

Issues To Consider Before Withholding Rent

As commercial tenants face a crisis in managing cash and juggling their financial obligations as the result of the COVID-19 crisis, one of the major expenses they may consider not paying is their rent. Rent is usually one of the largest financial obligations of any commercial tenant. Before deciding to withhold rent; however, we suggest a commercial tenant perform the following reviews and considerations:

1. Review Your Leases.

- a. Confirm whether there are any notice and cure periods for a missed payment before your non-payment constitutes an Event of Default.
- b. Review the force majeure provisions in your lease. It is not likely that they will apply to the payment of money, but you should confirm. Should the force majeure provision apply to the payment of rent, and should the definition of force majeure include a situation like the COVID-19 pandemic, a delay in the payment of rent due to a force majeure reason would be excused during the duration of the force majeure event.
- c. Confirm what consequences exist should you fail to pay the rent, in addition to “normal” remedies of termination and the like. Note that Texas law allows a landlord to “lock out” a tenant from its premises for failure to pay rent (subject to delivery of certain notices). Other issues include whether there is a corporate guaranty of the lease and whether the lease is cross-defaulted with any other lease. For significant leases, it may be wise to engage local counsel to confirm the remedies under the lease.
- d. Review the ancillary rights under your lease, such as renewals, expansions and the like. Confirm whether these rights may be forfeited if you go into default (even if the default is subsequently cured).

2. Loans.

Review your loan documents and guaranties (and franchise agreements, if applicable) to ascertain whether failure to pay Rent when due will breach any covenants or trigger liability under any “bad boy” guaranties.

3. Business Interruption Policies.

Review your business interruption insurance. While most business interruption insurance policies exclude damage “resulting from” a virus, it is prudent to confirm the actual terms of your policies. Depending on how the policy is drafted, there may be some coverage. Moreover, the currently existing exclusions of COVID-19 from business interruption coverage are being contested in multiple jurisdictions. For example, at least one suit on coverage for business interruption has been filed in Louisiana and legislative efforts to ban the virus exclusion are moving to the Senate in New Jersey and are under consideration in multiple other jurisdictions.

4. CARES Act.

Review the CARES Act (the newly enacted federal legislation) and apply for all assistance to which you may be entitled. A landlord will want to know that before you are asking the landlord for relief, you are doing all that you can to obtain available financial assistance. (See a summary of the lending provisions under the CARES Act at www.munsch.com.)

Once you have completed these reviews, we recommend that you reach out to your landlords. Many landlords are amenable to some concept of rent restructure or deferral, though it is certainly on a case by case basis. Communication will be far-better received by landlords than just a defaulted rent payment.

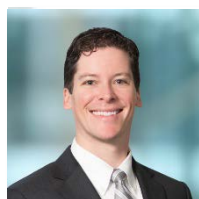
- Be prepared to provide information to the landlord in connection with any such request. Many landlords are requiring receipt of a “questionnaire” regarding the tenant’s business, financials and the like.
- Be prepared to ask for what you want. One of our landlord clients recently received a very well-written, short amendment that essentially requested X% rent deferral for April, May and June, with the amount to be repaid as “additional rent” over the 12 months of 2021. The amendment was so simple and reasonable, that the landlord client signed it, virtually as written.

The bottom line is that most tenants are in similar circumstances these days, doing their best to minimize expenses wherever possible in order to manage cash flow, maintain their employees and stay in business. We believe that landlords are most likely to work with those tenants who are honest, forthright and present a well-reasoned proposal or the landlord’s review.

Munsch Hardt Kopf & Harr is continually monitoring leasing and tenant developments related to COVID-19 and will send out additional information as pertinent updates occur. In the interim, please contact Kitty Henry if you have any questions or need any additional information.



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