

Legal Corner

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Tenants in Common - National Retail Tenants Association

Editor's Note: *Legal Corner contains case summaries and analysis of recent court decisions that impact retail leasing and lease administration. These summaries focus on the leasing issues covered in each case and do not include detailed discussions or analysis of the procedural and peripheral issues in the cases.*

Is a Liquidated Damages Clause Enforceable?

Rue21, Inc. v Los Lunas Inv'rs, LLC, no. 18-CV-715, 2019 WL 1375405(W.D.Pa. Mar. 27, 2019). Landlord executed a letter of intent with a fashion retailer tenant in 2015 for a store in New Mexico. Approximately one year later, the parties entered into a lease. The lease required Landlord to deliver Tenant possession before July 10, 2016 (the "Target Delivery Date"). The store was not delivered to Tenant until 84 days after the Target Delivery Date on September 29, 2016 (the "Actual Delivery Date"). Tenant advised Landlord that as a result of the delay, it would apply a credit in the amount of 755 days of rent to the first payments of rent due under the lease based on the following language in the lease, which Landlord in turn claimed was an unenforceable liquidated damage clause: "*Tenant shall receive five (5) days of abatement of Minimum Rent and Other Charges due under the Lease for each day the Actual Delivery Date is delayed past the Target Delivery Date. If the Actual Delivery Date is not delivered (sic) to Tenant within fifteen (15) days after the Target Delivery Date, then beginning with the sixteenth (16th) day after the Target Delivery Date and continuing from each day of delay thereafter, the Late Delivery Credit shall increase to ten (10) days of abatement of Minimum Rent and Other Charges for each day of delay.*" Liquidated damage clauses are provisions in contracts that fix the amount a party can recover as a result of a breach of the contract by the other party. Under New Mexico law, which the parties agreed in the lease would govern, liquidated damages clauses are generally enforced under the principles of freedom of contract with enforcement of the clauses generally only being denied if the amount is "*so extravagant or disproportionate as to show fraud, mistake or oppression.*" The court in this case did not find proof or allegations of fraud or oppression. Similarly, the court found that there was no mistake because the same liquidated damages provision was in the letter of intent and the lease. Landlord's argument that the liquidated damages were extravagant or disproportionate because they equaled over 25 months of rent for delivery that was 3 months late was rejected by the court that reasoned that Landlord could control the amount of damages because they were based on a credit for each day of delay and could have been anticipated at the time the lease was signed. Landlord's counsel also argued that typical damages for late delivery in New Mexico retail leases is a "*maximum of 2 days' credit for each day or delay during an initial period and 3 days of credit for each day of delay thereafter.*" The court was also unpersuaded by

this statement because there was no evidence that Landlord tried to negotiate for such lesser damages before lease signing. Landlord's argument that the increase in damages after 15 days was punitive was also rejected by the court stating that question is whether the damages clause as a whole is enforceable and that the court should not be parsing the provision and re-writing the contract for the parties. The court went on to state that its determination should end once it determines whether the clause is extravagant or disproportionate as a whole.

Is a Change of Control Deemed an Assignment in Hawaii?

Coggins v. Kona Seaside, Inc., 143 Haw. 102, 423 P.3d 421 (2018).

Landlord owns and leases a portion of its real property to a Tenant corporation for the operation of a restaurant. The lease states that "if the restaurant is sold by Tenant from September 1, 2011–August 31, 2016, Landlord shall receive 40% of the gross selling price." In addition, the assignment provision of the lease states that "[Tenant] shall not assign this lease, or any interest therein... without the written consent of [Landlord]... This lease shall not, nor shall any interest therein, be assignable, as to the interest of [Tenant], by operation of law, without the written consent of [Landlord]." In 2014 Tenant's shareholders executed an agreement to sell all of their stock in Tenant to third parties. Upon learning of the agreement, Landlord sent a letter to Tenant requesting information on the sale so it had information to determine whether it would consent to the assignment of the lease and stating that it expected to receive 40% of the gross selling price of the restaurant. Tenant argued that the sale of stock was not a sale of the restaurant and that Landlord had no claim to any portion of the gross selling price. The court examined whether the sale of the stock of Tenant (1) constituted a sale of the restaurant thus requiring the shareholders of Tenant to pay a portion of the gross selling price to Landlord; and (2) without Landlord's consent was a violation of the lease. The court explained that the shareholders of Tenant are not parties to the lease because the Tenant corporation is a separate and distinct legal entity from the Tenant corporation's shareholders and as such, the shareholders do not own the assets or the property of the Tenant corporation. The court found that the shareholder's sale of their interests in the Tenant corporation was not a sale of Tenant's assets or a sale of the restaurant and that after a sale of the shareholder's stock, the Tenant corporation would still be the owner of all of the Tenant corporation's assets and would be responsible for Tenant's contractual obligations. The court further stated that Landlord's presumption that it is entitled to a portion of the proceeds from the sale of the shareholder's interest in Tenant amounted to a presumption that Tenant's execution of the lease bound the shareholders of Tenant as individuals. The second issue was a matter of first impression for Hawaii and the court determined that it would follow the general rule that a shareholder's sale of the stock of a corporation, even if that sale is of a controlling interest in a tenant corporation, does not constitute an assignment of a lease unless the lease explicitly provides to the contrary. Since Landlord did not include a provision in the lease stating that a change of control of Tenant constituted an assignment under the lease, the shareholder's sale of stock would not violate the assignment provision of the lease.

Did a Landlord's Purported Termination of Lease Terminate an Option to Purchase?

Siarah Atlanta Hwy LLC v. New Era Ventures, LLC, 350 Ga. App. 59, 828 S.E.2d 4 (2019). Landlord owns commercial property that it leased to Tenant. The lease granted Landlord the right to terminate the lease by “*providing Tenant with thirty (30) days written notice.*” The lease also granted Tenant an option to purchase the property by giving Landlord notice of Tenant’s election to purchase “*at least ninety (90) days prior to the date of closing.*” Tenant paid Landlord \$175,000 for the option to purchase. On January 27, 2017, Tenant sent Landlord notice that it would exercise the purchase option scheduling a closing for May 12, 2017, more than ninety (90) days after the date of the notice. On the same date, Landlord sent Tenant notice that it was terminating the lease and demanded possession within 30 days. On February 17, 2017, Landlord’s counsel informed Tenant that Tenant’s exercise of the option was not sufficient because the option expired on January 31, 2017. Tenant’s counsel responded that the notice was sufficient. Prior to the scheduled closing date, Tenant’s counsel notified Landlord of the date, time, and location of the scheduled closing and indicated further that Landlord’s failure to confirm by a date certain that Landlord intended to convey the property to Tenant, would constitute Landlord’s intention not to accept tender of the purchase price at closing. Landlord’s counsel then reiterated that the lease terminated, Tenant needed to vacate and that “*This was a waiver of tender, and under the law relieved Tenant of any obligation to tender.*” Landlord contends that it terminated the lease and as a result, Tenant’s option to purchase terminated. The court did not agree, stating that the lease stated that Landlord’s termination would not be effective until 30 days after the date of Landlord’s notice of its intent to terminate, or February 26, 2017, and Tenant properly exercised the option to purchase on January 27, 2017, before the termination became effective. The court also rejected Landlord’s argument that Tenant was required to actually purchase the property before January 31, 2017 for the option to be validly exercised, reasoning that Tenant complied with the terms of the lease which only required notice within the option period for a closing scheduled at least 90 days later and stated that nothing in the lease required that the closing occur within the option period. Landlord also argued that Tenant was required to tender the purchase price prior to exercising the option. The court rejected this argument because “*an option to purchase can be exercised without the payment of the purchase price, or the tender thereof, unless the option contract provides for such payment as a condition precedent to the exercise of the option,*” and the lease did not require such payment. In the alternative, Landlord argued that under Georgia law, tender of the sale price was a pre-requisite for a buyer obtaining specific performance. However, the court pointed out that the law does not require tender as a pre-requisite to specific performance if rejection of tender is deemed likely and that given the communications between Landlord and Tenant, it was clear that Landlord would have rejected the tender. In addition, the court found that Landlord’s termination of the lease was ineffective because before the termination took effect, Tenant’s position changed from tenant to a purchaser in possession and occupied the property as a party under a contract to purchase the property and not as a tenant. Therefore, Tenant could not be dispossessed and the lease could no longer be terminated because there was no landlord-tenant relationship or tenancy for Landlord to terminate. The court held that Landlord was entitled to some funds for Tenant’s occupancy of the property after its exercise of the option to purchase, but any breach of contract damages owed to Tenant could reduce such amount. Ultimately, the court granted the remedy of specific performance of the sale of the property to Tenant.

