

Questions Regarding Rent Relief for Commercial Tenants Affected by COVID-19*



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Below, in question and answer form, is a discussion of the availability of rent relief for commercial tenants affected by COVID-19.

My lease contains a force majeure clause. If I can't use my space because of a government-mandated prohibition of occupancy, does that clause give me the right to suspend rent payments?

Almost certainly no, because:

- Under many leases, the force majeure clause only runs to the benefit of the landlord.
- In those leases in which the force majeure clause is reciprocal, the obligation to pay rent is often excluded.
- Depending upon the exact wording of your force majeure clause, the COVID-19 crisis might not even be considered force majeure.
- In the strict legal sense, COVID-19 may prevent you from occupying your premises, but it does not prevent you from paying rent. If you have the money, nothing is preventing you from making payment. Force majeure clauses do not cover financial hardship.

On the other hand, a properly worded force majeure clause will excuse a tenant from performing a covenant of continuous operation or other obligation whose actual performance is made illegal or impossible by COVID-19.

My lease provides that if building services or access are interrupted for more than a specified period of time, I am entitled to a rent abatement. Does that mean I have the right to suspend rent after that period?

Very likely no, because:

- In general, building services such as electricity, HVAC, cleaning, trash removal, etc., are not interrupted. They are available for any tenant in occupancy.
- Even access is not really interrupted. That buildings remain accessible is demonstrated by the fact that, even in states under strict shutdown orders, those businesses legally permitted to remain open (e.g., newspapers and other media, restaurants for take-out & delivery) can access their buildings and their premises, as can, in many states, workers performing essential services for non-essential businesses, such as retrieving mail and payroll processing.
- A typical inaccessibility provision in a lease would either be expressly limited to, or would be understood by a court to relate only to, inaccessibility caused by the landlord and not by inaccessibility outside of the landlord's control.

What about the fire & casualty clause in my lease? Does that help?

Probably not or not for very long, because fire & casualty clauses (and the rent abatements they include) only cover physical damage to the building or the premises, and the virus doesn't cause visible physical damage to buildings. Actual physical contamination by the virus might be deemed to constitute physical damage creating untenability, but this is speculative at best, and the landlord might avoid or limit even this claim by providing any requisite extra cleaning. Also, under many leases, landlord obligations under the fire & casualty clause are limited to the base building and exclude tenant's improvements and personal property altogether.

How about the condemnation or eminent domain clause?

No, that doesn't help either. A prohibition of occupancy is not a taking. If the government takes your premises and uses them as a COVID-19 command center, that would be a taking.

Are there any good theories, from the tenant's perspective?

There is the legal doctrine of frustration of purpose, but its applicability to tenants affected by COVID-19 is very speculative. Under this doctrine, as formulated in an important publication of the American Law Institute:¹

Where, after a contract is made, a party's principal purpose for entering into a contract is substantially frustrated without his fault by the occurrence of an event the non-occurrence of which was a basic assumption on which the contract was made, his remaining duties to render performance are discharged, unless the language or the circumstances indicate the contrary.

From the tenant's perspective, that sounds really good, because the tenant's principal purpose for entering into its lease was to occupy the premises for the conduct of business and that has been substantially (if only temporarily) frustrated by the government-mandated shutdowns in response to the virus. However, there are very few reported legal decisions in which a tenant advancing the doctrine of frustration of purpose has prevailed and most of those have involved situations in which a lease limited the tenant's use to a specific purpose and the tenant sought to cancel the lease because that purpose had become illegal. Additionally, for hundreds of years, the common law has treated leases differently than other commercial contracts and while this separate status has eroded in recent decades, applying the frustration of purposes doctrine to a pandemic in order to suspend rents under commercial leases would mark a major change in the common law. Finally, before advancing a frustration of purpose argument a tenant who seeks only a rent suspension, rather than a lease cancellation, will need to consider the possibility that only the latter will be available.

Are there any new laws that suspend rent or otherwise protect commercial tenants?

As of today, no state has adopted a law suspending commercial rents. A bill was introduced into the New York legislature that would have suspended rents for 90 days for many small businesses, but this bill was not reported out of committee, and the legislature adjourned without voting on it. Such legislation remains possible in New York and elsewhere, but the new federal Paycheck Protection Program for small businesses may lessen the calls for legislation specifically addressed to commercial rents.

Laws or orders suspending commercial evictions have been adopted or issued in many states and cities. For example, in New York, commercial evictions are now prohibited through June 17, 2020. Some California cities have gone further: not only are commercial evictions prohibited for the duration of the COVID-19 emergency, but tenants are given specific periods after the emergency ends to repay the overdue rent, and late charges are curtailed. Tenants should bear in mind that these laws do not forgive the rent accruing during the suspension nor, by their terms, do they eliminate other consequences of being in default, such as loss of expansion or renewal rights. Court cases addressing various questions under these laws can be expected.

¹ Restatement (Second) of Contracts, §265 (1979)

So should I just pay my rent? What will happen if I do not?

These are more difficult questions. As a legal matter (and, if applicable, after the expiration of any prohibition of the type described immediately above), if you don't pay, the landlord can usually charge interest (which under most leases is quite steep) and late fees and move to evict. Also, many leases provide that if the tenant defaults, the tenant loses the benefit of landlord concessions such as free rent, cash contribution, etc. and loses many important rights, such as renewal, expansion, and subletting. So it is risky to just stop paying rent. It might be better to negotiate with your landlord. Landlords understand that many of their tenants are struggling and may be willing to work with a tenant who is materially harmed by the crisis but who they believe will be restored to financial health as the crisis passes.

Various types of arrangements are being discussed, such as:

- Abating rent for a specific period and extending the lease term for an equivalent period or longer.
- Abating a specific amount of rent or rent for a specific period and adding the abated rent (with or without interest) to the rent payable for the balance of the term.
- Abating a specific amount of rent or rent for a specific period and requiring that the abatement be repaid when the tenant receives funding under the Paycheck Protection Program or other government program. This would need to be structured to avoid disqualification under the PPP or other program.
- Use of security deposit to fund rent.
- Relinquishing renewal or expansion rights in exchange for rent relief.

The willingness of the landlord to engage in discussions and the outcome will depend on many factors including, but not limited to, the landlord's financial objectives and condition, the perceived financial strength of the tenant, constraints imposed on the landlord by building financing, and other tenants in the buildings and their situations.

Caveat & Conclusion

There are in the United States many commercial leases in effect, many tenants seriously affected by the COVID-19 crisis, many highly skilled litigators, and many sympathetic judges. So, probably, there will be some cases which contradict the conclusions expressed above but, nonetheless, in the great majority of cases the principles and conclusions set out above should apply. The only potential exception to this which could have widespread applicability is the possibility that courts embrace the frustration of purpose doctrine explained above, something which the author does not expect.

Savills is available to help its clients deal with the effects of COVID-19 on their occupancies, leases, premises, and construction projects. This white paper deals with only one aspect of that topic.

**This white paper does not constitute, and neither Savills nor the author is providing, legal advice. No attorney-client relationship is or will be established. Tenants and other transaction parties are encouraged to consult with their legal counsel.*

***For more than 30 years before joining Savills in 2008, the author practiced law, specializing in representing commercial office tenants in New York and throughout the country.*

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