

Real Estate Law: COVID-19 brings commercial lease enforcement issues



By **JOHN A. ANDERSON**

In response to the COVID-19 emergency, the governor of New York issued executive orders significantly restricting the business activities that commercial tenants could conduct from leased locations in New York state. Many tenants impacted by these orders have refused to pay rent and other charges due under their leases on account of the inability to use their premises, financial hardship caused by such restrictions, or both. As the COVID-related restrictions are eased to allow commercial tenants to again use their leased locations, disputes over unpaid rent are likely.

Executive Order 202.8 issued by Gov. Andrew Cuomo on March 20 prohibited the enforcement of commercial evictions in New York State until June 18, 2020. At the same time, the Chief Judge of New York limited state court operations to essential matters. While the state court limitations have been (or soon will be) lifted in most New York counties, Executive Order 202.28 issued on May 7, 2020, extended the commercial eviction moratorium until August 19, 2020, for tenants “eligible for ... benefits under state or federal law or otherwise facing financial hardship due to the COVID-19 pandemic.” As a result, while commercial landlords are prohibited from commencing eviction proceedings against most commercial tenants until mid-August, they may still pursue other responsible parties and other remedies outside of an eviction proceeding.

One potentially responsible party is a guarantor. Commercial landlords usually request, and often receive, lease guaranties from a tenant’s parent company and/or major equity

owner(s). Courts in New York generally enforce such guaranties in accordance with their specific terms. If a commercial tenant has refused to pay rent, and if a lease guaranty exists, the landlord should review the guaranty to determine if additional notices to the guarantor are required and may also pursue independent legal remedies against the guarantor.

Another potentially responsible party is an assignor. Businesses that rent commercial property are bought and sold every day. Often, such transactions are structured as an asset sale under which the seller assigns its lease to the buyer and the buyer assumes the lease obligations. Under New York law, the seller/assignor remains primarily liable for all of the tenant’s obligations under the lease after assignment unless (1) the lease expressly provides for a release upon assignment, or (2) the landlord affirmatively releases the assignor. In many sale transactions, neither of those conditions is met. As a result, if an existing commercial tenant is in default, and if the existing tenant assumed the lease from a prior tenant, a landlord may be able to hold the prior tenant liable, if it is still in existence.

Commercial landlords often enter into agreements with third parties at the request of tenants. One example is a landlord lien waiver that benefits a tenant’s lender and which typically requires a landlord to notify the lender of tenant defaults and afford the lender time to retrieve its collateral from the premises. Another example is a franchisor waiver that the franchisor of a tenant who operates a franchise from the premises will often request from a landlord. Such a franchisor waiver typically requires the landlord to notify the franchisor of tenant defaults, to allow the franchisor to cure defaults, and to allow the franchisor to assume the lease following a tenant default. While such lenders and franchisors aren’t liable for a tenant’s default, they do have an interest in a tenant’s property and/

or business that might cause them to wish to prevent a lease termination following default. If any such third-party agreements were signed, a landlord should review them carefully and notify the third parties of a tenant default.

Until the moratorium on eviction proceedings expires or is lifted, commercial landlords should also explore additional remedies available outside of an eviction proceeding to address tenant defaults. If the tenant provided security for its obligations under the lease, whether as a cash security deposit, letter-of-credit, UCC security interest or otherwise, the landlord should consider if and when it wants to resort to such security. Next, the landlord may be entitled to terminate the lease without the necessity of commencing an eviction action which could “raise the stakes” for any tenant wishing to resume operations following the COVID-19 emergency. Finally, there may be other remedies provided in the lease, at law or in equity to remedy a tenant default outside of an eviction proceeding.

The COVID-19 emergency has had, and will continue to have, significant impacts on commercial lease arrangements between landlords and tenants across New York. Lease disputes are likely to increase as our commercial sector begins to reopen, causing landlords and tenants to examine and explore their legal rights, obligations and remedies. Both sides should take the time to prepare.

John A. Anderson is a partner and leader of the Real Estate practice at Harter Secrest & Emery LLP. He can be reached at jander-son@hselaw.com.