

# PUBLICATION

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## A Landlord's Guide to Landlord's Waivers: Five Potential Pitfalls For Landlords to Consider [Ober|Kaler]

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**Tenants, in the course of obtaining financing, often ask their Landlords to sign a Landlord's Waiver. Landlord's Waivers are intercreditor agreements for the benefit of the tenant's lender or equipment lessor, stipulating the landlord's and the lender's respective rights in certain property owned by the tenant. Such Waivers are deceptively simple documents, which may be only a page or two long and contain non-technical language, but nevertheless can present unforeseen problems for the landlord.**

Until recently, the scope of the typical Waiver was narrow. It was intended to affect a waiver only of a landlord's State statutory or common law lien rights (lien rights vary considerably from State to State). Landlord lien rights typically allow a landlord to obtain a lien or springing lien on the tenant's property in the leased premises to assist in the collection of delinquent rent. In some instances those liens could be superior to a lien created by a security interest in favor of the tenant's lender. Often, the lender would have provided financing for the tenant to purchase inventory or certain equipment and would require that its purchase money security interest in those items be superior to any statutory or common law lien available to the landlord.

Waivers in use today, however, are often not confined to purchase money security interests in inventory or specific equipment. Moreover, Waivers are often sought in a variety of circumstances, including highly leveraged financings where the lender's collateral has not been acquired with proceeds of the loan. These Waivers are often not limited to identifiable items or classes of the tenant's property, but rather attach to "all present and future property of the tenant". These broader Waivers, in particular, present the landlord with the following potential pitfalls, among others.

### Description of the Collateral

Ideally, the lender's collateral, which is the subject of the Waiver, would be limited in scope and easily identified. A landlord would not want to be faced one day with trying to figure out which assets of the tenant are or are not available to the landlord. But, what if the Waiver applies to "all present and future property of the tenant". Does that mean that the Waiver applies to everything that the tenant owns or will own? Does it apply to cash? And, does it mean that the landlord effectively has waived its right to recover anything from the tenant? This could present a significant issue for the landlord especially, as discussed below, if the Waiver applies to liens other than statutory or common law landlord's liens. In any event, the landlord should request that the collateral covered by the Waiver exclude the tenant's leasehold interest, sublease revenue, landlord financed tenant improvements and the tenant's interest in building service equipment or fixtures.

### Waiver vs. Subordination and Types of Liens Effected

Waivers, as their name implies, typically require that a landlord waive its lien rights as to the identified collateral. A landlord, however, would rather subordinate its lien to the lender's lien, as opposed to waiving its lien. Subordination would leave the landlord's lien intact, which may prove important for any number of reasons (e.g., the landlord would retain its ability to force a sale of the collateral, the landlord would be better off being a

secured creditor if the tenant files for bankruptcy and the landlord would have a superior position vis a vis other creditors of the tenant). While the lender may prefer that the landlord waive its lien, it may well accept subordination in lieu of waiver.

As noted above, Waivers were generally confined to specific statutory or common law landlord lien rights and not to, for example, judgment liens. Many waivers now, however, extend to any and all liens that the landlord may acquire. If the landlord waives all liens, the landlord may be unable to obtain a lien on the specified property of the tenant even if the landlord took the time to go to court and obtain a judgment against the tenant and levy that judgment on property of the tenant. If the collateral is all of the tenant's assets and the landlord waives all of its lien rights, the landlord could find itself in a position where it is unable even to attach the tenant's bank accounts after obtaining a judgment. This would make for a very unhappy landlord and would be particularly unfortunate if the financing related to the Waiver were not used by the tenant to acquire or refinance any of the collateral and/or if the financing caused the tenant to become overleveraged and contributed to the tenant's lease default.

These are core issues that the landlord may need to negotiate with the lender. If the lender is resistant to limiting the liens to be waived or limiting the extent of the collateral, the landlord may want to ask the lender "if I agree with your request, how can I ever collect any money from this tenant until you are paid in full?" If the lender's answer is "you can't", then the landlord might wonder whether it makes sense to execute the Waiver.

## **Period of and Limitations on Occupancy and Notice Obligations**

The lender will want a period of time during which it can enter upon the leased premises and either sell its collateral on site or remove the collateral for sale elsewhere. In addition, the lender will want to make sure that the expiration or termination of the lease, particularly if it is accelerated because of a default by the tenant, does not deprive it of its opportunity to do so. These reasonable desires of the lender can present a number of issues for the landlord, particularly in the context of a very lender-friendly Waiver.

Simplest of these issues is the period of the lender's occupancy. Lenders often request the right to occupy the leased premises for anywhere from 60 to 90 days but, depending upon the nature of the collateral and whether the disposition will be onsite or offsite, may accept a substantially shorter period.

A more difficult question is when the period of occupancy begins; because this question is usually tied to notification obligations of the landlord. If the tenant defaults under its loan before it defaults under its lease, the lender can elect whether and when to enter the leased premises and deal with the collateral. The lender, however, is concerned about the possibility that the tenant will default under its lease before it is in default under its loan. While the lender's loan documents may provide that a lease default constitutes a default under the loan, that isn't much help to the lender if it does not know about the lease default. Therefore, most Waivers require the landlord to notify the lender prior to terminating the lease. Some Waivers go further and require the landlord to notify the lender at the same time the landlord gives notice of default to the tenant or, in an extreme case, notice may be required whenever the tenant is not in compliance with any of the terms of the lease (irrespective of any notice and cure period and of whether the landlord was aware of the default).

Landlord notification obligations present several issues for the landlord, the most obvious of which is: What happens if the landlord forgets or otherwise fails to notify the lender - does the landlord incur liability for failure to send a timely notice? The landlord should attempt to limit its exposure expressly or by agreeing to use "reasonable efforts" to send notice. Similarly, the landlord would want to confine its notification obligations to those instances when it is sending the tenant a written notice of default or termination. The landlord may also

resist agreeing to give notice to the lender if the lease is expiring by its terms, as the lender should be capable of making a note as to when the lease is scheduled to expire.

The importance of the notice issue is hard to overstate. Not only is the landlord exposed to the possibility of lender damages, but if the landlord discovers after the lease has terminated or expired that it needs to allow the lender a 60 to 90 day period of time to control the leased premises, the landlord may be unable to deliver the leased premises to a new tenant on the date agreed to in that new tenant's lease.

There are other issues related to the lender's right of occupancy: The landlord should be certain that the occupancy is not exclusive so the landlord can simultaneously enter the leased premises to prepare the leased premises for the occupancy of the next tenant. The landlord may want to stipulate that the lender can only enter the leased premises while a representative of the landlord is present or only during business hours. Additionally, the landlord may want to prohibit the lender from selling the collateral at the leased premises. Or, if the lender can't accept that prohibition, at least provide guidelines for any on-site sale, including that the sale comply with applicable laws and park or business center restrictive covenants.

## Payment of Rent

If a lender occupies the leased premises during a period in which the tenant has failed to pay rent, it would seem reasonable for the lender to agree to pay the landlord for that privilege. Most lenders, indeed, do agree to pay rent, often at the lease rate, while they are in occupancy of the leased premises. While this is helpful, it may not adequately compensate the landlord.

For instance, if the lender agrees to pay rent during its period of occupancy and is allowed to occupy the leased premises for, say, 60 days after the landlord notifies the lender that the tenant is in default or the lease has been terminated, the landlord may think it is going to get rent for the period beginning with the notice and ending when the lender removes its collateral and leaves the leased premises. The lender, however, has agreed to pay rent only during the period in which the lender is actually in occupancy. In such a case, if the landlord gives the lender notice and 57 days later the lender enters the leased premises for three days, the lender is required to pay only three days rent, but the landlord has effectively lost the use of its leased premises for 60 days. To avoid this result, the landlord should request that the lender pay rent for the period during which the lender has the right to occupy the leased premises, rather than for the period of its actual occupancy of the leased premises. For instance, the landlord's version of the Waiver could provide that the lender must pay the landlord rent, beginning, say, five days after the lender has the right to enter the leased premises (to give the lender some rent free period to consider if it wants to incur the expense of preserving its occupancy right) and continuing so long as the lender retains that right. There are nuances involved in negotiating this issue with the lender, but typically the landlord and the lender can agree upon mutually acceptable language.

## No Further Obligation

The Waiver sets forth a number of specific rights that the lender will have with respect to its collateral. These rights should be sufficient to protect the lender. One situation the landlord does not want to encounter is the possibility that some of the lender's collateral remains in the leased premises after the tenant vacates and the landlord is uncertain of how it may dispose of that collateral to make way for a new tenant. For this reason, the landlord will want the Waiver to provide that any collateral remaining after the end of the lender's occupancy period will be deemed abandoned as far as the lender is concerned and the landlord may dispose of that collateral without any liability to the lender.

The number and nature of the issues raised by a Waiver are limited only by the particular provisions and language the Waiver contains. Those mentioned above are common to most Waivers. Whether or not the landlord executes a Waiver and what the landlord agrees to in the Waiver are primarily dependent upon the benefit the landlord anticipates to receive from the tenant's financing and the landlord's negotiating position. In any event, whenever a landlord reviews a Waiver it should read the Waiver carefully, consider the issues mentioned above and consider also obtaining the assistance of counsel.