

Retail Tenants – COVID-19 Implications for the Landlord/Tenant Relationship

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Among the businesses most adversely affected by the COVID-19 pandemic are many retail tenants that have had to close for significant periods and have experienced a significant decline in customer traffic. At the same time, their landlords have also experienced negative impacts to their cash flow but still have to meet their financial obligations to their lenders and others. As a consequence, the relationships between tenants and their landlords are under considerable strain, and the discussions between them can quickly turn adversarial. Turning to litigation solutions may not be the best or most cost-effective response. The following addresses some considerations that retail tenants should keep in mind as they engage with their landlords to mitigate some of the financial impacts resulting from COVID-19.

The first step for tenants intending to discuss modifying their contractual obligations is to review the actual lease. One should expect the landlord to be very knowledgeable about the provisions that govern a tenant's legal rights — both because the lease is likely based on the landlord's preferred form and because the landlord has been having many conversations with other tenants on similar issues. The tenant's representative should be as familiar with the provisions that will impact the parties' negotiations as the landlord. Among the provisions a tenant should review are:

- Rent payment provision – Is it an absolute provision requiring payment regardless of other circumstances? Does it waive the tenant's rights to "set off" amounts the landlord may owe the tenant against amounts owed to the landlord?
- Force majeure or disaster provision – Force majeure is a legal concept referring to an event that can excuse or provide more time to perform an obligation that is disrupted due to a superseding event — in this context, the consequences of a pandemic, government regulations, or supply chain disruptions that make it extremely difficult or impossible for a tenant to perform a specific obligation.

- Landlord's insurance obligations – Does the lease require the landlord to maintain business interruption insurance or reference the possibility/option? While insurance coverage litigation based on pandemic impacts is in its early stages, several courts have determined that coverage exists. If the landlord can secure insurance relief related to a tenant's obligations, the tenant should also benefit.
- Landlord's lease obligations to the tenant – Has the landlord satisfied all the obligations owed to the tenant under the lease at issue? The usual provisions that come into play involve exclusive rights, co-tenancy requirements, landlord maintenance obligations, and provisions allowing for full access or quiet enjoyment.

The next step will be to get a better understanding of the landlord's perspective and what is most important to it. How many vacant storefronts are there? Are most of the other tenants still closed for business? Are there any indications that the lender is going to step in? Is the landlord flexible or inflexible (which can be the product of the landlord's loan documents or its preferred business methods)? Is the landlord part of a large corporation or is it owned by an individual/family? Is the tenant's presence important to the landlord complying with co-tenancy obligations for other tenants? Learning as much as possible about the landlord will help a tenant determine how its specific request will be received and may help it tailor the request for accommodation to those items to which the specific landlord is more likely to consent.

Next, the tenant should determine what it is requesting and how best to structure its request. Is the tenant seeking rent abatement or rent deferment, or both? Can the tenant offer anything that would be of interest to the landlord, such as surrendering an exclusive, waiving a co-tenancy requirement, or electing an option period in advance of a future deadline? If the tenant is seeking a significant rent adjustment, is there a way to structure it so that the landlord can participate in the tenant's upside possibilities if things return to normal or the tenant's business model favors the post-pandemic world that is coming? If possible, the tenant should look for ways to make the negotiation a win-win where both have the possibility of an upside down the road.

Finally, when it comes time to have the discussion with the landlord, knowing the personalities of the various landlord representatives and knowing who is the ultimate decision-maker can play a significant role in the negotiations. The tenant's proposal should never lose sight of the landlord's interests — tailoring the request to meet the landlord's critical concerns will improve the chances of success. Ultimately, the landlord has to believe that the tenant's proposal is in its best interests even if the only benefit is keeping a tenant instead of having to market another open space (at a time when there is likely to be significant retail space coming on to the market). Do not underestimate the value of making a human/emotional connection. While a landlord may still reject a tenant's request, it will always be harder when the landlord knows that the tenant has done everything it could to turn things around and/or personally likes the tenant representative.

In conclusion, there are a few universal principles that will govern a conversation between a tenant and a landlord concerning COVID-19 impacts. Each conversation is likely to be unique based on the personalities involved, the parties' contractual rights, the economic realities of the tenant's business, and the particular impacts to the geographical area where the retail center is located. Ultimately, in the discussion with the landlord, the tenant will need to answer the question of why the tenant's proposal is in the best interests of the landlord.

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