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Resources

- This Week's Q & A
- Latest Alert
- Articles
- Web Sites
- Sample Policies
- Archives



“Evergreen” and Right-of-First-Refusal Clauses

Set Contract Traps for Unwary Boards

By John Shaffer

Main Menu

- Welcome
- Practice
- Partners
- Associates
- Resources
- Contact Us
- Search Site

Most condominium associations enter into a variety of agreements with different vendors and suppliers to provide essential services, such as laundry room facilities, snow-plowing, and landscape maintenance, to condominium residents. Boards often sign these agreements without paying much attention to the legal terms governing the relationships, but imagine the following scenario:

Your association's five-year contract with its laundry room vendor is ending (and not a moment too soon as far as most board members are concerned). Although the company hasn't done anything terribly wrong, its level of service has slipped steadily over the past couple of years and you've found another vendor offering the association a much better deal along with the promise of better service. You send a letter to the laundry company explaining that the association does not intend to renew the parties' existing agreement and asking the company to remove its laundry equipment from your property at the end of the contract term.



Shortly thereafter, however, the laundry company's in-house attorney responds with a letter indicating cheerfully that the contract, in fact, has already renewed for another five years. The letter explains that the association's contract included a "self-renewal" clause requiring the association to provide "notice of an intent not to renew no less than 90 days but no more than 120 days prior to the end of the current contract term."

Since the association failed to provide that required written notice within the contractual window, the contract automatically renewed itself. As a result, not only can't you take advantage of that better offer (which you better not have signed before getting out of the existing agreement), the association is going to be stuck for another five years with a vendor you don't like who, having now locked you in for another five years, will have little incentive to try and make you like him better. Adding the potential for future insult to that injury, unless someone is paying attention when this new contract ends, the association could find itself in the same position five years from now. That's why they call these self-renewal provisions "evergreen" – because they can last virtually forever.

A Major Concern

Although such self-renewal provisions are common in contracts for services that are provided regularly ¼ laundry room management, garbage pick-up and elevator maintenance, for example ¼ they often go unnoticed when the contract is being negotiated, because boards tend to focus primarily on price, often to the exclusion of other concerns.



If questioned about the contractual language, vendors will usually downplay its significance, insisting that: It is a "minor" provision; it protects both parties; and the board can avoid the automatic renewal by providing the required notice. In fact, the inclusion of an automatic renewal or evergreen clause in any agreement should be anything but a minor concern.

Such provisions protect the vendor's interests while potentially prejudicing the interests of the association. And while it is true that proper notice will short-circuit the automatic renewal of the agreement, given the likelihood that association boards and management companies will change during any five-year period, it is highly unlikely that anyone will notice the automatic renewal provision and the required notification date in time to prevent the renewal.

Somewhat less common than self-renewal provisions, but equally undesirable for community associations, is the "right of first refusal" that many vendors insert in their contracts. A right of first refusal entitles the existing vendor to match the material terms offered by a competing firm at the end of the current contract. Depending on how this clause is drafted, the existing vendor may have the right to exercise its right of first refusal well after the current agreement has expired or been terminated. Like the self-renewal clause, a right of first refusal can act like fly paper, binding an association indefinitely to a relationship it may well want to end.

Limited Options

If you have an agreement with a vendor that includes one or both of these traps – and they are in fact traps – your options are somewhat limited:

- You can hold your nose, accept the new contract and hope the vendor commits a significant breach that gives you a basis for terminating it.
- You can negotiate with the vendor to waive the fly-paper provision. Your prospects here aren't great, however, as vendors won't easily relinquish the option of locking a client into a new long-term contract, particularly in a difficult economy when vendors will do all they can to hang on to the clients they have. Most vendors either won't waive their right under an existing contract or they will demand a buy-out price that associations are unable or unwilling to pay.
- You can ignore the objectionable provisions, sign a contract with the vendor you prefer and dare the existing vendor to sue you. Most will do precisely that. One recent example: Anticipating that a laundry company the association wanted to replace would exercise its right-of-first refusal, the board obtained a proposal from a vendor offering to install new equipment under a one-year contract, foregoing the longer-term most laundry vendors require in order to recoup their up-front investment in the equipment they provide. The existing vendor has claimed the offer is a sham and is threatening to sue the association for negotiating in bad faith.

While suing a client is not a recommended business practice, this example illustrates the importance vendors attach to fly-paper provisions and the lengths to which they will go to enforce them. Large companies – the ones most likely to have self-renewal or right-of-first-refusal provisions – are also likely to have in-house counsel, so litigation costs won't be a serious concern for them, as they should be for community associations. The vendors also have the law on their side. Many of these provisions may be unpalatable but they are enforceable. If you signed the contract, you accepted its terms, even if you didn't anticipate how problematic they might become in the future.

Just Say No

The best way to deal with undesirable contract provisions is to keep them out of the contract at the start, even if that means accepting a smaller cut of the

revenue (on a laundry service contract) or selecting a vendor who charges more. The best way to avoid signing an agreement containing objectionable terms ¾ those discussed in this article and a host of others not mentioned here - is to have your attorney review the agreement terms BEFORE signing.

If you elect to proceed without counsel, there are a number of things you can do to minimize the likelihood that you will be contacting your attorney later to ask how the association can get out of this objectionable contract:

- Put extended terms (more than two or three years) on your list of undesirable contract provisions. With the exception of laundry service companies, which have a legitimate need to recover their investment in the equipment they provide, most vendors have no justification for locking the association into a long-term agreement, other than that it is clearly in their interests to do so. An association has a much better chance of rejecting undesirable provisions during initial contract negotiations than of persuading a vendor not to enforce them after the contract has been signed.
- If a board decides its preference for a particular vendor outweighs its concerns about the self-renewal clause, it should insist on language requiring the vendor to provide a reminder of the required termination notice at least 60 days before the deadline. The board should also make sure that someone is responsible for keeping track of the non-renewal notification dates for this contract and any others with similar provisions and make sure as well to comply with the notice requirements, for example, sending the notice by certified mail or mailing it to a particular address.
- If your board is putting a contract out to bid, make it clear to competing vendors from the start that you consider self-renewal and right-of-first-refusal clauses to be non-starters or include a proposed agreement that the association will accept in the bid package.
- If you are skipping the bid process and negotiating with a selected vendor, ask that vendor to provide a copy of its standard contract up front, before the negotiations begin. This is not a standard request, but there is no reason boards shouldn't insist on it, in the interest of getting fly-paper provisions on the table (and preferably out of the contract) as quickly as possible.

[Home](#)

[Archive of Past Articles](#)

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