

Guide for Business Tenant and Commercial Landlord Relationships During COVID-19 Crisis (prepared 4-5-2020)

This guide is intended to suggest communication methods and create awareness between business tenants and commercial landlords during the COVID-19 Crisis. This guide was prepared from multiple sources including the CCIM Institute, law firm websites providing guidance to parties involved in commercial leases, and interviews with local landlords.

On April 1, 2020 the Wall Street Journal reported that \$81 billion in rent payments were due in the United States, so please understand that this is a concern for many and the situation is still evolving. Now more than ever, the need for tenants and landlords to **communicate**, and **continue to communicate**, is vital and necessary.

It is important that tenants and landlords **have a process** established through communication, to make quick and informed decisions. These processes are necessary to deal with relationships between tenants and landlords, tenants and lenders, and landlords and lenders.

Tenants need to **document the impact** of COVID-19 on their business today, **gather and track important financial information**, and prepare to show what their business will look like on the back end of this crisis so that **assessments of continuing viability** can be discussed. This tenant information becomes critical in helping landlords understand what the situation looks like upstream in the relationships with their lenders. With the same high degree of urgency, the FDIC is communicating guidance to lenders to prepare responses for landlords who will not be able to make building mortgage payments due to business failures, thus further demonstrating that we are all in this together.

Not every tenant is in the same situation, so it is important for tenants and landlords to speak frankly about whether an individual's situation is a **short-term cash flow issue OR major overall risk that ends in rapid failure** of the business. Landlords may only have limited ability to not accept rent payments, so preserving that ability for those businesses in the worst shape and dealing with the immediate threat of not existing is an important consideration to keep our local economy intact through this crisis.

About Leases

Every lease is different. It is important for tenants to understand the provisions of their lease before asking their landlord to consider a response to the impact of the COVID-19 situation. Take time to understand, for example, provisions regarding interruption or stoppage of services, casualty, and what responsibilities are considered under landlord control or tenant control. Tenants should begin to narrow down what "help" for this situation really means relative to specific provisions of their lease.

How Landlords Can Respond

As businesses across the country close, if it has not happened already, it is only a matter of time before tenants approach landlords about negotiating rents. When a business closes suddenly, even if it's temporarily, the tenant may not be able to produce rent, meaning a landlord may have difficulty paying a mortgage (if there is one). There are no winners in this situation. Here are some viable alternatives to mitigate this issue:

- **Rent Reduction.** The landlord can reduce the tenant's rent for a portion or all of the term left on the lease. The usual forms of rent reduction are to reduce the base rent, operating expenses, or both. In regard to retail, it is possible to convert base rent to percentage rent.
- **Rent Deferral.** In this case, the landlord can defer a portion of the tenant's rent but would require them to repay the rent deferred at a later time, either in a lump sum or by increasing subsequent payments. A variation of rent deferral could be to cap or set a base year to operating expenses for a short or extended period of time.
- **Rent Abatement.** If a tenant is significantly past due on rent payments, a landlord may agree to forgive a certain amount of the past due rent if the tenant remains current thereafter.
- **Loan Conversion.** Rather than abating past due rent, a landlord may agree to convert the past due rent into a loan payable over time. The tenant would, however, continue to pay the current rent. The loan is then evidenced by a promissory note that is cross-defaulted with the lease.
- **Application of Deposit.** If the landlord holds a deposit, this amount could be credited against the tenant's current obligations.
- **Subletting.** Bringing in a new tenant (for part of or all of the rented space) could reduce or eliminate the rent obligations while replacing revenue for the landlord.
- **Franchise Credits.** Franchise tenants may be different than mom & pop tenants. Franchise parent companies may provide relief by crediting recurring franchise royalty payments in response to this crisis. Inquire with the franchise tenant about how their parent company is providing relief and consider a similar or complementary mitigation response to address the tenant situation.

How Tenants Can Respond

Be prepared to communicate with landlords by providing detailed information about the current status of your business and any efforts you have already made to access federal or state sources of COVID-19 financial relief. Frame your communications with the understanding that landlords are not motivated by the COVID-19 situation to hurt tenants, and good landlords all understand that it is more expensive to lose a good tenant than it is to work through the challenges of this situation.

- Review your lease to see if your rent is simply base rent or it includes pass-through expenses. How much are these expenses and are they set to increase?
- When does your lease end? What renewal options are available?
- What constitutes a default of the lease? What tools are available to the landlord in such a case (penalties, eviction, interest, etc.)?
- Does your landlord hold a security deposit? If so, how much is it?
- Review operating covenants and co-tenancy.
- Speak to your insurance agent to see what coverages are maintained by each party. Know your options to file a claim under existing insurance.

- Does the lease include force majeure, excusing a party's performance due to outside circumstances?
- Explore governmental relief programs, which may be popping up quickly, for tax relief, access to loans, relaxed restrictions/regulations, etc.
- Consider consulting a lawyer to know your options in limiting your financial obligations.
- Based on our current financial position, understand what concessions you would need from your landlord in both best- and worst-case scenarios related to COVID-19.
- Contact your landlord and specifically outline how your business is being impacted by the COVID-19 pandemic. Arrange an appointment and be prepared with data to have an open conversation to identify a solution or combination of solutions.
- Assess and re-assess the situation. Set up follow-up appointments as needed with your landlord, and do a check-in just before the next month rent payment is due.

Ratification of Negotiated Terms

Finding creative and practical solutions to weather this storm is critical, and in many cases these solutions may be substantial. Both tenants and landlords should be prepared to ratify the negotiated terms of these solutions accordingly so that both parties are protected from future claims by others in the future. Any ratification should be memorialized 'in writing'. Misunderstandings through phone calls (or even misinterpreted emails) could cause unwanted issues between landlords and tenants.