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IN THE CHANCERY COURT FOR THE STATE OF TENNESSEE
TWENTIETH JUDICIAL DISTRICT, DAVIDSON COUNTY

SH NASHVILLE, LLC AND UNI NASHVILLE AIRPORT HOTEL, LLC	)	
Plaintiffs,	)	**Case No. 22-0569-BC**
v.	)	
FWREF NASHVILLE AIRPORT, LLC,	)	
Defendant.	)	

MEMORANDUM AND ORDER

This matter came to be heard on August 4, 2022, upon the motion of Defendant FWREF Nashville Airport, LLC ("Seller") made pursuant to Tenn. R. Civ. P. 12.02(6), to dismiss the claims in the Complaint filed by Plaintiffs SH Nashville, LLC and UNI Nashville Airport Hotel, LLC ("Purchasers"). Purchasers bring a declaratory judgment action and conversion claim seeking a refund of $18,917,500 in earnest money that was paid for the purchase of a Hilton hotel located near the Nashville airport. Seller contends that Purchasers have failed to state a claim because the contract and its amendments are clear and unambiguous and provide that Purchasers agreed the earnest money would be non-refundable and that they released any and all claims related to the earnest money. Having reviewed the pleadings and relevant caselaw, and having considered the arguments of counsel, the Court finds as follows.

Rule 12 Motion to Dismiss Legal Standard

A motion pursuant to Tenn. R. Civ. P. 12.02 challenges only the legal sufficiency of the complaint, not the strength of the plaintiff's proof or evidence. *Webb v. Nashville Area Habitat for Humanity, Inc.*, 346 S.W.3d 422, 426 (Tenn. 2011) (citing *Highwoods Props., Inc. v. City of Memphis*, 297 S.W.3d 695, 700 (Tenn. 2009)). The resolution of a Rule 12.02 motion to dismiss is determined by an examination of the pleadings alone. *Leggett v. Duke Energy Corp*., 308 S.W.3d

843, 851 (Tenn. 2010); *Trau-Med of Am., Inc. v. Allstate Ins. Co*., 71 S.W.3d 691, 696 (Tenn. 2002). A defendant who files a motion to dismiss "admits the truth of all of the relevant and material allegations contained in the complaint, but … asserts that the allegations fail to establish a cause of action." *Brown v. Tenn. Title Loans, Inc*., 328 S.W.3d 850, 854 (Tenn. 2010) (quoting *Freeman Indus., LLC v. Eastman Chem. Co*., 172 S.W.3d 512, 516 (Tenn. 2005)). In considering a motion to dismiss, courts "must construe the complaint liberally, presuming all factual allegations to be true and giving the plaintiff the benefit of all reasonable inferences." *Tigg v. Pirelli Tire Corp*., 232 S.W.3d 28, 31-32 (Tenn. 2007) (quoting *Trau-Med*, 71 S.W.3d at 696); *see also Leach v. Taylor*, 124 S.W.3d 87, 92-93 (Tenn. 2004).

Factual Allegations in the Complaint

UNI Nashville Airport Hotel, LLC ("UNI") and Seller entered into a Purchase and Sale Agreement dated October 23, 2019 for a Hilton hotel located at 2200 Elm Hill Pike in Nashville for an original purchase price of $79,000,000, and UNI agreed to deposit $1,750,000 of earnest money with an original closing date of January 3, 2020. UNI later assigned its interest to SH Nashville, LLC. The Purchase and Sale Agreement provided in relevant part:

> 6.1. **Seller's Remedies** Prior to entering this transaction, Purchaser and Seller have discussed the fact that substantial damages will be suffered by Seller if Purchaser shall fail to perform its obligations under this Agreement . . . . Due to the fluctuation in land values, the unpredictable state of the economy and of governmental relations, the fluctuating money market for real estate loans of all types, and other factors which directly affect the value and marketability of the Property, the parties recognize that it would be extremely difficult and impracticable, if not impossible, to ascertain with any degree of certainty the amount of damages which would be suffered by Seller in the event of Purchaser's failure to perform its obligation to purchase the Property under this Agreement. Accordingly, the parties agree that a reasonable estimate of Seller's damages in such event is the amount of the Earnest Money, and if Purchaser defaults in any material respect in performing the obligation to purchase the Property under this Agreement to close, including, but not limited to, its obligations under Section 5.4(b), then Seller, as its sole remedy therefor, after delivery of written notice to Purchaser of such failure and the expiration of a five (5) business day cure period from delivery of such notice, shall

> be entitled to immediately terminate this Agreement by giving Purchaser written notice to such effect, **and receive and retain the Earnest Money as liquidated damages**, whereafter the parties shall have no further rights or liabilities under this Agreement, except that (i) Purchaser shall pay the expenses of escrow, and (ii) each party shall continue to be obligated under the Surviving Obligations. **Upon the occurrence of a Purchaser default entitling Seller to receive and retain the Earnest Money as liquidated damages and following the proper termination of the Agreement by Seller pursuant to this Section 6.1, Purchaser hereby waives and releases all rights to purchase the Property** and upon demand from Seller, Purchaser agrees to evidence such waiver and release in written form satisfactory to Seller, which obligation shall survive the termination of this Agreement. . . .

(Emphasis added).

The total purchase price was later increased via an amendment to $82,125,000. The parties entered into 24 total amendments in which the Seller agreed to extend the closing date and give Purchasers the exclusive right to purchase the property in exchange for additional earnest money, with the last amendment effective December 17, 2020 (collectively, the "Agreement"). On October 21, 2020, a press release was issued announcing a 14-story on-airport Hilton hotel at the Nashville airport, which would be located only a few miles away from the hotel at issue, and which was also a Hilton. As of this date, Purchasers allege they had provided earnest money totaling almost 22% of the purchase price for the hotel.

Purchasers allege most of the amendments and closing date extensions were necessitated by the COVID pandemic. Further, that the COVID pandemic and the press release had a negative impact on securing financing to close on the purchase of the hotel. Purchasers allege that it had secured a lender prior to the press release, but that the lender was no longer willing to provide financing for the closing following the announcement of the new Hilton hotel located at the airport, and Purchasers had to find a replacement lender. Purchasers allege the Seller agreed to extend the closing date to obtain a replacement lender, but Seller insisted Purchasers make substantial additional earnest money deposits and that Purchasers were compelled under severe economic

duress to enter further amendments—specifically, Amendment 23, effective October 28, 2020, and Amendment 24, effective December 17, 2020, with a closing date of January 11, 2021.[1] The last amendment provided that the earnest money would be credited towards the purchase price upon closing and that any further requests for extensions "shall result in immediate forfeiture of Earnest Money to Seller." The Purchasers also agreed in twenty-two of the amendments, including the last amendment, as follows in Section 2(e):

> Notwithstanding any other provision of this Agreement to the contrary, Seller and Purchaser acknowledge and agree that the Earnest Money (including the First Deposit, the Second Deposit, the Third Deposit) has been deemed earned by Seller and is non-refundable to Purchaser for any reason (including any reason specifically provided for elsewhere in the Agreement), except (and only in the event) as provided in Section 6.2(b) but solely with respect to a default by Seller in any material respect to perform its obligations under Section 5.4(a) and failure to cure such default within five (5) business days after receipt of written notice from Purchaser of such default. Except in the event of a default by Seller in any material respect to perform its obligations under Section 5.4(a) and failure to cure such default within five (5) business days after receipt of written notice from Purchaser of such default, Purchaser hereby irrevocably releases and forever discharges Seller from any and all claims or demands, whether in law, statute, or equity, whether known or unknown, present or contingent, which Purchaser may now or hereafter have, own, or claim to have in regard to the Earnest Money. In the absence of such event of default by Seller and failure to cure, this Agreement (including specifically this Section) shall be treated as a complete defense to any action or proceeding that may be brought, instituted, or taken by Purchaser against Seller in regard to the Earnest Money and shall forever be a complete and absolute bar to the commencement or prosecution of any such action or proceeding.

Purchaser was unable to close by the closing date. By letter dated January 12, 2021, Seller declared that "the Purchase Agreement has automatically terminated, upon which termination Seller is entitled to all of the Earnest Money." Seller withdrew from escrow and retained the earnest money, totaling $18,917,500, or approximately 23% of the purchase price.

[1] In Amendment 23, Seller expressly acknowledged that the "Purchase Agreement was assigned by UNI to SH Nashville pursuant to that certain Assignment and Assumption of Purchase and Sale Agreement dated October 20, 2020, by and between UNI and SH Nashville (the 'Assignment') . . . ."

Over four months later, after securing a replacement lender to provide adequate financing to purchase the hotel, Purchasers requested in letters dated May 21, 2021 and June 25, 2021 that Seller either proceed with the sale of the hotel or provide a refund of the earnest money. Seller refused. Around June 2021, Seller sold the hotel to Nashville HA Owner, LLC.

Purchasers filed suit on April 22, 2022 and contend that the earnest money "is clearly unreasonable on its face in relation to any potential or estimated damages alleged by [Seller]" and "constitutes a penalty that is invalid and unenforceable as a matter of Tennessee public policy." (Am. Compl. ¶ 48-49.) Purchasers bring two claims—declaratory judgment and conversion.

Legal Analysis of Claims

In its Motion to Dismiss, Seller argues that the Agreement is clear and unambiguous which is dispositive of both claims. Seller contends that Purchasers specifically and repeatedly agreed that the earnest money was non-refundable and a reasonable measure of liquidated damages if they failed to close, and that the claims they now assert were released and barred by the numerous releases in the Agreement. Specifically, Purchasers agreed twenty-three times, including in the last amendment, that the earnest money paid was "deemed earned" by Seller and "non-refundable" for any reason. Purchasers also agreed twenty-two times, including in the last amendment, that Purchasers would discharge and release Seller from any and all claims in regard to the earnest money and that the Agreement would be a "complete defense" to any action or proceeding brought against Seller in regard to the earnest money. Seller contends that it agreed to multiple extensions in exchange for additional earnest money deposits and provided Purchasers with the exclusive right to sell.

In response, Purchasers contend that they have sufficiently alleged their claims to survive a motion to dismiss. Specifically, that the circumstances surrounding the contract formation and

amendments thereto, including COVID and the announcement of the on-airport Hilton hotel which it alleges amounted to severe economic duress, constitutes a forfeiture and penalty contrary to public policy. Purchasers' position is that the $18,917,500 paid in earnest money is so high that it is unreasonable on its face and against public policy. Purchasers' contend that the Court is required to consider the circumstances at the time of formation. In contrast, Seller contends that one cannot look at the aggregated amount of earnest money received, but rather must look at each amendment and separate earnest money deposit as consideration for each extension, which it contends is reasonable under the circumstances.

In a similar case, *Kendrick v. Alexander*, 844 S.W.2d 187 (Tenn. Ct. App. 1992), the parties entered into a purchase and sale agreement for real estate with a total purchase price of $500,000 to close in ninety days with an earnest money deposit and partial down payment of $10,000. *Kendrick*, 844 S.W.2d at 188. Before the ninety days, the parties executed an addendum in which the purchaser agreed to pay an additional $20,000 in earnest money in exchange for an extension, with the $30,000 to be forfeited as liquidated damages if the closing was not timely. *Id*. at 189. When unable to obtain financing, the purchaser signed a second addendum in which the seller agreed to an additional extension of the closing date in exchange for additional monies, and, further, that $60,000 of the earnest money would be forfeited as liquidated damages if purchaser failed to timely close. *Id*. The purchaser failed to close and then sued to recover $110,000, including the $60,000 of forfeited earnest money. *Id*. After a trial, the trial court found the sums paid by plaintiff were "greatly in excess of a reasonable estimate of the damages that would occur" from purchaser's breach of contract and that, therefore, it was "a penalty constituting a punishment and forfeiture not permitted by law." *Id*. The Court of Appeals reversed, finding the liquidated damages provision was reasonable:

> [W]e conclude that the amount stipulated as liquidated damages, $60,000.00, is reasonable in relation to the terms of the parties' contract. The initial contract required a down payment of $10,000.00 which would be forfeited in the event that Plaintiff defaulted. In order to extend the parties' closing date, the December 29 addendum required Plaintiff to pay an additional $20,000.00 earnest money and, accordingly, raised the stipulated amount of liquidated damages to $30,000.00. The January 15 addendum, which extended the closing date to January 19, again raised the amount of liquidated damages to $60,000.00. Obviously, the parties' renegotiation of the liquidated damages provision comprised part of the consideration for Defendants' extensions of the closing date. *See Testerman v. Home Beneficial Life Insurance Co.*, 524 S.W.2d 664 (Tenn.App.1974).

Id. at 190-91. Thus, as Seller argues, the Court should look at each extension and separate payment of earnest money, which Seller contends is reasonable, instead of the aggregated amount of earnest money retained by Seller.

At issue is whether the liquidated damages provision(s) and the amount of earnest money retained by Seller as a result of Purchasers' breach is a reasonable estimate of damages. Regarding liquidated damages, our Supreme Court has explained:

> From our review of the law on liquidated damages, we recognize that there are two important interests at issue: the freedom of parties to bargain for and to agree upon terms such as liquidated damages and the limitations set by public policy. Generally, the parties to a contract are free to agree upon liquidated damages and upon other terms that may not seem desirable or pleasant to outside observers. In that respect, courts should not interfere in the contract, but should carry out the intentions of the parties and the terms bargained for in the contract, unless those terms violate public policy.
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> When parties agree to a liquidated damages provision, it is generally presumed that they considered the certainty of liquidated damages to be preferable to the risk of proving actual damages in the event of a breach. Liquidated damages permit the parties to allocate business and litigation risks and often serve as part of the contractual bargain. In addition, they lend certainty to the contractual agreement and allow the parties to resolve defaults and other related disputes efficiently, when actual damages are impossible or difficult to measure.
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> * * *

> We, therefore, adopt a prospective approach for addressing the recovery of liquidated damages. **Under this approach, courts must focus on the intentions of the parties based upon the language in the contract and the circumstances that existed at the time of contract formation. Those circumstances include: whether the liquidated sum was a reasonable estimate of potential damages and whether actual damages were indeterminable or difficult to measure at the time the parties entered into the contract.** If the provision satisfies those factors and reflects the parties' intentions to compensate in the event of a breach, then the provision will be upheld as a reasonable agreement for liquidated damages. However, if the provision and circumstances indicate that the parties intended merely to penalize for a breach of contract, then the provision is unenforceable as against public policy.

Guiliano v. Cleo, Inc., 995 S.W.2d 88, 99-100 (Tenn. 1999) (internal citations omitted) (emphasis added). A "penalty" in a contract, as distinguished from liquidated damages, is defined as "a sum inserted in a contract, not as the measure of compensation for its breach, but rather as a punishment for default, or by way of security for actual damages which may be sustained by reason of non-performance, and it involves the idea of punishment." *Harmon v. Eggers*, 699 S.W.2d 159, 163 (Tenn. Ct. App. 1985) (quoting 22 Am. Jur. 2d *Damages* § 213 (1965)).

In their Amended Complaint, Purchasers have alleged that COVID and the press release regarding the development of the on-site Hilton airport hotel were circumstances that existed at the time of contract formation which prevented it from obtaining financing to close, and that this, coupled with the high number retained by Seller that encompassed roughly 23% of the overall purchase price, was unreasonable and constituted a penalty. While Seller's arguments regarding the unequivocal and clear terms of the Agreement are quite strong, the Court finds, given the standard applicable to Rule 12.02(6) motions to dismiss, that Purchasers have sufficiently pled their declaratory judgment claim. The Court notes, however, that Tennessee courts have regularly upheld liquidated damages provisions at the summary judgment stage. *See, e.g.*, *Teter v. Repub. Parking Sys., Inc.*, 181 S.W.3d 330, 343-44 (Tenn. 2005) (finding summary judgment appropriate on question of enforceability of liquidated damages provision in contract but reversing on other

grounds); *Guiliano*, 995 S.W.2d at 101 (reinstating trial court's award of summary judgment to the plaintiff on his claim for liquidated damages); *see also Raley v. Jackson*, No. 3:04–0877, 2007 WL 1725254 (M.D. Tenn. June 12, 2007) (applying Tennessee law and granting counterplaintiff's motion for summary judgment enforcing the liquidated damages provision of the parties' contract).

As to Purchasers' claim for conversion, Seller contends that this claim is barred by the economic loss doctrine. The economic loss doctrine "has been described as a 'judicially-created remedies principle that operates generally to preclude contracting parties from pursuing tort recovery for purely economic or commercial losses associated with the contract relationship.'" *Com. Painting Co. Inc. v. Weitz Co. LLC*, No. W2019-02089-COA-R3-CV, 2022 WL 737468, at *13 (Tenn. Ct. App. Mar. 11, 2022) (citing *Milan Supply Chain Sols., Inc. v. Navistar, Inc*., 627 S.W.3d 125, 142 (Tenn. 2021)). The Court agrees, as the parties have a controlling contract that outlines the parties' rights and obligations. *Id.* at *1 (The Court of Appeals concluded the economic loss rule is applicable to construction contracts negotiated between sophisticated commercial entities).

IT IS THEREFORE ORDERED, ADJUDGED and DECREED that Seller's motion to dismiss is DENIED IN PART as to Purchasers' claim for declaratory judgment, and GRANTED IN PART as to Purchasers' claim for conversion. Purchasers' claim for conversion is hereby DISMISSED.

CASE MANAGEMENT

Given the Court's ruling on Seller's motion to dismiss, it must file a response to Purchasers' Motion for Leave to File Second Amended Complaint so that the Court can determine whether to set the motion for hearing. If there is no objection to the motion, then an Order can be entered allowing the amendment and the filing of the Second Amended Complaint and triggering

Seller's obligation to file an answer. Once the pleadings are closed the Court can proceed with a Rule 16 Conference.

Seller's response or notice of no opposition to Purchasers' Motion to Amend shall be due on or before August 24, 2022. If a response in opposition is filed, the Court will set a hearing. If a notice of no opposition is filed, Purchasers are ordered to file an Order granting the motion and allowing the filing of the Second Amended Complaint. After it is filed and an answer is filed, the Court will set the Rule 16 Conference at which the Court will address, among other subjects, a discovery schedule for the case. The Court has noted above one of the issues for resolution—whether the liquidated damages provision(s) are a reasonable estimate of damages, with attention to the intentions of the parties based upon the language in the contract and the circumstances that existed at the time of contract formation.

IT IS SO ORDERED.

s/Anne C. Martin

ANNE C. MARTIN
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