchase?** A strong LOI is usually drafted with your attorney involved early in the process.
- **What are common mistakes made in a commercial real estate LOI?** Common LOI mistakes include treating the LOI like a casual email, failing to state which terms are binding, leaving diligence start dates unclear, ignoring prorations, or ignoring local legal issues. Buyers should also avoid signing an LOI before counsel reviews it. The LOI may be short, but it can shape the purchase agreement and limit your leverage.
- **Is a letter of intent binding?** Usually, the obligation to buy or sell is non-binding until the parties sign a purchase agreement. Certain LOI provisions may still be binding, including confidentiality, exclusivity, access rules, broker provisions, or expense reimbursement.
- **What should be included in a commercial real estate LOI?** The LOI should expressly state that it does not bind either party to sign a purchase and sale agreement or close the transaction based on the LOI’s terms, and that the obligation to buy or sell is non-binding until the parties sign a purchase agreement. However, certain LOI provisions should be binding before the purchase agreement is executed, including confidentiality, exclusivity, broker terms, assignment rights, and key operating covenants.
- **How long should the due diligence period be?** The right period depends on the asset. A small, stabilized building may need a shorter review period. A larger property, distressed asset, tax-uncertain asset, or property with physical issues usually needs more time.
- **Should the buyer ask for exclusivity?** Yes, buyers often should ask for exclusivity if they will spend meaningful money on legal review, inspections, lender work, title, survey, or third-party reports.
- **Should an attorney review the LOI before signing?** Yes, an attorney should review your LOI before signing. Legal review before signing helps you avoid unclear language, unintended binding obligations, and weak diligence rights.

Aaron Whyte is a Chicago multifamily real estate attorney focused on helping investors buy small-to-mid-size multifamily assets in the City of Chicago and across Illinois. He advises buyers on purchase agreements, due diligence, leasing risk, title/survey, zoning and closing execution to help deals close smoothly and avoid post-closing surprises. Contact Aaron at awhyte@gouldratner.com.