

Considering Lease Concessions in the Face of a Tenant Bankruptcy

June 16, 2020

Landlords are receiving a deluge of requests to provide rent relief to commercial tenants whose operations have either been closed or substantially restricted as a result of state and local governments' COVID-19 stay-at-home orders and related restrictions. Some tenants are using the threat of a bankruptcy filing as leverage to obtain these concessions. Meanwhile, landlords are facing their own challenges with mortgage lenders and servicers as they try to service real estate loans with limited available cash.

Landlords should understand the significance of the bankruptcy threat. The most significant shift in negotiating leverage resulting from a bankruptcy is the tenant's right under the Bankruptcy Code to assume, assign or reject leases. Pre-bankruptcy, the landlord is entitled to terminate a lease in response to a tenant default; however, the tenant continues to be bound by the terms of the lease. Post-bankruptcy, it is now the tenant and not the landlord that holds the power to elect whether to assume (keep), assume and assign without landlord consent or reject (terminate) a lease. This shift gives the tenant the leverage to use bankruptcy and the threat of either rejection as a bargaining chip to negotiate for concessions. However, a tenant cannot use the bankruptcy to modify lease terms without landlord consent.

When the tenant comes knocking, a landlord should first consider whether it wants the space back, or the tenant to remain in possession (for example, if the location will be difficult to re-let). The former could make sense where a bankruptcy assignment is a greater risk because the location is highly desirable, the lease is under market, there is significant term remaining, a redevelopment opportunity exists or there is a broad use clause. The presence of these factors may make the lease more marketable for assignment in bankruptcy. By declining a tenant's request for concessions, the Landlord may increase the likelihood that the lease will be rejected if the tenant were to file for bankruptcy. The landlord can then retake possession of the premises.

Another important consideration is the financial condition of the tenant, including the economics of the premises. If the location was highly profitable prior to the COVID-19 shutdown or critical to the tenant's business operations, then it is more likely that the tenant will remain without the requested concessions even if, for other reasons, a bankruptcy filing were to occur days when the tenant is not open and operating (and, thus, not generating sales).

There are ways to manage the threat of a tenant bankruptcy when negotiating lease modifications. However, as a threshold matter, the landlord needs to decide whether it wants the tenant to stay or go.

This piece was originally written for and published in The Anton Group June 2020 Newsletter. [Click here to view the full newsletter.](#)