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The Warning from Pittsburgh's Golden Triangle: Home of the Steelers, the Pirates and the Amorphous Favoured Nation Clause in the Commercial Lease

Cover Page Footnote
A.B. Brown University; LL.B. Columbia University School of Law; LL.M. New York University School of Law. The author is senior litigation partner of Spitzer & Feldman P.C., New York City and served as lead trial counsel to the defendant landlord in National Intergroup, Inc. v. Oliver Tyrone Corp., No. GD 87-19306 (C.P. Allegheny County Pa., May 19, 1989). The author wishes to acknowledge and express his appreciation to his partner M. James Spitzer, Esq. without whose contribution this article could not have come to fruition, and to his colleagues Michael H. Smith, Esq. and Joseph J. Pash, Jr., Esq. for their invaluable assistance. Appreciation is also expressed to David B. Fawcett, Jr., Esq. and Richard S. Dorfzaun, Esq. of the Pennsylvania bar for their review of the first draft of this article and to Ms. Sheral Delgado for her assistance in preparing the manuscript. Copyright 1995.

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THE WARNING FROM PITTSBURGH'S GOLDEN TRIANGLE: HOME OF THE STEELERS, THE PIRATES AND THE AMORPHOUS FAVORED NATION CLAUSE IN THE COMMERCIAL LEASE

*Ronald J. Offenkrantz**

> *I have decided that the United States should renew Most Favored Nation trading status toward China. This decision, I believe, offers us the best opportunity to lay the basis for long-term sustainable progress in human rights and for the advancement of our other interests with China.*
>
> President Bill Clinton[1]

Introduction

It is not unusual for users of large areas of office space to feel justified in demanding assurance that they are, and will continue to be, the most favored tenants in a commercial building or, at least, that no other tenant is or will be more favored. That is true whether they are prospective tenants wooed by a landlord to occupy long vacant space or space to be constructed or whether they are existing tenants whose leases are about to expire. As one Washington D.C. real estate broker reportedly explained, a most favored tenant is assured that an "agreed-upon deal will be improved upon or matched if another future tenant leases space at a

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1. President Bill Clinton, Press Conference at White House on U.S. Policy Toward China (May 26, 1994) (*available in* 1994 WL 209851).

better rate or discount than the first lead tenant."[2] To achieve that objective, a tenant with bargaining power may make what it regards as a simple request to have a "most favored nation" provision included in its lease.

Whatever may be the case with respect to commerce between nations or the impact on human rights, the request for favored nation treatment in a commercial lease poses a dilemma for the landlord. This is particularly true when the commercial real estate market is depressed and there is an abundance of competitive space available, as is currently the case in many communities.[3] If the landlord rejects a favored nation demand, he faces the loss of an existing or potential major tenant. Such losses can lead to his inability to rent up space for a period of time, and in consequence have insufficient rental income to fulfill his financial commitments. On the other hand, if he acquiesces in the demand, he may find that compliance with the lease of the favored tenant compels him to seek from subsequent tenants a rental rate and terms that are not obtainable in the prevailing economic climate; especially for space on lower floors, inferior quality space or areas required to meet the expansion needs of the major tenant. A difficult decision is also presented to the developer who has acquired a site, is under pressure to go ahead with the project, and requires signed leases for a specified amount of space in order to comply with the requirements for the funding of a mortgage needed to finance the development.[4]

"Favored nation" is beguilingly straight-forward and seemingly uncomplicated in concept, but, as will be shown, can be quite diffi-

2. Miles Maguire, *Ranking Land Use on Payoff To City*, THE WASHINGTON TIMES, Oct. 5, 1990, at D2. The broker noted that "[t]his approach 'may be difficult for lenders to accept, particularly in light of today's financial market. Yet to motivate a tenant leasing a large block of space, this approach can offer peace of mind in an otherwise unstable economy.' " *Id.*

3. In the prime midtown Manhattan (New York City) area, there are almost 26,000,000 square feet of office space available, and over 21,000,000 square feet in the downtown area. *See* EDWARD S. GORDON, CO., GORDON OFFICE MARKET REPORT NEW YORK (Winter 1995) at 2, 6; *see also* Andrea Adelson, *A Los Angeles Tenant for I.B.M.'s Extra Space*, N.Y. TIMES, July 19, 1995, at D19 (reporting 24% vacancy rate in Los Angeles, 19% vacancy rate in Chicago, and 33.9% vacancy rate in Dallas). The 1995 Real Estate Market Report published by Arnheim and Neely reports a vacancy rate in Pittsburgh of 5,700,000 square feet, 32,900,000 square feet in Houston, 12,000,000 square feet in Philadelphia and 24,200,000 square feet in the District of Columbia.

4. *See* Maguire, *supra* note 2, at D2 (reporting recommendations by brokers "that developers offer a 'favored nation clause' in leases as a way of closing a deal in the currently uncertain market").

cult in application and may have disastrous consequences.[5] Part I of this Article gives a brief outline of the more obvious concerns posed by the introduction of a favored nation concept in a commercial lease. Part II discusses cases involving favored nation clauses in various types of commercial contracts and illustrates the difficulty courts have had in assessing whether one contract is, in fact, more favorable than another. Part III introduces the reader to the trilogy of cases in Pittsburgh's Golden Triangle starting with the Pittsburgh Steelers and Pittsburgh Pirates litigation with the Pittsburgh Stadium Authority. This litigation gives focus to the problems posed by a favored nation clause in commercial leasing. The remainder of Part III outlines important questions those cases determined or left unresolved. Part IV analyzes in detail the first known commercial lease case involving a favored nation claim tried to a conclusion and examines how, and to what extent, fact intensive analyses and expert testimony were required by both sides to the dispute, and sets forth the trial judge's reasoning in concluding that disfavor did not exist. Part V concludes that the current state of the law makes it difficult to predict, with any degree of certainty, the outcome of a dispute concerning a commercial lease's favored nation clause. Part V then sets forth a list of considerations a clause draftsman should consider to avoid the unexpected as well as the complications of concealing more favorable terms in later leases from a favored nation beneficiary.

I. Economic Dilemmas a Most Favored Nation Clause Can Cause in a Commercial Lease

The favored nation principle has a long history in international relations, where it has a fairly broad but clearly defined scope. The only definition of "most favored nation" contained in Black's Law Dictionary identifies it as:

> A clause found in most treaties providing that the citizens or subjects of the contracting nations may enjoy the privileges accorded by either party to those of the most favored nations. The general design of such clauses is to establish the principle of equality of international treatment. The test of whether this principle is violated by the concession of advantages to a particular nation is not the form in which such concession is made, but the condition on which it is granted; whether it is given for a

5. *See* discussion *infra* parts I, II.

> price, or whether this price is in the nature of a substantial equivalent, and not of a mere evasion.[6]

In every area that the concept of equal or preferred treatment has been applied in commercial contractual relations,[7] it has spawned costly, multi-million dollar disputes, with unpredictable and unwitting results.

In the area of commercial real estate leases there have been only a limited number of publicized disputes, each of which is discussed in detail below. These disputes graphically illustrate that unless drafted with meticulous care, foresight, and specificity, a favored nation provision can result in consequences both drastic and unanticipated for everyone involved. If the clause is unqualified or inadequately limited, the landlord has the problem of disposing of any space, however small, poorly situated (and every office building has such space), or on lower floors at a rent at least as high and on terms at least equal to those contained in the favored nation lease of the major tenant. Another harsh result is that the landlord is prevented from renting space for which the favored nation or other large tenant has an option to acquire for its expansion at a later date. Such space has diminished economic value and will appeal only to a prospective tenant who is willing to accept a short term lease, without knowing whether the option will be exercised, in which event he must vacate. Another inequitable result that can be reasonably contemplated is the possibility that a lower rent differential enjoyed by a tenant of a small unit can be applied, not to a like amount of space occupied by the larger most favored tenant, but to the latter's entire area. The lower differential may be applied retroactively without regard to the myriad other provisions contained in a modern office lease and may continue to the end of the major tenant's term.

For the owner/mortgagor, the most favored nation provision can be the difference between success and foreclosure, and when a lender has insisted on absolute and unconditional personal guaran-

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6. BLACK'S LAW DICTIONARY 1013 (6th ed. 1990).

7. "In a survey of corporate general counsels, Russell Weintraub found that provisions to protect against price changes were commonly used in long-term contracts. Other provisions used were price indexing (71.6% firms used), cancellation options (66.2%), force majeure clauses (40.5%), renegotiation clauses (41.9%), and other types of provisions, mostly 'most favored nation' clauses." Mark P. Gergen, *The Use of Open Terms in Contract*, 92 COLUM. L. REV. 997, 1046 n. 144 (1992) (citing Russell J. Weintraub, *A Survey of Contract Practice and Policy*, 1992 WIS. L. REV. 1, 17 (1992)).

tees of all or part of the mortgage indebtedness by the developer or his investors, it can mean economic ruin.[8]

The mortgagee/lender can likewise be economically disadvantaged when its loan goes into default and becomes converted into ownership of property that produces no positive cash flow or an amount insufficient to cover capital improvements and operating expenses, with little or no interest on the loan, and having a residual value that is less than the loan, even without taking into account the defaulted interest.[9] A non-recourse loan, defined as a " 'type of security loan which bars the lender from action against the borrower if the security value falls below the amount required to repay the loan,' "[10] poses a particular risk to the lender where a favored nation clause is contained (i) in a lease that is superior to

8. *See, e.g., Another Citicorp Client In Dire Straits*, ATLANTA JOURNAL AND CONSTITUTION, Mar. 8, 1991, at D2 (reporting that Daniel M. Galbreath, a principal of the eighth largest U.S. developer was "struggling to stave off bankruptcy by negotiating with his lenders to restructure debts, some of which he personally guaranteed"); Richard D. Hylton, *A Real Estate Fortune Dissolves*, N.Y. TIMES, Mar. 6, 1991, at D1 (reporting on the "severity of this real estate recession and how developers who were once lauded for their conservative financings and careful gambles," including developers such as Galbreath, "are being swamped along with the highfliers"); Jill Dutt, *Bankruptcy Kalikow Style*, NEWSDAY, (Nassau and Suffolk ed.), Aug. 30, 1992, at 76 (reporting that developer Peter Kalikow's personal bankruptcy filing resulted, in part, from "his penchant for issuing personal guarantees" and, with regard to developers generally, that "[a]ll of them, including Kalikow, made one mistake: they believed their own net worth statements and borrowed more money than they could afford to repay. They forgot that real estate development is highly cyclical and risky"); Peter Grant, *Judgments Squeezing Cohen*, CRAIN'S N.Y. BUSINESS, Dec. 2, 1991, at 1 (reporting guarantees by Arthur G. Cohen and his partners of millions of dollars in loans and that "many of these personal guarantees were structured with 'joint and several' liability, meaning that if Mr. Cohen were unable to pay his share, lenders could go after his partners"). Where the defaulting borrower is a partnership, economic ruin may also follow the individual partners in the absence of a non-recourse provision in a mortgage. *See* 182 Franklin Street Holding Corp. v. Franklin Pierrepont Associates, 630 N.Y.S.2d 64 (N.Y. App. Div. 1995).

9. *See* 1 MILTON R. FRIEDMAN, FRIEDMAN ON LEASES § 5.7 (1990) ("[F]avored nations" clauses are "disliked by mortgage lenders who rely on leases as security for substantial mortgage loans."); *See* Kenneth M. Block and Jeffrey B. Steiner, *Assignment of Rents, Prepayment Plan May Impair a Mortgagee's Security Interest*, N.Y.L.J., Sept. 20, 1995, at 5 ("In a typical commercial mortgage transaction, the mortgagor provides an assignment of rents to the lender, granting the lender a security interest in rents paid by tenant of the mortgaged premises."). Virtually every commercial mortgage contains an "assignment of rents" provision which is triggered by the default of the mortgagor. Those "assignment of rent" clauses are hotly contested in bankruptcy because of the benefits conveyed on the lender. *See In re* Northport Marina Assocs., 136 B.R. 911 (Bankr. E.D.N.Y. 1992); *In re* SeSIDE Co., 152 B.R. 878 (Bankr. E.D. Pa. 1993).

10. Delphi Industries Inc. v. Stroh Brewery Co., 945 F.2d 215, 218 (7th Cir. 1991) (quoting BLACK'S LAW DICTIONARY 953 (1979)).

the mortgage, or (ii) in a lease that is inferior to the mortgage and which the lender has agreed will not be disturbed. In these instances, the value on foreclosure and the ability to lease up vacant premises will be negatively impacted.

These disadvantages to the landlord and mortgagee do not necessarily translate into a reverse measurement of benefits for the favored tenant. For the latter, the gains may be more illusory than real because after engaging in extensive and expensive litigation it may find that the degree of disfavor is so insignificant as to be *de minimis*, thereby barring any recovery at all.

II. When "Favored Nation" Has Been Applied to Commercial Transactions

The commercial application of the "favored nation" concept historically has been more frequent in the field of patents than in other areas and even there it has been recognized to be "often difficult to apply in practice."[11] Protracted and costly disputes have been generated by the asserted rights to equal treatment regarding patent licenses,[12] sales contracts,[13] labor contracts,[14] oil and gas/

11. STEVEN Z. SZCZEPANSKI, ECKSTROM'S LICENSING IN FOREIGN AND DOMESTIC OPERATIONS § 3.06(1) (1987).

12. *See, e.g.*, Studiengesellschaft Kohle m.b.H. v. Novamont Corp., 704 F.2d 48 (2d Cir. 1983), *cert. denied*, 464 U.S. 939 (1983); Shatterproof Glass Corp. v. Libbey-Owens-Ford Co., 482 F.2d 317 (6th Cir. 1973), *cert. denied*, 415 U.S. 918 (1974); Plastic Contact Lens Co. v. Frontier of the Northeast, Inc., 441 F.2d 67 (2d Cir. 1971), *cert. denied*, 404 U.S. 881 (1971); Prestole Corp. v. Tinnerman Prods., Inc., 271 F.2d 146 (6th Cir. 1959), *cert. denied*, 361 U.S. 964 (1960); Carpenter Technology Corp. v. Armco, Inc., 800 F. Supp. 215 (E.D. Pa. 1992), *aff'd*, 993 F.2d 876 (3d Cir. 1993); Searle Analytic, Inc. v. Ohio-Nuclear, Inc., 398 F. Supp. 229 (N.D. Ill. 1975); Dwight & Lloyd Sintering Co. v. American Ore Reclamation Co., 44 F. Supp. 401 (S.D.N.Y. 1941).

13. *See, e.g., In re* Remington Rand Corp., 836 F.2d 825 (3d Cir. 1988); Kaiser Aluminum & Chem. Corp. v. United States, 287 F.2d 890 (Ct. Cl. 1961); Zurn Constructors, Inc. v. B.F. Goodrich Co., 746 F. Supp. 1051 (D. Kan. 1990); Chemplex Co. v. Tauber Oil Co., 309 F. Supp. 904 (S.D. Iowa 1970); *In re* Ethyl Corp., 101 F.T.C. 425 (1983), *vacated sub nom.* E.I. Dupont De Nemours & Co. v. FTC, 729 F.2d 128 (2d Cir. 1984); *see generally* Donald S. Clark, *Price-Fixing Without Collusion: An Antitrust Analysis of Facilitating Practices After Ethyl Corp.*, 1983 WIS. L. REV. 887, 932-934 (discussing use and effect of most favored nation clauses in sales contracts).

14. *See, e.g.*, Chicago Tribune Co. v. NLRB, 965 F.2d 244 (7th Cir. 1992); Local 1199, Drug, Hospital & Health Care Employees Union v. Brooks Drug Co., 956 F.2d 22 (2d Cir. 1992); Chicago Typographical Union No. 16 v. Chicago Sun-Times, Inc., 860 F.2d 1420 (7th Cir. 1988); H.C. Lawton, Jr., Inc. v. Truck Drivers, Chauffeurs and Helpers Local Union No. 384, 755 F.2d 324 (3d Cir. 1985); Associated Milk Dealers, Inc. v. Milk Drivers Union, Local 753, 422 F.2d 546 (7th Cir. 1970); Central States, Southeast & Southwest Areas Pension Fund v. Reebie Storage & Moving Co., 815 F. Supp. 1131 (N.D. Ill. 1993).

utility contracts,[15] real estate conveyances,[16] and common area maintenance charges in shopping center leases.[17] Favored nation clauses have been included in profit participation agreements[18] and consent decrees resolving antitrust actions.[19] They have also formed the basis for antitrust complaints.[20] Examination of the "favored nation" clauses in these contractual arrangements demonstrates the difficulty courts have had in determining whether one contract is more favorable than another. In particular, as the following cases illustrate, difficulties arise in (i) determining which factors to compare and (ii) assessing the value of specific factors.

In *Shatterproof Glass Corp. v. Libbey-Owens-Ford Co.*,[21] the defendant, Libbey-Owens-Ford Co. (LOF), licensed its patent to Shatterproof under an agreement that contained the following "favored nation" provision:

> LIBBEY-OWENS-FORD agrees that if any license heretofore or hereafter granted by it under any one or more claims of the licensed patents contains any more favorable terms or rates of royalty than granted to LICENSEE hereunder, then LICEN-

15. *See, e.g.*, Texas Gas Transmission Corp. v. Shell Oil Co., 363 U.S. 263 (1960); Pure Oil Co. v. Federal Power Comm'n, 299 F.2d 370 (7th Cir. 1962); Louisiana-Nevada Transit Co. v. Woods, 393 F. Supp. 177 (W.D. Ark. 1975); Hall v. Arkansas Louisiana Gas Co., 379 So. 2d 1142 (La. Ct. App. 1980), *vacated on other grounds*, 453 U.S. 917 (1981); Hall v. Arkansas-Louisiana Gas Co., 359 So. 2d 255 (La. Ct. App. 1978), *cert. denied*, 444 U.S. 878 (1979); Eveleth Taconite Co. v. Minnesota Power & Light Co., 221 N.W.2d 157 (Minn. 1974).

16. *See, e.g.*, Dodek v. CF 16 Corp., 537 A.2d 1086 (D.C. 1988); 1726 Cherry St. Partnership v. Bell Atl. Properties, Inc., 653 A.2d 663 (Pa. Super. Ct. 1995), *appeal denied*, 664 A.2d 976 (Pa. 1995).

17. *See, e.g.*, Enterprise-Laredo Assocs. v. Hachar's, Inc., 839 S.W.2d 822 (Tex. Ct. App. 1992), *application for writ of error denied*, 843 S.W.2d 476 (Tex. 1992).

18. *See* Jay S. Kenoff & Richard K. Rosenberg, *Calculating Distribution, Interest Expenses; Multiple Participations*, N.Y.L.J., Aug. 9, 1991, at 5 (cautioning that favored nation clauses in profit participation agreements should be used advisedly or not at all).

19. *See, e.g.*, American Soc'y of Composers, Authors and Publishers v. Showtime/The Movie Channel, 912 F.2d 563 (2d Cir. 1990); Fisher Bros. v. Phelps Dodge Indus., Inc., 614 F. Supp. 377 (E.D. Pa. 1985), *aff'd mem.* 791 F.2d 917 (3d Cir. 1986); *In re* Ampicillin Antitrust Litigation, 82 F.R.D. 652 (D.D.C. 1979); *In re* Chicken Antitrust Litigation, 560 F. Supp. 943 (N.D. Ga. 1979), *aff'd*, 669 F.2d 228 (5th Cir. 1982)(favored nation clause struck from settlement agreement); *see also* FEDERAL JUDICIAL CENTER, MANUAL FOR COMPLEX LITIGATION, THIRD, § 23.23 (1995).

20. *See, e.g.*, Ocean State Physicians Health Plan, Inc. v. Blue Cross & Blue Shield, 883 F.2d 1101 (1st Cir. 1989), *cert. denied*, 494 U.S. 1027 (1990); Associated Milk Dealers, Inc. v. Milk Drivers Union, Local 753, 422 F.2d 546, 552 (7th Cir. 1970); *see also* Department of Justice, Antitrust Div., Proposed Final Judgment and Competitive Impact Statement in United States v. Vision Serv. Plan, Case No. 1:49 CV 02693 (D.D.C.), 60 Fed. Reg. 5210 (1995).

21. 482 F.2d 317 (6th Cir. 1973), *cert. denied*, 415 U.S. 918 (1974).

> SEE shall thereupon have the benefit of such more favorable terms or rates for the same claim or claims, but under no other claims of any of the licensed patents.[22]

This language must have seemed clear to the participants when it was drafted. Subsequently, however, LOF licensed the same patent to the Ford Motor Company, and Shatterproof contended that the Ford license was at "more favorable terms or rates of royalty" because the rate (i.e., cents per square foot of product) required to be paid by Shatterproof exceeded that payable by Ford.[23] Shatterproof ignored the fact that Ford received its preferential royalty as consideration for both its grant to LOF of a cross-license to use certain Ford patents, as well as payment for a release of all claims for prior infringement by Ford of LOF's patents.[24]

The United States Court of Appeals for the Sixth Circuit concluded that, in evaluating "more favorable terms or rates of royalty," it could not merely compare the royalty rate per square foot, but instead had to consider "the full consideration paid by each licensee."[25] The court determined that the definition of "royalty" necessarily included the full "cost, consideration, compensation, or price paid or incurred for a license, [and that] the specified rate should not be the sole criterion by which to determine what was in fact the price paid for the license."[26]

In *Kaiser Aluminum & Chemical Corp. v. United States*,[27] Kaiser bought a manufacturing plant from the government pursuant to a letter agreement in which the government committed that it would "not offer the same type of plants to Reynolds Metals or others on a more favorable basis."[28] Kaiser claimed that a more favorable contract was subsequently made with Reynolds and that it was entitled to compensatory damages.

Recognizing that the conditions of each plant were different, the United States Court of Claims reasoned that:

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22. *Id.* at 318.

23. *Id.* at 319-20.

24. *Id.* at 323-24.

25. *Id.* at 324.

26. 482 F.2d at 323. The fact that the consideration given by Ford and Shatterproof was different was held not to be determinative. The issue was "whether one was more favorable than the other," and that required "a comparison of the value of the consideration given in each instance," with a value assigned to each element of consideration given by Ford. *Id.* at 324.

27. 287 F.2d 890 (Ct. Cl. 1961).

28. *Id.* at 891.

> the only practical way to determine whether one purchaser was treated more favorably than the other is to match terms in so far as they are comparable, to analyze the advantages and disadvantages in the two contracts, and upon this analysis to determine whether an adjustment should be made pursuant to the terms of the letter.[29]

Kaiser complained of five items which the court evaluated "as to whether, viewing each item on an overall basis, Kaiser was discriminated against."[30] The court stated, "[w]hat is decisive in this case is not whether as to certain particulars these two purchasers were treated differently but whether viewing these particulars together Kaiser was treated unfairly in comparison with Reynolds."[31]

The court concluded that, except for a more beneficial effective sale date having been given to Reynolds, the other four items complained of by Kaiser when viewed on an "over-all basis" led it to hold that "the Reynolds 'deal' was nearly equivalent to the Kaiser 'deal'," and did not disfavor Kaiser.[32]

In *H.C. Lawton, Jr., Inc. v. Truck Drivers, Chauffeurs and Helpers Local Union No. 384*,[33] the United States Court of Appeals for the Third Circuit referred to arbitration a dispute involving a labor contract containing a favored nation provision and the issue of its violation by granting a better term in a contract with another union which required the interpretation of the meaning of "better terms and conditions."[34] The court observed the "difficult[y]" of interpreting the phrase arises from the fact that it is unclear whether it "refer[s] to the contract as a whole, or . . . require[s] that each individual term and provision be identical?"[35]

In *Eveleth Taconite Co. v. Minnesota Power & Light Co.*,[36] the Minnesota Supreme Court held that the duration of a contract was

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29. *Id.*

30. *Id.* at 892. Kaiser complained that it was disadvantaged because (1) it had to install a fume control system at its own cost while Reynolds received a fume control system at 39.39 percent of its cost, (2) it had to make expenditures to deal with a carbon-electrode deficiency, (3) its acquisition costs were higher than Reynolds', (4) it paid more interest on its purchase of plants than Reynolds, and (5) the government used the same effective sale date in the purchases of the plants, resulting in Reynolds receiving a higher amount in rental forgiveness than Kaiser. *Id.* at 892-95.

31. 287 F.2d at 894.

32. *Id.* at 895. As to the advantage obtained by backdating the sale to Reynolds to coincide with the Kaiser sale date and forgiving of rent, the court found that Reynolds had received an advantage in the amount of $583,549. *Id.* at 896.

33. 755 F.2d 324 (3d Cir. 1985).

34. *Id.* at 330.

35. *Id.*

36. 221 N.W.2d 157 (Minn. 1974).

not included within the meaning of "more favorable terms and conditions,"[37] after observing that the court "never had occasion to interpret a so-called most-favored-nations clause" and that "the parties have not called to our attention, a case in any jurisdiction interpreting the clause on an issue similar to the one in this case."[38]

III. "Favored Nation" Provides Fertile Ground for Confusion and Conflict When Used in Commercial Real Estate Leases

A "favored nation" clause in a commercial real estate lease not only has the problems associated with its use generally — what is being compared and how do you calculate whether a party is disfavored — but also has the problems derived from a long-term complex agreement that contains numerous monetary and non-monetary provisions over lengthy time periods. This characteristic of commercial leases makes judicial comparison between existing and future leases difficult to predict and the outcome of the litigation arising out of favored nation clauses uncertain.[39]

A. The Lesson From the Pittsburgh Experience

In the 1990 edition of his treatise on commercial leasing, Professor Milton Friedman introduced for the first time a "most favored nation" chapter, observing that "the only case found that involved a most favored nation clause in a real estate lease is one in the Pennsylvania Common Pleas Court," *National Intergroup, Inc. v. Oliver Tyrone Corporation.*[40]

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37. *Id.* at 162.

38. *Id.* at 160.

39. The protection afforded beneficiaries of favored nation clauses in sales agreements is somewhat analogous to the protection afforded by the Robinson Patman Act, 15 U.S.C. § 13 *et seq.* Sales agreements affect specified goods or services. The customers protected by Robinson Patman compete functionally and geographically in goods of like grade and quality sold at or about the same time, after factoring in cost of delivery and other stated offsets. In such situations, the determination of discrimination is to be made on the basis of known or ascertainable factors, unlike commercial real estate leases which can differ from one to another in numerous respects: term, renewal option, expansion option, basic rent, operating and tax escalation, size and location of demised premises, improvements, etc.

40. No. 87-19306 (C.P. Allegheny County, Pa., May 19, 1989); 1 FRIEDMAN, *supra* note 9, § 5.7. "There the judge and several local real estate witnesses were surprised at the existence of the clause. The clause was deemed enforceable but enforcement was denied for lack of proof." *Id.* "In the court system in Pennsylvania, the Court of Common Pleas is the court in which all civil and criminal actions are begun (except such as are brought before courts of inferior jurisdiction)." BLACK'S LAW DICTIONARY 356 (6th ed. 1990).

In fact, at the time of publication, favored nation disputes sufficient to send chills up the spines of lease draftsmen had arisen in Pittsburgh's Golden Triangle both before and after *National Intergroup*. These disputes arose in *Pittsburgh Steelers Sports, Inc. v. Stadium Authority of Pittsburgh*,[41] and *Federated Investors, Inc. v. Liberty Center Venture*.[42] They involved, respectively, the Steelers' and Pirates' attempt to terminate their leases of Three Rivers Stadium and/or secure damages for alleged breaches by the Stadium Authority, and the claim of the nation's seventh largest mutual fund for the alleged breach of its long term commercial office lease.

The Pittsburgh Steelers and the Pittsburgh Pirates played their home games at Three Rivers Stadium under an agreement that contained the following favored nation provision:[43]

> 6.03. The [Pittsburgh Stadium] Authority further agrees that it shall not enter into any leases or licenses or grant any other occupancy rights on a continuing basis to any entity, firm or person, at rentals, license fees and other charges which shall be materially more favorable to such lessee, licensee or occupant than the rentals and other charges payable by the [Pirates] Athletic Company and [Steelers] Football Club under the Stadium Agreements.[44]

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41. No. GD 84-1517 (C.P. Allegheny County, Pa.).

42. No. GD 91-16178 (C.P. Allegheny County, Pa., Sept. 30, 1991) (confirming arbitration award by American Arbitration Ass'n, Docket No. 55-183-0072-90).

43. Favored nation clauses have been included in other stadium and arena leases to professional sports teams in cities where multiple teams occupy the same or adjacent facilities. *See, e.g.*, Ken Stephens, *North Stars' Move Had Many Turns; Step by Step Deal-Makers Beat Hurdles*, THE DALLAS MORNING NEWS, Mar. 11, 1993, at 1B (Mavericks' [basketball] lease of Reunion Arena with city of Dallas contains most favored nation clause guaranteeing team terms at least as favorable as those given to Stars [hockey]); *Mariners, Seahawks Concerned Over Sonics Arena Contract*, UPI, June 29, 1990, *available in* LEXIS, Nexis Library, UPI File (Supersonics [basketball] lease at Ackerley arena contains most favored nation clause guaranteeing Sonics same financial benefits that city of Seattle gives to Mariners [baseball] and Seahawks [football] at Kingdome); Colin Flaherty, *Chargers Demanding New Deal*, SAN DIEGO BUS. J., June 27, 1988 at 1 (most favored nation clause in Chargers [football] lease of San Diego's Jack Murphy Stadium which is also leased to Padres [baseball]). The disputes generated by such favored nation clauses have been resolved without litigation. *See, e.g.*, Steve Richardson, *The Big Chill; Arena Mates, Mavericks, Stars Can't Get Along*, THE DALLAS MORNING NEWS, Oct. 3, 1993, at 1B; Leonard Bernstein, *City Gives Chargers Bigger Stadium Cut*, LOS ANGELES TIMES, San Diego County Ed. July 12, 1988, Part 2, at 2.

44. Settlement Agreement dated January 1, 1982, § 6.03, Exhibit F, Pittsburgh Steelers Sports, Inc. v. Stadium Auth. of Pittsburgh, No. GD 84-1517 (C.P. Allegheny County, Pa.). The Settlement Agreement was executed as part of a settlement of a 1981 lawsuit filed by the Pirates against the Stadium Authority, and amended the Basic Agreement, Management Lease, Baseball Lease and Football Lease.

Federated Investors' favored nation clause in its 1984 office space lease for more than 200,000 square feet of the office tower of Pittsburgh's Liberty Center provided:

> 39.1 *More Favorable Leases.* If, any time during the Initial Term (a) Landlord enters into a lease (the "More Favorable Lease") with a lessee other than Tenant or an affiliate of Tenant (the "Third Party Lessee") upon terms and conditions which are in the aggregate more favorable to such Third Party Lessee than those received by Tenant under this Lease and all related agreements and (b)(i) entering into such More Favorable Lease causes an aggregate of more than 50,000 square feet of office space in the Building to be leased under more Favorable Leases or (ii) an aggregate of 50,000 square feet of office space in the Building is then subject to More Favorable Leases; the Landlord shall offer to amend this Lease so that the terms and conditions of the Lease as amended are as favorable to a tenant as those of the More Favorable Lease. In no event however shall the terms and conditions of this Lease be modified pursuant to this Section 39.1 to change the length of the Term, change the amount of Square Feet leased or permit Tenant to relocate its Premises. In determining whether a lease to a Third Party Lessee is a more Favorable Lease all of the terms, conditions, inducements and agreements relating to this Lease and to the lease to the Third Party Lessee, respectively, shall be considered. Such terms, conditions and inducements shall include without limitation rent, term, expansion options, renewal options, location of the Leased Premises within the Building, tenant improvement allowances, and tenant improvements provided by Landlord.
>
> 39.2 *Effective Date of Amendments.* In the event that the Lease is amended pursuant to this Section, such amendments shall become effective from and after the effective date of the More Favorable Lease.
>
> 39.3 *Tenant's Right to Review.* Tenant shall have the right to review any leases entered into by Landlord for space in the Office Area. Landlord shall deliver to Tenant all such leases within five (5) days of their execution. Tenant shall keep confidential the terms and conditions of all such leases.[45]

In *National Intergroup*, the favored nation clause was contained in a side letter to the National Steel Company lease at One Riverfront Center and provided:

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45. Lease between Federated Investors, Inc. and Grant Liberty Development Group Associates dated November 30, 1984, § 39 annexed to Petition to Confirm Arbitrators' Award, Exhibit A, Federated Investors, Inc. v. Liberty Ctr. Venture, No. GD 91-16178 (C.P. Allegheny County, Pa.).

> If landlord at any one or more times agrees with any other tenant[s]. . . to grant such tenant[s] any more favorable terms and conditions than those contained in [tenant's] lease from landlord, including without limitation the terms and conditions relating to rent or to absorption of costs for tenant's work, landlord will offer to [tenant] such more favorable terms and conditions then [sic] those contained in the [tenant's] lease.[46]

Each clause generated heavily litigated or arbitrated disputes involving millions of dollars. Costs were compounded by the fact that in the two commercial office buildings, the disputes hindered the landlords' ability to lease up vacant space because of uncertainty as to the terms in new leases to which they could agree and how they were going to pay debt service and avoid foreclosure if the challenging tenants were successful. The landlords had to suffer uncertainty for several years and engage in costly litigation despite their characterization of their allegedly disfavored tenant's interpretation that (i) a high rise multi-floor office tenant was comparable to a first floor building convenience cafeteria and that (ii) in comparing lease terms only similar provisions should be compared and then, only in overlapping years, as "absurd", "makes no sense" and could not possibly have been within the contemplation of the parties.

The *National Intergroup* dispute was actually two disputes: one by National and the other by its attorneys who were also tenants in the same building and who also had the same favored nation provision. Both cases were consolidated and were adjudicated at Common Pleas as a "complex" case where, after trial, the court rejected entirely the tenants' favored nation interpretation.[47] *Pittsburgh Steelers Sports, Inc.* was resolved by settlement after lengthy litigation.[48] *Federated Investors* was contested in arbitration and resolved by an award in favor of the tenant and against the landlord

46. Letter from Richard K. Means to George B. Angevine dated July 14, 1981, annexed to Complaint in Equity, Exhibit B, National Intergroup, Inc. v. Oliver Tyrone Corp., No. GD 87-19306 (C.P. Allegheny County, Pa.)

47. *See National Intergroup, Inc.*, GD No. 87-19306 (C.P. Allegheny County, Pa.)

48. The 1988 settlement in the Steelers' lawsuit (in which the Pirates intervened) in turn generated a second round of litigation by the Pirates Baseball Club (in which the Steelers intervened). *See* Pittsburgh Baseball Inc. v. Stadium Auth. of Pittsburgh, 630 A.2d 505 (Pa. Commw. Ct. 1993); Pittsburgh Baseball Inc. v. Stadium Auth. of Pittsburgh, 618 A.2d 1248 (Pa. Commw. Ct. 1992). The Pirates sued the Stadium Authority for failing to convey favored nation benefits based upon the Steelers earlier settlement, i.e., that the Authority's failure to grant revisions to the Pirates "economically comparable to those being given to the Steelers . . ." was violative of the Pirates favored nation rights. Second Amended Complaint, ¶ 58, Pittsburgh Baseball Inc. v. Stadium Auth. of Pittsburgh, No. GD 92-01392 (C.P. Allegheny County, Pa.).

for a rent abatement equal to $6 million and $1.7 million for past rent and overcharges.[49] The award was confirmed, judgment was entered thereon, and no appeal taken.[50]

Thus, there is no appellate guidance available to permit a landlord, tenant, borrower, lender, or bankrupt estate to chart a course with any reasonable certainty of result.[51] Indeed, until *National In-*

49. The award was calculated at $4 per square foot multiplied by the tenant's total leasehold estate of 206,000 square feet and provided for a rent reduction from 1989 through 1996. Federated was the only tenant in the office tower when it opened in 1986. There was no other tenant until 1988. After Federated demanded arbitration the landlord began making mortgage payments to its lender, Metropolitan Life Insurance Company, at an interest rate of 10% instead of the 14.5% as provided for in the mortgage note, which Metropolitan Life refused to accept. In March 1991, shortly before the adverse arbitration award, Metropolitan Life instituted a foreclosure action which ultimately resulted in the appointment of a receiver. *See* Metropolitan Life Ins. Co. v. Liberty Ctr. Venture, 650 A.2d 887 (Pa. Super. Ct. 1994). In 1990, partners in the joint venture landlord sued Metropolitan Life (which was both a lender and a 60% partner in the landlord) in the United States District Court for the Western District of Pennsylvania, for breach of fiduciary obligations (which included the claim that Metropolitan Life required rentals in the building to be higher than market — which Metropolitan Life justified, in part, by adverting to Federated's favored nation clause) and, later, for failure to refinance the mortgage loan. *See* Complaint, Grant Liberty Dev. Group Assocs. v. Metropolitan Life Ins. Co., Docket No. 90-1424 (W.D. Pa.).

All litigation was resolved in May 1995 when the office building in which Federated held its long term lease was sold to new investors at a $9 million loss from the original $67 million construction price. *See* Keri Conley, *After a 5-year Court Battle, Liberty Center Gets Liberty*, PITT. BUS. TIMES & J., May 15, 1995, at 17 (quoting the building leasing agent: "The property isn't worth those larger dollars because rents haven't been as fruitful as they anticipated . . . . When they built it in the 1980s, they were projecting rents in the $30 (per square foot) range. Today rents are in the low $20s.").

By April 1990, when Federated demanded arbitration, Metropolitan Life was no stranger to favored nation litigation having been sued by a law firm tenant in Houston for breach of a favored nation clause in a long term lease and for damages under the Texas Deceptive Trade Practices Act (Tex. Bus. & Com. Code Ann. § 17.505 [Vernon 1987]). *See* Butler & Binion v. Block 144 Joint Venture, Docket No. 89-23348 (281st District Court, Houston, Texas). A six-figure settlement was agreed to before trial and after mandamus and other relief was denied to the landlord. Telephone interview with Louis B. Paine, Jr. (managing partner at Butler & Binion) (Aug. 10, 1995); *see* Block 144 Joint Venture v. Lesher, 1990 Tex. App. LEXIS 44 (Tex. Civ. App. Jan. 11, 1990).

The Texas Deceptive Trade Practice Act under which the disfavored tenant demanded relief in *Butler & Binion* was held not to afford relief to the disfavored tenant in Enterprise-Laredo Assocs. v. Hachar's, Inc., 839 S.W.2d 822 (Texas Ct. App. 1992).

50. Federated Investors, Inc. v. Liberty Ctr. Venture, No. GD 91-16178 (C.P. Allegheny County, Pa., Sept. 30, 1991). The judgment was not satisfied of record until March 1995.

51. National's fully briefed appeal to the Superior Court from the adverse judgment on the favored nation issue was dismissed by that Court upon the landlord's motion based on the landlord's argument that by taking a benefit, i.e. executing in respect of a portion of the judgment favorable to them (tax escalation) the tenants had waived their right of appeal on the favored nation issue. National Intergroup, Inc.

tergroup, *Pittsburgh Steelers* and *Federated Investors*, no consideration appears to have been given by any court or by any arbitral tribunal to the impact of a favored nation provision on the bundle of rights and obligations long recognized as comprising a long term commercial office lease.[52]

Until *National Intergroup*, *Pittsburgh Steelers* and *Federated Investors* were litigated/arbitrated, no tribunal is known to have been asked to determine the following important "favored nation" questions:

1. Whether comparability of space and/or the nature of the tenants being compared is implicit in a favored nation analysis and what factual elements determine "comparability?"[53]

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v. Oliver Tyrone Corp., Nos. 1721, 1838, 1758 and 1865 PGH 1989 (Pa. Super. Ct. June 7, 1990) (reargument denied August 2, 1990); *accord* Annotation, *Right of Appeal From Judgment Or Decree As Affected By Acceptance of Benefit Thereunder*, 169 A.L.R. 985 (1941).

Review of the order of dismissal was granted by the Pennsylvania Supreme Court. National Intergroup, Inc. v. Oliver Tyrone Corp., 589 A.2d 692 (Pa. 1991). In its *per curiam* order dated February 26, 1991 the court "limited" its review "to the question whether two claims [tax escalation and favored nation] arising out of the same contract may be separated sufficiently so that one decision [favored nation] may be appealed even though estoppel has occurred as to the other [tax] claim."

The Stadium Authority's settlement of both the Steelers' and Pirates' claims, first in 1988, and then a second time in 1994, precluded adjudication of the merits of their disputes.

The only appellate court to address favored nation in the context of a commercial lease is the Supreme Court of Arizona which recently upheld a jury award in favor of a disfavored tenant without reviewing the evidence in the trial court or interpreting the clause. *See* Gust, Rosenfeld & Henderson v. Prudential Ins. Co., 898 P.2d 964 (Sup. Ct. Ariz. 1995). The Arizona court refused to apply the Arizona six year period of limitations to the disfavored tenant's claim based on alleged disfavor commencing 17 years before suit holding that the period of limitations did not commence until the favored nation beneficiary "knew or in the exercise of reasonable diligence should have known that it had been injured." *Id.* at 969.

52. *See* ELLIOTT L. BISKIND & CLARENCE S. BARASCH, LAW OF REAL ESTATE BROKERS, § 117.02 (1969) where the authors note that "[t]o determine whether or not there has been a meeting of minds in a lease transaction, a jury must find agreement on" such items as (1) term; (2) annual base rent; (3) additional rent; (4) obligations to pay operating and maintenance costs, all realty taxes, assessments, financing carrying charges, and increases in realty taxes above base year; (5) work letter; (6) building standards/above building standards; (7) renewal options/expansion options; and (8) alternative rentals/steps/lower rent in early years offset by higher rent in late years.

53. The tenants in *National Intergroup* (National Steel Company and its law firm) occupied the high rise portion of an office building in Pittsburgh's Golden Triangle. They argued that "the covenant [favored nation] would apply to [and would be triggered by] a small newsstand on the first floor, to a renewal lease, and, indeed, to any person or entity with whom the landlord entered into a subsequent lease agreement. To conclude that this language is to be restricted to agreements with comparable tenants and comparable tenancies flies directly in face of the unqualified phrase 'any other tenant[s].' " Joint Brief for Appellants (Nos. 1721 and 1728) dated Mar. 12,

2. To the extent there is any proven disfavor (however calculated), whether the favored nation beneficiary is entitled to relief based on the entire gross footage demised to it or only on a portion of that footage equal to footage demised to the allegedly favored tenant?[54]
3. Whether benefits having a calculable monetary value granted to favored nation beneficiaries (either before or af-

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1990, at 24, National Intergroup, Inc. v. Oliver Tyrone Corp., Nos. 1721, 1838, 1758, and 1865 PGH 1989 (Pa. Super. Ct.). The Steelers argued that they were disadvantaged by the difference between their rent and the rent paid by the fledgling Pittsburgh Maulers USFL football team which they viewed as a comparable occupant of the Stadium, and that the rent disparity should be made applicable to the Steelers' entire term of forty (40) years and not merely to the Maulers' four year term. Complaint, ¶ 20, Pittsburgh Steelers Sports, Inc. v. Stadium Auth. of Pittsburgh, No. GD 84-1517 (C.P. Allegheny County Pa.); *cf.* Ken Stephens, *supra* note 43, at 1B (Dallas Mavericks, in fifth year of 20-year lease, refused to agree to Stars' lease of Reunion Arena unless Mavericks lease was amended under most favored nation clause to 5-year term which was initial lease-term for Stars).

The Steelers also argued that the Maulers were favored by the fact that no bond service charges were imposed upon their tickets and that the Maulers were not required to play any pre-season games at Three Rivers Stadium, unlike the Steelers. The Stadium Authority asserted that the Steelers' lease favored the Steelers with the inclusion of lounge boxes and their advantageous parking provisions, advantageous provisions with regard to ground crew personnel and the maintenance of the Steelers office at Three Rivers Stadium. The Pirates, as intervenors, asserted disfavor in respect of the Maulers' (a) lease termination opportunity; (b) more liberal advertising; (c) right to audit the Stadium Authority's books; (d) rent reduction as per schedule to the Maulers' lease; (e) more favorable payment terms for game service charges; (f) certain rights in the determination of, and participation in, new facilities; (g) lesser insurance requirements; and (h) lesser minimum annual rents. Complaint, ¶ 20, *Pittsburgh Steelers Sports, Inc.*, (No. GD 84-1517).

54. The tenant in *Federated Investors* demanded and was awarded in arbitration a rent abatement for its entire premises of more than 200,000 square feet based on allegedly favored smaller tenants because the trigger mechanism in Federated's lease, 50,000 square feet, had been leased to more favored tenant[s] occupying office leases aggregating that amount. *See* Award of Arbitrators, annexed to Petition to Confirm Arbitrators' Award dated Sept. 12, 1991, Exhibit B, Federated Investors, Inc. v. Liberty Ctr. Ventures, No. GD 91-16178 (C.P. Allegheny County, Pa.). The award was based on the 50,000 square foot threshold having been crossed so as to permit a rent abatement with respect to Federated's entire space. The award did not answer how or to what extent relief would have been available if, for example, there had been three separate tenancies of 17,000 square feet each at different points in time with different lease terms ranging from the very favorable to the marginally favorable. Conceptually the two earlier leases might have been vastly superior to that of the favored nations beneficiary while the third lease, which carried past the 50,000 square foot threshold, was only marginally more favorable. Whether and how the three leases are required to be reduced to a common denominator for purposes of a favored nations analysis is an open question. Similarly unanswered is the effect of abandonment of the favored tenant's leasehold or disaffirmance of a lease by a favored tenant in bankruptcy on the favored nations beneficiary whose rights appear to be fixed by the mere execution of a more favorable lease and not by the favored tenant's continued possession of its leasehold interest under more favorable terms.

ter later assertedly favored tenancies) must also be valued as part of the favored nation analysis and, if so, how are they to be valued?[55]

4. Whether and what values are to be placed on such non-monetary lease provisions as renewal options, the value of which may increase or decrease depending on the real estate market,[56] options to relocate, options to expand, rights of first refusal, and the like, given to the favored nation beneficiary but not to the allegedly favored tenant who simply pays a lesser amount of money each month?[57]

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55. In *National Intergroup* the tenants predicated their allegedly disfavored position only on the overlapping years on a line item basis using only elements expressed in monetary terms, and only secondarily attempted to prove disfavor on an analysis of the lease as a whole. The Steelers, (and, later, the Pirates as intervenors) early in their litigation, had argued that "one can reasonably interpret the clause to mean that no other tenant will receive a more favorable position *on any item* concerning rentals, license charges or fees." Plaintiffs' Brief in Opposition to Preliminary Objections Filed by the Stadium Authority of the City of Pittsburgh at 24, *Pittsburgh Steelers Sports, Inc.*, (No. GD 84-1517). The Stadium Authority responded:

> After all, the Pirates have rights only if the 'rentals, license fees, and other charges' . . . [are] materially more favorable. The use of the word '*materially*' is evidence that the 'rentals, license fees and other charges' are to be compared in the aggregate.
>
> Moreover, for the parties to intend that the 'rentals, license fees, and other charges' not be compared in the aggregate would be for them to ignore the true economic nature of complex lease negotiations. Both sides in such negotiations keep a firm eye on the 'bottom line.' The landlord tries to determine how much revenue is going to come in and at what expense. The tenant tries to determine the total cost of its occupancy under the proposed lease.

Brief in Support of Preliminary Objections to Intervenor's Complaint, at 15, *Pittsburgh Steelers Sports, Inc.*, (GD 84-1517).

The line item analysis approach taken by the Steelers and the Pirates in *Pittsburgh Steelers Sports, Inc., supra*, was later disavowed by the Pirates in its suit against the Stadium Authority in Pittsburgh Baseball, Inc. v. Stadium Authority of Pittsburgh, No. GD 92-01392 (C.P. Allegheny County, Pa.). In seeking to avoid dismissal of its claimed right to equal treatment with the Steelers it responded to the City of Pittsburgh's position: "The City argues that Pittsburgh Associates make more use of the Stadium than do the Steelers and that it would be unreasonable for the Steelers and Pittsburgh Associates to have an equal economic relationship with the Stadium Authority. This statement completely misconstrues the nature of a most favored nations clause. As this court, Wekselman, J., has recently held, a comparison of leases for purposes of enforcing such a clause is not to be made on a line by line basis, but rather on the basis of the whole of each contract." Plaintiff's Brief in Opposition to Defendant's Preliminary Objections to Second Amended Complaint at 9, *Pittsburgh Baseball, Inc.*, (GD 92-01392) (citing *National Intergroup, Inc.* (GD 87-19306)).

56. *See* Dennis' Natural Mini-Meals, Inc. v. 91 Fifth Ave. Corp., 618 N.Y.S.2d 771 (N.Y. App. Div. 1994).

57. The *National Intergroup* tenants asserted that no non-monetary lease provision was relevant to a favored nation determination. Conversely, both the Steelers and the Pirates asserted that "favored nation" was violated by the lease with the Pitts-

IV. Favored Nation in Microcosm: The Anatomy of National Intergroup

National Intergroup is the only known instance of a trial court considering fact and expert testimony and valuing the elements of a commercial lease and all ancillary agreements on the totality of all the lease terms, and rejecting the concept that each discrete lease provision is treated separately for comparison purposes.[58] Applying that rationale, the *National Intergroup* court specifically recognized that the long term commercial lease is a package of rights and obligations and is to be treated in its entirety to determine favor or disfavor.[59] The result was a holding that a perceived discrepancy of more than $5 per square foot in "rent" was no discrepancy at all.[60]

The trial evidence established that the lease negotiations between the National Steel Company and its landlord for occupancy of the space in the building then in construction (and ultimately named for National Steel) extended over a period of almost six months in 1981, with the involvement of principals and technicians (architects, designers, engineers, etc.) on both sides and the active participation of their respective counsel.[61] Despite those extensive negotiations and preparation of multiple drafts and redrafts that went into the making of the lease, there was admittedly not a single memorandum, notation or internal note made by anyone relating to the subject of "favored nation."[62] On National's own version of what took place during the entire 6-month period, the subject of "favored nation" arose inconclusively at most twice at the very inception of discussions, lasting a total of no more than five minutes, without any attempt to define what was meant by the concept or its application.[63]

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burgh Maulers by virtue of a right of early termination granted to the Maulers. Complaint, ¶ 20, *Pittsburgh Steelers Sports, Inc.*, (GD 84-1517).

58. National Intergroup, Inc. v. Oliver Tyrone Corp., GD No. 87-19306 (C.P. Allegheny County, Pa.)

59. Transcript of Non Jury Verdict at 9, *National Intergroup, Inc.*, (No. 87-19306).

60. *Id.* at 18.

61. Joint Consolidated Reproduced Record at 500-502, National Intergroup, Inc. v. Oliver Tyrone Corp., Nos. 1721, 1838, 1758, and 1865 PGH 1989 (Pa. Super. Ct.) (References to the testimony at trial are to pages of the Trial Transcript included in the Joint Consolidated Reproduced Record on the Consolidated Appeals and Cross-Appeals to the Pennsylvania Superior Court).

62. *Id.* at 504.

63. *Id.* at 510-512. In early July 1981 the lease was completed and sent to National's General Counsel for execution. It was at that point that he instructed National's attorneys to prepare a most favored nation clause, which took about fifteen

A. The Purported Multi-Million Dollar Disfavoring of National

The tenants in *National Intergroup* demanded damages and rent abatements for their entire demised areas totalling more than 200,000 square feet based upon 940 square feet of retail space leased to a ground floor take-out restaurant and/or 45,000 square feet leased to the allegedly favored Federal Home Loan Bank (FHLB) of Pittsburgh.

1. The Upper Crust Lease

More extreme, perhaps, than the Steelers' and Pirates' claimed disfavor vis-a-vis the fledgling United States Football League's Maulers, National - a major steel company - and its law firm instituted and vigorously prosecuted, at great cost to them and the landlord, a complaint of favored nation violation based primarily on a subsequently made lease of 940 square feet located in the rear of the building's ground floor and overlooking the loading docks, trash receptacles and a parking lot, and used as a cafeteria for the convenience of the building tenants.

That lease to the Upper Crust Restaurant was for a term of five years commencing June 1, 1983 and ending May 31, 1988 with two five-year renewal options. By 1989, when the National litigation was tried, Upper Crust was already out of possession.

Predicated on the Upper Crust lease, there were two components of National's claim. The first component, a claim for $7,221,381 ($5,271,081 plus interest of $1,950,300), was based on a $30,000 construction allowance to Upper Crust which on a square foot basis allegedly exceeded the allowance granted to National.

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minutes to prepare; it was retyped and signed by the landlord on its letterhead. *Id.* at 1717-20.

No National witness was able to offer testimony of any discussion of a "favored nation concept" or how it would, or could, be applied. Whether "favored nation" would apply to "parking", inasmuch as at execution of the lease in 1981 parking had not been provided for (except for an agreement that National would have the right to sixty spaces upon proper notification), was admittedly not the subject of any discussion. Whether "favored nation" would apply only to the square footage originally leased to National, which was subsequently expanded, was never discussed. How "favored nation" would integrate with the renewal rental option which was keyed to "space comparable to the Premises and the condition thereof, situate in a building comparable to that in which the Premises are situated and located in the Golden Triangle area of the City of Pittsburgh . . .," was also not the subject of any testimony. There was no evidence of any discussion as to whether a slightly reduced rental per square foot given to an amenity such as a first floor newsstand would then be applicable to all of National's leased premises. National's leasing consultant admitted that he personally had never previously seen a favored nation provision in a commercial lease. *Id.* at 689.

The space, however, was leased raw to Upper Crust, with no floor, ceiling, finished walls or utilities, and the allowance was towards the tenant's cost to improve the area so that it would be usable and up to building standard. In stark contrast, the area demised to National was improved by the landlord at its cost from the raw state to building standard level and the additional construction allowance granted, was to enable National to elevate the quality of its premises above building standard, at a cost many times greater than the allowance to Upper Crust.

The second component, a claim for $6,264,139 ($5,037,380 plus interest of $1,226,759), was based on an alleged rent differential between National's basic rent and that of Upper Crust, without regard to the qualitative disparity of the space.

The landlord argued to the trial court that National's position was untenable for four reasons:

1. First floor retail space is leased without heating, cooling, cleaning, utilities, maintenance or parking rights and is not comparable to upper floor office space which is provided with all those facilities and services.[64]
2. The cafeteria's 940 square feet, comprising the least desirable area in the building, could not be compared with 165,160 square feet (National) or 54,104 square feet (its attorneys) as to quality, size, or location.[65]
3. The Upper Crust construction allowance was to defray part of the cost to enable the tenant to bring the space *up to* building standard, whereas the allowances to National and its attorneys were to provide prime space over and beyond building standard.[66]
4. Those non-comparable differences could not be twisted and distorted into disadvantages for National and its attorneys and then be applied to their approximately 200,000 square feet of the building's most desirable space.[67]

2. *Federal Home Loan Bank Lease*

The second prong of National's and its attorneys' complaint was that on a line item approach, and only in overlapping lease years,

64. *See* Joint Consolidated Reproduced Record at 1387, *National Intergroup, Inc.*, (Nos. 1721, 1838, 1758 and 1865 PGH 1989).

65. *See id.* at 1354.

66. *See* Joint Consolidated Reproduced Record at 1388, *National Intergroup, Inc.*, (Nos. 1721, 1838, 1758 and 1865 PGH 1989).

67. *See generally id.* at 1346-1398.

FHLB was favored principally as to base rent and parking.[68] The following discussion demonstrates the importance of expert testimony, and the fact intensive analysis which was required to demonstrate the invalidity of that position, and the potential complexities and ramifications that a "simple" favored nation lease provision can cause.

a. Rent

National had a ten year lease from 1982-1992 and occupied 165,160 square feet on floors 11, 12, and 14-20. FHLB's ten year lease ran from 1985-1995 and it occupied 45,611 square feet on floors 3, 4 and one-half of 5. By comparing only the stated rent for the years that overlapped (1986-1992) and ignoring the lower rents paid by National for the years 1982-1985, National complained that FHLB's rent was more favorable by $5-$6 per square foot, as illustrated by this chart:

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68. National's original negotiator, to whom National's attorney ascribed originating the idea of favored nation, acknowledged that "absolutely" everything in the lease had to be considered as a totality, including, among the many matters of importance, (i) the landlord's accommodation of staggering the rent so that it would be lower in the earlier years in order to improve the tenant's cash flow, (ii) the parking facility, (iii) its name on the building, (iv) control over development of an adjacent parcel, (v) occupancy of the upper floors, (vi) the landlord's alteration of the skin of the building using steel spandrel panels manufactured by National, (vii) a renewal option, (viii) an expansion option, (ix) favorable assignment and subletting provisions, (x) and the landlord's payment of part of the cost of the heliport on the roof of the building. Joint Consolidated Reproduced Record at 398-419, *National Intergroup, Inc.*, (Nos. 1721, 1838, 1758, and 1865 PGH 1989).

Even National's real estate expert testified that, to compare leases, it is essential to take into consideration and to value all components of each lease "as a whole," a total package, and not to segregate each discrete item for separate comparison. *Id.* at 1097-1106. He acknowledged that in his experience and from his perspective each party "looks to that lease as a package of benefits, obligations and liabilities." *Id.* at 1100, 1105.

Nonetheless, National's expert accountant testified that he had been instructed by his client to disregard the earlier years of its ten year lease, ignoring that, at its request, its rent had been started at a low level and gradually increased in order to improve its cash flow and earnings in the early years. Also disregarded were the many benefits it had been granted at the commencement of the lease term. He limited his comparison solely to the overlapping years of the subsequent tenancies. *Id.* at 1003-1005. National's real estate expert used the same methodology and neither he nor the accountant attempted to value any of the non-monetary elements contained in the lease. National also complained that FHLB received (1) 5 hours of free utilities on Saturdays which National did not, (2) more months of free rent, and (3) a space planning allowance, as well as some other particular items including a construction allowance the grant of which was disputed by the landlord. *Id.*

Term		FHLB 10 years (1985-95)	National 10 years (1982-92)
Base Rent(SF)	1986	$15.00	$19.63
overlapping	1987	16.00	21.04
years with	1988	17.00	22.39
(lease yr.	1989	18.00	23.67
ending)	1990	19.00	24.88
	1991	20.00	26.01
	1992	21.00	27.06

Landlord's expert rejected as illogical a comparison based on overlapping years, and opined that only by dealing with each lease in its entirety as an integrated document can there be a meaningful evaluation.[69] Accordingly, when there are two leases with ten (10) year terms and different starting dates and staggered rents (that is to say annually increasing rents), the first year of the one lease must be matched against the first year of the other lease and that procedure followed for each subsequent year. By doing so for the National and FHLB leases, the claimed $5-$6 per square foot rent differential became $2.32 per square foot in favor of FHLB, which was further reduced by discounting to present value. When that differential was placed in the context of all the other lease monetary and non-monetary provisions, it not only disappeared but clearly established that National was substantially favored over FHLB.[70]

b. Parking and Its Valuation

National argued that FHLB had 20 parking spaces available to it for $140 per space, whereas it had only 60 available spaces at a claimed cost of $188 per space. There were two basement parking levels in the building. The upper level was operated as an attended parking garage and had a capacity of 80 cars. The lower level contained the same area and was reserved for National's private use, which it rented for $10,000 per month. National chose to operate it as a self-park facility for 60 cars (rather than 80), with a private card-operated gate. As both levels had the same area, landlord's expert concluded, after an on-site inspection, that it was appropriate to treat the lower level as having the same capacity (80 cars) as the upper level.[71] The rental rate of $10,000 per month thereby

69. *See* Joint Consolidated Reproduced Record at 1363-1365, *National Intergroup, Inc.*, (Nos. 1721, 1838, 1758, and 1865 PGH 1989).

70. *Id.* at 1384.

71. *Id.* at 997-998.

equated to $125 per month per car for National. The available parking space represented one car space for each 2,064.5 square feet of National's office area, as against one space for each 2,280.55 square feet of FHLB's office space. The net effect was that National had exclusive access to a better ratio of parking than FHLB and at $15.00 per car space less rent.[72] Based on that analysis he opined that National had a parking advantage over FHLB of at least $.10 per square foot per year.

c. Location Within Building and Its Valuation

Whereas Federated's favored nation clause specifically made location of the favored/disfavored tenant part of the analysis, National's clause was silent on this matter.[73]

National's 165,160 square feet of net rentable area (or 148,779 square feet of usable area) were on floors 11 through 20, which comprised all the top floors of the building (with the 13th floor housing mechanical equipment).[74] FHLB's 45,611 square feet of net rentable area (or 40,192 square feet of usable area), were on the 3rd and 4th floors and part of the 5th floor.[75]

The landlord's expert was permitted to testify that rentals in high rise office buildings increase for the higher floors as the views are generally better.[76] Based upon a physical inspection of the building, he concluded that the city-side views from floors three to five looked directly at the facades of old two to four-story buildings and that above that level the city views cleared the adjoining rooftops to the city skyline.[77] He deemed it appropriate to make the National/FHLB comparison by using the middle floor of FHLB (4th floor) as against the middle floor of National (16th floor).[78] Using that guidepost, he deemed each of National's floors to have a rental value that escalated every floor by $.10 per square foot of usable area or an average of $1.20 per square foot.[79] Moreover, to offset the particularly poor exposure of FHLB's floors, he determined that an additional $.25 per square foot should be added to

72. The landlord's expert concluded that this discrepancy would likely widen in the future.

73. Joint Consolidated Reproduced Record at 1358, *National Intergroup, Inc.* (Nos. 1721, 1838, 1758, and 1865 PGH 1989).

74. *Id.* at 1371.

75. *Id.* at 1371-1372.

76. *Id.*

77. *Id.* at 1372-1374.

78. Joint Consolidated Reproduced Record at 1373-1374, *National Intergroup, Inc.* (Nos. 1721, 1838, 1758 and 1865 PGH 1989).

79. *Id.* at 1373.

the comparative value of the National space, for a total differential of $1.45 per square foot in National's favor.[80]

d. Landlord's Loss of Roof Area and Its Valuation

As required by National, the entire roof area, comprising approximately 18,000 square feet, was converted into a heliport for its use.[81] In addition, 8,600 square feet was converted into office and storage space for National's use, for which utilities, including HVAC, were supplied without cost and for which National paid no rent.[82] The landlord's expert testified that, barring the negative effect that the roof heliport could have on some prospective tenants and based on his own experience in leasing roof spaces for heliports, communications dishes and the like, the advantage to National had a value on the lease commencement date of $126,000 per year.[83] Additionally, the value of the office/storage space was $.40-$1.00 per square foot, and the value of the landlord's contribution to the construction on the roof was approximately $300,000.[84]

e. Valuing the Building Name

At National's insistence, the building was named National Steel Center. The landlord's expert testified that, excluding any negative effect[85] a named building could have on the landlord's ability to attract other tenants, it has a positive value to the favored tenant,

80. *Id.* at 1373-1374.

81. *Id.* at 1376.

82. *Id.* at 1697.

83. i.e. $.85 per square foot per year for the 148,779 square feet of National's usable building area. *See* Joint Consolidated Reproduced Record at 1376, *National Intergroup, Inc.* (Nos. 1721, 1838, 1758, and 1865 PGH 1989).

84. *Id.* at 1126.

85. There are, of course, different views as to whether a named building is a plus or a negative. Many lead tenants want to have their name on the building they occupy. For some, this is mandatory, and it can become a "deal-breaker" in their negotiations. Other lead tenants, however, prefer *not* to have their name on a building. For example, many law and accounting firms feel that it would be unprofessional to have a building carry their name. *Id.* at 1376-1377.

The landlord needs a lead tenant and will usually be willing to name the building for that tenant, sometimes for a specific price, but more often as part of the overall deal. The landlord also needs to fill the building with secondary tenants and must recognize that his universe of prospects grows smaller as soon as the building is named for a lead tenant since some secondary tenants object to using another firm's name in their own return address, and avoid "named" buildings entirely. Moreover, some secondary tenants may be concerned with a building named after a competitor. For example, the ABC Insurance Company does not wish to be in the XYZ Insurance Building, even if it is desirable in every other way, but the DEF Shipping firm might have no objection.

and a portion of the basic rent is properly ascribable to that value.[86] It was his judgment that the name had a value to the tenant of $200,000 on the lease commencement date which, at a 13% annual discount rate, represented $26,000 a year.[87]

f. Valuing Landlord's Accommodation to Tenant's Construction/ Alteration Requests

The 14th and 20th floor ceilings were constructed approximately 1 foot higher than other floors. The 14th floor was originally planned that way and the 20th floor was raised at the request of National, with an estimated cost to the landlord of approximately $200,000.[88] Amortizing that amount over the initial term of the lease at 13% amounted to $36,858 per year or $.25 per square foot.[89] Revision of the building plans in connection with elevator crossover on the 11th floor to accommodate National's request cost the landlord approximately $130,000, which incorporated a loss of square footage which the landlord could have rented.[90] This cost represented an additional $.16 per square foot benefit to National.[91]

g. Other Benefits Enjoyed by National in the Nature of Secondary Monetary Benefits Which Were Not Valued

First, National signed a lease for 4,460 square feet of lobby level areas at $15.09 per square foot for the first five years and $22.39 for the second five years.[92] After holding that area off the market, National requested that it be released from that obligation and the landlord acquiesced without receiving any consideration for the release.[93] It took five more years for the landlord to lease the main portion of that space to another tenant.[94] Although difficult to quantify in dollars and cents, the release had a value to the tenant and a cost to the landlord. Second, in addition to its prestigious

86. *Id.*

87. That represented an average of $.17 per usable square foot for the 148,779 square feet demised by the National Steel lease. Joint Consolidated Reproduced Record at 1377, 1385, *National Intergroup, Inc.*, (Nos. 1721, 1838, 1758, and 1865 PGH 1989).

88. *Id.* at 1378.

89. *Id.*

90. *Id.* at 1269.

91. *Id.*

92. Joint Consolidated Reproduced Record at 1380, *National Intergroup, Inc.* (Nos. 1721, 1838, 1758, and 1865 PGH 1989).

93. *Id.*

94. *Id.*

location in the building, National enjoyed a private elevator bank stopping only on its floors; no similar benefit was conferred on FHLB.[95] Third, the landlord owned an adjacent site on which another office building could have been erected. National was given a first refusal purchase option as well as the right to reject any plans for architectural and aesthetic compatibility to the National Steel Center.[96] Fourth, National's lease was superior to all ground and air rights leases and mortgages.[97]

B. Summary of the Landlord's Expert Opinion

Offsetting FHLB's basic rent advantage of $2.32 per square foot (which had a first year present value of $1.06 per square foot of usable area), the landlord's proof established that the aggregate secondary monetary advantages that National enjoyed over FHLB exceeded $2.82 per square foot, consisting of its parking, location within the building, building name, heliport and roof office and storage space and higher ceilings. In addition, it enjoyed non-monetary advantages consisting of the release of its first floor retail space, private elevator bank, option on adjoining property and superior lease. The landlord's expert concluded that the favored nation clause had not been violated and did not justify a reduction in rent for National.

C. The Trial Court's Opinion Dismissing the Claim of Alleged Disfavor

Unlike the Federal Rules of Civil Procedure and various state rules that require a court sitting without a jury to make specific findings of fact and conclusions of law, Pennsylvania practice permitted the court to render a general verdict dismissing the favored nation claims. Without attempting to state the precise extent to which National and its law firm retained their favored positions over FHLB and Upper Crust, the court found the favored nation clause "to be murky and vague."[98]

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95. *Id.* at 1381.

96. *Id.* at 1382.

97. Joint Consolidated Reproduced Record at 1383, *National Intergroup, Inc.* (Nos. 1721, 1758, and 1865 PGH 1989).

98. Transcript of Non-Jury Verdict at 5, National Intergroup, Inc. v. Oliver Tyrone Corp., GD 87-19306 (Allegheny County, Pa., May 19, 1989). "[T]here was a meeting of the minds with respect to the clause, but . . . neither side contemplated the result for which the plaintiffs contend." *Id.* "There are so many things which lead me to that conclusion, not the least of which, of course, is the renewal clause in the leases

It held that it is unreasonable to "compare this kind of a most favored tenant clause with a technical licensing most favored nation clause . . . Those things are very simple . . . This is not . . . ."[99]

Regarding the clause's construction, the court stated: "The only reasonable interpretation, is a comparison of tenancy to tenancy and not a line by line comparison of leases, ..."[100]

With respect to the plaintiffs' satisfaction of its burden of proof, the court held: "[T]he plaintiffs have simply failed to [prove] by a preponderance of the evidence that either of the plaintiffs has been . . . disfavored by a comparison of lease to lease whether it involves the Upper Crust or the cigar stand or the barber shop or the Federal Home Loan Bank."[101]

As for the expert testimony, "[t]he court basically accepted the expert testimony of defendants' witnesses and rejected that of plaintiffs' expert witnesses."[102] In doing so, the court explained:

> [Tenant's expert] testified on which the plaintiffs place such great reliance, among other things he considered only the economic factors. He said that because it is too tough to figure values, the value of some advantages. Well, the fact [that] it may have been tough to figure out their value doesn't mean they don't have any value and he indicated that they do. He gave no consideration to the eighty-six hundred square feet of space occupied by National for no rent.
>
> I recognize the fact they paid a lot of money to build it [the heliport], so forth, they don't own it, they don't pay any rent for it. That was a matter that could have been negotiated.
>
> He gave no consideration to the amount of money that was spent by [landlord] with respect to the heliport or to the allowance which they made toward the design of it.
>
> He gave no consideration to the extra cost of the elevator crossover. This is from his own testimony. He gave no consideration to the raising of the ceilings on [floors] fourteen or twenty.
>
> I recognize what your [tenant's] position is with respect to that, but there are, nevertheless, benefits which were received by the tenants at the expense of the landlord at their request, that is the

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that exist when it talks about renewals at rates for comparable office space." *Id.* at 5-6.

99. *Id.* at 6-7.

100. *Id.* at 8.

101. Transcript of Non-Jury Verdict at 9, *National Intergroup, Inc.* (GD 87-19306).

102. Opinion and Order of Court Granting Motions for Post-Trial Relief at 24, *National Intergroup, Inc.* (GD 87-19306).

> tenant's request, and a number of other items, comparison of rentable and useable space and other things.[103]

The trial judge denied the tenant's motion to vacate, repeating substantially its prior holding.[104]

V. The Ultimate Lesson

No municipal or private landlord, and no lender could look at the Pittsburgh experience, including the judgment assessing liability against the landlord in the *Federated* dispute of $7.7 million, or the scope of the claims of the Steelers/Pirates, or those of the tenants in *National Intergroup*, and conclude that a favored nation provision in a commercial lease is other than a potential hornet's nest unless drafted with the highest degree of precision and so as to anticipate all reasonably foreseeable eventualities.

To compound the complexities of the problem, *National Intergroup* was decided by a court of original jurisdiction, and dismissal of the tenant's appeal prevented appellate review. Although it is believed that the right result was reached and for the right reasons, there is no assurance that another court or tribunal will follow the same rationale and will, for instance, require comparability, reject the line item approach, value non-monetary items or attribute similar values to them. Conceivably there could be a literal interpretation by some courts of leases negotiated by sophisticated parties that will prevail over what is objectively reasonable even if the result is to render a lease unassignable and unfinanceable and "at odds with normal business practice."[105]

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103. Transcript of Non-Jury Verdict at 17-18, *National Intergroup, Inc.* (GD 87-19306).

104. Opinion and Order of Court Granting Motions for Post-Trial Relief, *National Intergroup, Inc.* (GD 87-19306). The court granted the plaintiff's motion for post-trial relief, in part, as to the issue of the application of the Pittsburgh Business Privilege Tax to damages awarded due to a violation of the tax escalation clause of the lease. The court adhered to its decision in favor of the defendants on the favored nation issue.

105. *See* Wallace v. 600 Partners Co., 618 N.Y.S.2d 298 (N.Y. App. Div. 1994) (Ellerin, J., dissenting), *aff'd*, 1995 WL 643828 (Nov. 2, 1995). The real danger of a literalist approach to lease construction may be found in the unanimous affirmance of the Appellate Division order in *Wallace* by the New York Court of Appeals. In *Wallace*, a literal reading of what was characterized by the Court of Appeals as a "novel" and "unconventional" appraisal clause in a lease providing that the rent payable for a 33 year option period would not be determined until the end of that period in 2025 was upheld against a "scrivener's error/absurd result argument" because "the instrument was negotiated between sophisticated, counseled business people who negotiated at arms length." Wallace v. 600 Partners Co., 1995 WL 643828 (N.Y. Nov. 2, 1995). The court found "unavailing" the claims of the ground lessee that the clause should not be

For some guidance, barring a lender's outright rejection of the favored nation concept, the following is a non-exhaustive list of inclusions/exclusions/limitations for the draftsman's consideration:

1. Are there time limitations on the favored status of the favored nation beneficiary? Will it apply only to the basic lease term; to any renewal term or terms; to a limited number of years which is less than the basic lease term?
2. How will comparability be defined? Will it apply to non-comparable tenants in non-comparable space, e.g., retail tenants, tenants occupying smaller units or less desirable space, leases of tenants who merely provide building amenities, quasi-public agencies[106] (e.g., Federal Home Loan Bank), tenants leasing space covered by expansion options of the favored or other tenants which necessarily have to be more favorable inasmuch as the duration is shorter and subject to more restrictions? Will there be a trigger mechanism similar to the 50,000 square foot "safe harbor" concept found in Federated's lease?
3. Take nothing for granted.[107] Is the comparison to be predicated upon the entire lease term and not simply overlapping years and are entitlements to be based on aggregating benefits and not on a line item comparison which ignores

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read literally because it would give rise to "fiscal uncertainties resulting from retroactive appraisal" and "difficulty in selling or mortgaging its interest in the lease and setting rents when subleasing to tenants of the office building." *Id.* at *2. Query how a literalist court such as the *Wallace* court would have dealt with *National Intergroup's* argument that:

> the covenant [favored nation] would apply to [and would be triggered by] a small newsstand on the first floor, to a renewal lease, and, indeed, to any person or entity with whom the landlord entered into a subsequent lease agreement. To conclude that this language is to be restricted to agreements with comparable tenants and comparable tenancies flies directly in the face of the unqualified phrase 'any other tenant[s].' "

See supra note 53.

106. The federal government, for example, has its own requirements in connection with leasehold interests and the incorporation of its terms may automatically result in a "more favored term" in the context of favored nation. *See* 1 FRIEDMAN, *supra* note 9, § 3.1.

107. Expectations of anchor or prime tenants with regard to favored, or even bargained for, benefits measured by provisions in leases of subsequent tenants do not always come to fruition. In *J. Henry Schroder Bank & Trust Co. v. South Ferry Bldg. Co.*, 472 N.Y.S.2d 382 (N.Y. App. Div. 1984), a lead tenant that rented over one-third of a new office building was required to pay operating expense escalation, but was entitled to credit for moneys paid by other tenants in reimbursement of landlord. Leases to later tenants required escalation of those tenants' rents based on an increase in wages paid to building cleaning personnel. The lead tenant was denied credit for those sums paid by other tenants because the sums were deemed "rent" and not "reimbursement".

the complexities and the give and take of a long term office lease? Although that concept was rejected in *National Intergroup* it was not so absurd on its face as to justify dismissal as a matter of law in the Steelers/Pirates litigation.

4. Set forth precisely the factors to be included/excluded in the favored nation analysis, such as (a) non-monetary provisions and/or (b) parking, HVAC, electrical inclusion, cleaning, tax/operating stops, free rent, relocation/construction/design allowances and other like or different factors which can be reduced to monetary values.
5. Clarify whether a favored tenant's smaller area can be exploded and held applicable to the entire larger area of the favored nation beneficiary as was done in *Federated* and as was demanded in *National Intergroup* (either as demised in its original lease or as expanded) or be limited to a like area.
6. Provide what will be the effect if the subsequent favored lessee's tenancy has been terminated by eviction or abandonment of the premises or disaffirmance in bankruptcy.
7. Agree in advance if the comparison between favored and disfavored is to be based on usable space, thereby recognizing the potential of different loss factors on floors of different elevations, as opined by the expert in *National Intergroup* or based on a formula or method, sometimes referred to as "phantom footage,"[108] such as the New York rule.
8. If favor/disfavor is qualified by use of the terms "substantial" or "material", such as was found in the Three Rivers Stadium leases, there should be a definition and, if possible, a specific percentage of deviation should be stated. Consideration should be given to provisions for the allocation of costs and legal fees to the prevailing party if it is ultimately determined that the percentage of deviation had not been exceeded.
9. Pre-determine the values to be ascribed to floors on different elevations in the building or negate comparability of lower floors/higher floors.
10. Specify what effect is to be accorded to leases of different duration.
11. Grant/decline favored nation beneficiaries the right to inspect subsequent leases, perhaps on an annual basis at the same time as any annual review of operating escalation and/or audit landlord's books and records, to determine whether any subsequent lessee has been favored with ap-

108. 1 FRIEDMAN, *supra* note 9, § 3.1.

propriate provisions for confidentiality and prescribe a period of limitation within which to contest/adopt any more allegedly favorable lease or lease term or be precluded from so doing or from making any further challenge.[109]

12. Agree on a discount rate for purposes of calculating present value in connection with landlord contributions.
13. Consider the impact of any payments by the landlord to a subsequent tenant to buy out a leasehold or to forgive any current obligation to pay rent or change the terms of payment as impacting on any right granted to the favored nation beneficiary, which arguably would constitute a reduction in rent.

Conclusion

"What we anticipate seldom occurs; what we least expected generally happens."[110] The Pittsburgh Stadium Authority settled favored nation disputes not once, but twice, after three unsuccessful motions to dismiss for legal insufficiency.[111] The Liberty Center Tower, except for Federated Investors, was otherwise unleased and untenanted until 1988 when the landlord, suffering from a negative cash flow, was impelled to lease on below market terms thereby directly and promptly causing a breach of Federated's favored nation clause costing millions. The favored nation clause in *National Intergroup*, written in fifteen minutes, led to lengthy litigation at

109. In *Gould v. Laser Photonics, Inc.*, 93-915-CIV-ORL-19 (M.D. Fla.) the favored nation clause was triggered by "materially more favorable" royalty rates given to a "similarly situated licensee." On a motion for summary judgment triable issues were held to be posed by the application of those clauses. Since the favored nation clause did not impose any time deadline, *Laser* also posed the issue as to when a favored nation beneficiary was deemed to have waived the right to elect a more favorable license and whether the right to elect was retriggered each time an adjustment was made to another licensee based on its favored nation provision. Given the decision of the Arizona Supreme Court in *Gust, Rosenfeld & Henderson v. Prudential Ins. Co.*, 898 P.2d 964 (Sup. Ct. Ariz. 1995) allowing a seventeen-year old claim and the recognition by that court that the parties could have provided for appropriate reviews to assure compliance with favored nation obligations, a clause which is silent with respect to notice or limitation exposes the landlord to potential liability over periods of time which could not be reasonably contemplated.

110. BENJAMIN DISRAELI, HENRIETTA TEMPLE, Book II, Ch. 4 (1837).

111. Memorandum Order (dismissing Preliminary Objections of the Stadium Authority of the City of Pittsburgh and Mellon Bank, N.A. to the Pittsburgh Steelers' Complaint), *Pittsburgh Steelers Sports, Inc.*, No. GD 84-1517 (C.P. Allegheny County, Pa., Apr. 19, 1984); Order of Court (dismissing Preliminary Objections of the Stadium Authority of the City of Pittsburgh and Mellon Bank, N.A. to the Pittsburgh Pirates' Intervenor Complaint), *Pittsburgh Steelers Sports, Inc.*, No. GD 84-1517 (C.P. Allegheny Co., Pa., Sept. 5, 1984); Order of Court, *Pittsburgh Baseball Inc.*, No. GD 92-01392 (C.P. Allegheny Co., Pa., Sept. 1, 1992).

the end of which the tenants, to use their own words, were "complete losers"[112] on the favored nation issue after both landlord and tenant expended huge sums and absorbed their own costs.

Given the magnitude of the potential liabilities resulting from favored nation claims, the costs of litigating them to conclusion and the chilling impact on the ability to lease vacant space at prevailing market rentals, the goal should be to guard against what "we least expect." From the developer's point of view no one should be lulled into concluding that favored nation "can offer peace of mind" to anyone.[113] It does not.

112. Appellant's Application for Reargument of Order dated June 7, 1990 Dismissing Appeal, at 3, Jackson, et al. v. Riverfront, No. 1721 Pittsburgh 1989, National Intergroup Inc., et al. v. Oliver Tyrone Corp., No. 1758 Pittsburgh 1989.

113. *See* Maguire, *supra* note 2.