Friday, October 26, 2018
9:00 – 10:15 AM

Peer to Peer 8

Remedies, Recoverable Damages and Creative Solutions: What You Want vs. What You Need vs. What You Can Get

Presented to

2018 U.S. Shopping Center Law Conference
JW Marriott Orlando Grande Lakes
Orlando, FL
October 24-27, 2018

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Clients sometimes present dispute scenarios that do not fit neatly into the "Default" box. Worse, a breach, violation, default, or "occurrence" may be clear, but the remedy provided in the lease may be much less than ideal. The litigation process presents its own uncertainties, expenses and delays. Participants in this "Peer to Peer" session will examine several dispute scenarios, common lease provisions and state law questions. We will then roll up our sleeves to confer and collaborate on Plan A, Plan B and Plan C solutions looking at the risks and benefits that each might afford, what can be reasonably achieved and managing expectations.

I. Special Defaults and Remedies

There are many violations of the lease that are not appropriately addressed in the general defaults and remedies clause of the lease. For example, the violation might be caused by events that may not entirely be within the control of either party—so it cannot truly be viewed as "default" of one of the parties, but the event is so dramatic that remedies must result—such as co-tenancy violations. Or the violation might require a faster cure than the standard of 30 days, such as violation of the Protected Area. Or the violation may not be susceptible to any cure and is not material enough to justify lease termination, but requires some type of remedy that will discourage repeated action, such as violation of operating hours. Or the violation may be one for which traditional remedies are not adequate, such as co-tenancy violations. This section will explore those special defaults and remedies in depth.

A. Delayed Delivery

The landlord's failure to deliver the premises and satisfy the delivery conditions can have a dramatic effect on the tenant. Merchandise may need to be redirected to another store (resulting in an overstocking of product at that other store) or put on sale immediately due to product cycles. Construction contractors may need to be rescheduled, triggering penalties in the construction contracts and creating uncertainty as to whether the contractor will be available when delivery is eventually made. Marketing events and ad buys may need to be rescheduled or terminated. Salaried employees for the store may need to be paid even if the work for which they were hired has not yet materialized. And, most critical, sales would be lost—a particularly bitter pill to swallow if the retailer has included the store in its disclosures to Wall Street or private investors.

Remedies for late delivery are typically liquidated damages based on a certain number of days of rent for each day of delay. Tenants who have only a few opening days each year may instead negotiate for a lump sum payment. Many tenants bargain for the right to terminate for late delivery, often with a cure period of several months. The key issue in determining the late delivery fee is ensuring that the liquidated damages are reasonable and not a penalty. The clause should confirm the uncertainty of actual damages and a bona fide attempt to place on a reasonable value on the delay. It should also avoid references to a "late delivery penalty" or other intentional suggestions that the remedy is punitive.

B. Opening/Operating Covenant

The very definition of a successful shopping center takes 100% occupancy (or close to it) for granted with each store fully stocked open and operating with a full complement of staff. Is there an operating covenant? The tenant's lease gives the tenant a possessory interest in the subject property or premises, but the tenant does not have an obligation to be open for business or remain open for business unless the lease so states. The obligation to open is an "opening covenant" and the obligation to operate and remain operating is known as an "operating covenant." It may be perpetual or be limited and it is important to understand the ramifications and potential consequences of those provisions in a lease or the lack thereof. For instance, what are the landlord's rights if a tenant closes its doors—"goes dark"? If the answer is that the tenant did not have an operating covenant, then the failure to operate is not a default and the landlord has no remedy. If the lease does contain an operating covenant, but does not specify the remedy, the landlord could be stuck in the unenviable positon of having no effective remedy to compel performance. The only way the landlord might be able to have a functioning location is to replace that tenant. Some leases provide landlords with the right to seek a mandatory injunction, but historically, it has been very difficult to get courts to enforce them. If the tenant closed its doors because it was cheaper to pay rent on a dark store than to operate it or if the tenant simply has insufficient resources and is also in monetary default, an injunction forcing the tenant to re-open or stay open may not be helpful unless the landlord has other reasons for wanting a tenant to remain open, such as satisfying the landlord's cotenancy requirements in other leases.

1. Commencement and ongoing operations

The obligation to open and operate is a hotly negotiated term of a lease. Savvy tenants think of avoiding an operating convent as part of an "exit strategy." A tenant may covenant to at least open and/or to remain open

for some limited amount of time in order to give a landlord some comfort since it is unlikely that a reputable tenant would go to the effort and expense of opening, only to close shortly thereafter. However, circumstances change and a landlord could be left with a closed store and the potential of triggering a cotenancy situation. Certainly, a tenant allowance would not be paid (or completely paid) unless the tenant has also opened. It is common for a landlord to bargain for the right to recapture a dark space, but that may not be a good remedy if the landlord has a significant economic investment that has not been fully amortized. A landlord in negotiating the lease should attempt to negotiate for reimbursement of the unamortized potion of any tenant allowance if a recapture right is exercised.

2. Contingencies giving rise to right to close or delay opening

A tenant may negotiate as part of its own remedies, the right to delay opening until such time as a landlord has met some of its other obligations such as achieving a certain level of occupancy or obtaining a certain number of specified anchor leases. A tenant may also have the right to open but not the obligation to pay full rent until those conditions are met.

C. Exclusives

Exclusive or protected use clauses are among the key provisions that are specially negotiated at the outset of the lease. They present multiple challenges in drafting, because landlords and tenants have very different objectives and because the concepts and measurements must be expressed carefully in the words used. Tenants seek such clauses to provide some measure of protection against competition, and while landlords are often willing to provide *some* protection, they also seek to preserve as much flexibility in future leasing as possible, to maximize their ability to create the most advantageous tenant mix at the shopping center. So the key issues in drafting exclusive clauses are crafting clear, unambiguous definitions of what kind of use or business is being protected (sale of specific merchandise, brands, or items), and how to measure what is an acceptable or unacceptable use by a competitor (percentage of sales or floor area). Counsel drafting such clauses must think around corners into the future, envisioning scenarios from the perspective of the opposing party, and use language and diction that is as clear, specific, and definite as possible.

Realizing that even the best drafted exclusive use clauses create obstacles to leasing, landlords often negotiate for limitations on scope and duration of exclusive use clauses. Such covenants can cause the exclusive protection to end after a specified period of time, or perhaps be bargained away when a lease is amended or extended. Landlord's counsel also seek limitations on the exercise of remedies, including rights to notice and an opportunity to cure, especially in the case of a "rogue tenant" that might be violating its own covenant to respect existing exclusives in the shopping center. Since landlords are often unaware of whether any given tenant is honoring its exclusive use obligations at any particular time, well drafted exclusive use clauses ensure that the landlord is provided some specific notice of any alleged violation and a reasonable opportunity to bring a violating tenant into compliance before any remedy may be exercised.

Exclusive use clauses also typically feature negotiated remedies for violation, and careful drafting of such remedies is also essential to ensure that both sides understand their rights and obligations under the clause. Because it can be difficult to prove actual damages resulting from a breach, landlords and tenants sometimes negotiate for a liquidated damage provision to fix a measure of damages in the event of a breach. Such provisions, especially if designated as an *exclusive* remedy for a breach, have advantages for both sides, because the consequences of breach are known, allowing the parties to account for the risk of such remedies in making future leasing decisions. Some remedies are drafted to be only prospective, such as a right to pay a reduced rent going forward, requiring the tenant to exercise the remedy in order to avail of it. These remedies reflect a balance of risk and remedy for both sides, by providing a clear remedy for the tenant, but avoiding big surprises to the landlord. In all cases, drafting remedies carefully, to avoid disputes and litigation, should be a paramount objective for both sides.

D. Co-Tenancy

The central purpose of the co-tenancy provision is to ensure that the shopping center's co-tenancy is as anticipated by the tenant when it entered into the lease. Specifically, the concept is that the tenant would not have agreed to pay the rent stated in the lease, or might not have even entered into the lease, if a certain co-tenancy threshold is not met. That co-tenancy threshold typically requires a certain number of department stores (e.g., 2 of the 3 department stores at the shopping center) to be open, of which one or two named department stores must be open in the location shown on the site plan attached to the lease, plus a certain percentage of the balance of the shopping center (e.g., 85%) to be open, and possibly a certain number of named stores to be

open. The named department stores are determined by a variety of factors, including traffic draw, proximity to the tenant's premises, consistency with the tenant's customer base, and existence of complementary uses.

There are 3 types of co-tenancy provisions: delivery co-tenancy, opening co-tenancy and ongoing co-tenancy. Delivery co-tenancy requires that certain co-tenants have signed leases and are under construction, or that other co-tenancy are met requirements, prior to the tenant's obligation to accept delivery of the premises. Remedies include the right to delay taking possession, and possibly the right to terminate with some form of liquidated damages.

The opening co-tenancy typically requires that certain co-tenancy conditions are met upon the tenant's opening (or the expiration of the tenant's construction period). Remedies include the right to delay opening, or opening at reduced rent until the opening co-tenancy is met, or possibly the right to terminate with some form of liquidated damages. For new shopping centers, the opening requirement occasionally contains a lower threshold than the ongoing co-tenancy, with the idea of getting the tenant open, albeit on reduced rent.

The ongoing co-tenancy usually gives the tenant remedies if certain co-tenancy conditions are not met, including reduced rent, the right to close, or possibly the right to terminate with some form of liquidated damages.

Is the reduced rent in reality a form of liquidated damages? Given the purpose behind co-tenancy, the better view is that the reduced rent is merely the rent that the tenant would have paid if the tenant were bargaining for a shopping center that did not meet the co-tenancy threshold. This is particularly true if the reduced rent is automatic, and not a right that must be elected, although that is not necessarily determinative of liquidated damages. However, a prudent retailer will attempt to ensure that the rent reduction reasonably estimates the damages that the tenant may incur as a result of the lower co-tenancy.

Is the co-tenancy provision penal in nature if the tenant's sales do not decline as a result of the co-tenancy failure? Again, given the purpose behind co-tenancy, it should not be viewed a punitive, just as a landlord's request for percentage rent if the tenant is meeting certain sales thresholds should not be viewed as a penalty.

A key concern is addressing the evolving nature of the shopping center in the co-tenancy provision. Many tenants argue that department stores are necessary for the success of a shopping center. Indeed, the shopping center industry promoted this concept in the early days of mall development. Given the dramatic consolidation of department stores and the shrinking size of department stores from the 200,000 square foot behemoths of the 1980's, many landlords have argued that it is impossible for them to sustain strict department store requirements in co-tenancy provisions. Indeed, today some inline stores, big-box stores and movie theatres drive more traffic than some department stores. Replacement of a tired department store with a fresh mix of lifestyle retailers and restaurants can increase foot traffic as well. The challenge is to draft for the future of the shopping center which is not yet in focus, while retaining the tenant's need for the shopping center to meet the tenant's needs as a vibrant, attractive draw.

E. Radius

Radius restrictions may confine certain behaviors on the part of a tenant and/or the landlord. For instance, a tenant may be prohibited from opening another store within a certain proximity to the existing leased premises. Similarly, a landlord might be restricted from leasing to another similar use or to another prohibited use within a certain proximity to the tenant's location or to any adjacent property owned by the landlord or an affiliate. Parties have been known to create affiliates to avoid the reach of the particular lease language. Thus, it is important to define the parties to include affiliates and even to have Franchisors agree to these restrictions as part of the Addendum that a Franchisor might require. Where parts of a shopping center are actually owned by different entities, this issue is especially important as a part of the center could be sold to an entity that is not a party to the particular tenant's lease.

Also, the scope of the radius protection needs to follow a rule of reason and should be the subject of negotiation. Should it be phrased in terms of miles. Should it be of a limited duration or could it even be springing such that the radius only comes into being if the tenant ceases operating?

The remedy for a radius violation must also be negotiated. Older leases attributed the gross sales of the new store to the existing store. However, if the existing store's lease did not call for percentage rent, how would that even be a remedy. Surprisingly, some lawyers do not catch that when using form leases. Might injunctive relief be appropriate? How about increasing rent by a certain factor? Do liquidated damages make sense? How about a sliding scale of rent increasing depending on how close the new store is to the existing? How about a springing operating covenant?

F. Occupancy Transfers (Assignment, Subletting and Mortgaging)

Most shopping center leases have restrictions on transfers of the tenant's leasehold interests, including assignment, subletting, and mortgaging. The landlord's goal, embedded in many form lease provisions on this issue, is to preserve as much control as possible over the tenant mix at the center, and to ensure the best and highest quality tenants. The tenant's goal in negotiating such provisions is to obtain a reasonable measure of flexibility, to allow an encumbrance when needed, to provide options to assign or sublet should the lease turn out more or less successful than anticipated. In most cases, these competing goals result in a clause that restricts transfers except with the landlord's consent, often specified that it shall not be unreasonably withheld, and often with specific conditions listed for obtaining of consent. In this way, the landlord is held to an objective standard of reasonableness. Further, if no standard for giving of consent is specified, a standard of reasonableness will be implied, and any ambiguity in a transfer restriction will generally be construed in favor of transferability.

In some instances, if landlord has an overarching business reason to ensure a maximum level of control over occupancy of a particular space, a lease can lawfully prohibit transfer entirely, or provide a subjective standard of consent, allowing the landlord to refuse consent to a transfer in its own discretion – for good reason or no reason at all. The tradeoff for preserving this subjective right is that the landlord's remedies for a breach may be limited. For instance, in many states, a landlord may not avail itself of the remedy of keeping a lease in effect and suing for damages as they come due, unless the tenant is afforded a reasonable right to assign or sublet. Because occupancy transfers can present benefits of flexibility for both sides, most leases provide an objective standard for consent, perhaps with negotiated terms and conditions.

Of course, failure to adhere to such provisions can give rise to liability for breach of the lease. If a landlord fails to timely respond to a request for consent in violation of the lease, tenant remedies may include but are not limited to, the right to pursue contract damages for breach or the right to terminate the lease. Similarly, if a tenant transfers its interest in violation of a transfer restriction in a lease, landlord remedies include pursuing a claim for damages or terminating the lease, or both.

Whether a landlord's refusal to consent to an assignment or sublease is reasonable, is a common topic of litigation. From the landlord's perspective, controlling the real estate and profits derived from the leasehold estate are paramount. From the tenant's perspective, the ability to transfer the lease as part of a sale, restructure or exit strategy are equally important considerations. If the landlord withholds consent to a requested assignment or sublease, the tenant's remedy must be immediate so as not to lose the assignment or sublease prospect. The typical remedy of specific performance, which takes years to try, is an ineffective remedy.

G. Protected Area/No Build

The Protected Area (or No Build Area) is typically a portion of the common area adjacent of the tenant's storefront, show windows or exterior signs in which the landlord cannot permit interference with (a) visibility of the

tenant's storefront and signs, or (b) access to the tenant's entrances, or (c) parking for the tenant's customers. The Protected Area could prevent specific uses, such as fairs or car shows or even construction during holiday periods. It could also prohibit obstructions, such as kiosks or children's play areas or trees. It can even disallow construction staging and snow mounding. It is prudent to be as specific as possible if certain obstructions are permitted to remain, by referencing the locations of the exemption obstructions on a site plan or in sketches or even photographs attached to the lease.

The typical 30-day cure period for a non-monetary default is insufficient in this instance. The tenant is likely to feel the impact of the obstruction immediately and in most instances carts and displays can be moved in a matter of hours, not days, so the cure period, if one is offered at all, should be reflective of this reality. It is difficult to determine damages as a result of violations of the Protected Area provision. A decline in sales may be attributed to a lack of visibility or access as a result of forest of kiosks in front of the premises, but how much? Should the landlord's compensation from the kiosk be taken into account when formulating the damages? Care should be taken in crafting the remedy so that, if the remedy is determined to be liquidated damages, the remedy is not voided as a penalty.

H. Use Related Violations—Parking, Excessive Noise, Troublesome Odors

This category of default is considered nuisance issues and may be violations of the lese of the rules incorporated into the lease. They are less problems for the landlord than they are problems for other tenants in the center that become problems for the landlord because of the complaints of others. The biggest problem is finding a remedy that truly solves the problem. Leases that give tenants 30 days to resolve non-monetary defaults basically render the landlord helpless since the landlord cannot acct without giving notice and opportunity to cure. Termination is the "nuclear option," but is generally not helpful except as a club. Self-help and liquidated damages after notice and cure opportunity may be the best ideas.

I. Construction/Renovation Interference

This is similar to protected areas and no-build zones. Important to carefully identify all of these areas that may be necessary for staging and also specify the consequences for interference. Equitable remedies or liquidated damages may be the best answers here. Long delays for cure can have disastrous consequences on a retailer.

J. Bankruptcy Clauses

Many shopping center form leases contain standard provisions that purport to prohibit the tenant from filing bankruptcy, or that define the filing of bankruptcy as a default that entitles the landlord to terminate the lease or exercise self-help based on the bankruptcy. Such clauses, sometimes referred to as "ipso facto" clauses, are not enforceable. Landlords who rely on them to exercise rights after a bankruptcy is filed risk serious consequences for violating the automatic stay. The automatic stay acts as an immediate injunction under federal law against taking actions to collect debts or enforce rights against a tenant outside the bankruptcy process. Nonetheless, such clauses remain common in many commercial leases because (i) they are harmless as long as the landlord does not rely on them, and (ii) they may have some prophylactic effect, to discourage a tenant from filing bankruptcy before or without consulting with counsel.

While ipso facto clauses are not enforceable, well drafted leases can include provisions that would assist landlords in the event of a tenant's future bankruptcy. For instance, many leases incorporate language from the Bankruptcy Code to confirm expressly that any assumption and assignment of the lease in a tenant bankruptcy must meet all the requirements of Bankruptcy Code §365, including prompt cure of defaults, adequate assurance of future performance, and that such assignment not violate existing use, radius, or exclusivity clauses. While these rights exist even if the lease does not mention them, many landlords prefer to assert them expressly in the lease. In addition, leases that expressly allow landlords to recover reasonable attorney's fees and costs incurred in asserting and protecting the landlord's rights in bankruptcy, including the right to prompt cure of defaults and adequate assurance of future performance when a lease is assumed and assigned, can be helpful. Bankruptcy law provides for some recovery of attorney's fees in such instances, but this can depend on whether the lease language provides for such recovery. Leases that provide for recovery of attorney's fees only where a landlord is the "prevailing party" in litigation over the lease may be too narrow to permit recovery in a bankruptcy proceeding.

II. Standard Defaults and Remedies

A. Events of Default

1. Monetary Defaults

While lease defaults come in all shapes and sizes, the most common defaults are *monetary*, where an amount due is not paid. While rent is the most basic financial covenant which can be breached, most shopping center leases contain a variety of monetary obligations beyond just "rent," including monthly charges for a prorata share of common area maintenance, real estate taxes, insurance, trash, and promotional expenses. These charges are often referred to as "triple net" charges meaning that the amount received by the landlord is net of taxes, insurance, and maintenance expenses. In most leases, triple net charges are defined as "additional rent" and payable every month, just like the regular base rent. Many retail leases also require payment of percentage rent, calculated as a percentage of gross sales above a specified breakpoint.

In addition to monthly charges, most shopping center leases include provisions for reconciliation of triple net charges annually, where the monthly prorata estimates that have been charged are compared with actual charges for maintenance, taxes, and insurance. If there is an overpayment, the difference is typically credited back to the tenant, and if the monthly amounts paid are determined to less than the tenants actual prorate share, additional reconciliation charges for the difference are assessed. Sometimes tenants fail to pay such charges, or dispute their calculation, which can result in a dispute and possible default.

2. Abandonment/Surrender

Abandonment, surrender or just failing to operate (“going dark”) have separate and distinct meanings and it is important to be able to identify the act to determine the applicable right or remedy available to the parties. The concepts of “abandonment” and “surrender” are frequently confused. There is also a difference between a failure to open and operate, ceasing operations and either an abandonment or a surrender. Abandonment itself may have different meanings depending on the context. It can have different meanings for real property as opposed to personal property. For instance, abandonment of possession by a tenant will not terminate a lease, but will give rise a landlord’s right to re-enter a premises without necessity of a court order. Abandonment of personal property by a tenant will allow a landlord to dispose of that personal property. Surrender involves an offer by the tenant to return possession and the landlord’s acceptance of the surrender will operate to terminate the lease and, therefore, the tenant’s obligation to pay future rent. A Landlord who desires to recover possession of a leased premises, but without cutting off the tenant’s liability should be express in preserving that right when recovering possession.

a. Not all store closings the same? Seasonal businesses

Seasonal businesses. It is not uncommon for certain businesses to lease premises but only be open during certain seasons. Ice cream and other frozen dessert operations come to mind as do certain party stores for Halloween or Christmas as well as certain types of garden stores. Leases for these types of operations should take these types of operations into account, including the maintenance and insurance obligations and expenses. Some landlords use special short from leases or even so-called “temporary license agreements” for these types of uses that give a landlord certain expedited rights.

b. Liability issues and state statutes

A landlord is well advised to carefully review its lease and consult its attorney since re-entering a tenant’s premises using self-help can expose a landlord to more liability than just damage to the premises. Numerous states have statutes that expressly define the efforts a landlord must make to establish abandonment or locate the “missing” tenant and may impose double or treble damages and attorney fees for a violation of a tenant’s rights to quiet enjoyment.

3. Other Nonmonetary Defaults

In the case of the landlord, nonmonetary defaults include breaches of the landlord’s obligations to perform the landlord’s work, repair the Premises, maintain the common areas, ensure access to the Premises, enforce exclusives and prohibited uses, rebuild after damage or destruction, deliver an SNDA. It also includes defense of the covenant of the tenant’s quiet enjoyment, which can cover a watershed of issues related to a tenant’s perception that there has been some type of interference with its ability to operate.

In the case of the tenant, other nonmonetary defaults could relate to violation of the tenant’s use clause, operating requirements, prohibited uses, other tenants’ exclusives, shopping center rules and regulations, noise restrictions, odor restrictions, signage requirements and prohibitions and sales reporting requirements.

The key issue with respect to nonmonetary defaults is tailoring the cure period to the violation. Waiting 30 days for completion of repairs may be acceptable; giving a 30-day cure period for a failure to take down an offensive sign may not. In fact a cure period may not even make sense—how can a tenant "cure" a failure to open on time? But, it may be unfair to terminate a lease if the default stems from the store manager opening the doors 15 minutes late. Instead, tailor the default of operating hours requirement to exempt the occasional late opening and focus on repetitive or egregious violations.

4. Triggering Dates, Windows and Sunsets

It is important for the Lease to specify both the beginning and the end of a remedy. When is a default deemed to occur? When does the right to a remedy commence? After notice? After opportunity to cure? During a set period of time? When does the right to a remedy end? After a specified period of time? After the occurrence is abated? Never? If a party is not truly being harmed by the occurrence, but bargained for a substantial remedy and exercises an extension option, would that be an indication that the remedy should sunset? What if there are multiple factors that must occur to give rise to a default and trigger a remedy, but one of the triggers is cured (e.g. multiple store closings for a specified period of time, but one later reopens or is replaced). The triggering date for the remedy may depend on how long it may take a party to reasonably cure or commence the effort to cure. Similarly, the trigger date should also take into account the likelihood of actual damages having commenced as a result of a default or occurrence. It seems unreasonable that a remedy should commence before a defaulting party has had an opportunity to cure. On the other hand, if it was a blatant situation and the non-breaching party has actual damages, a case could be made for a remedy being retroactive to the first occurrence and be triggered before notice is given. If the remedy is liquidated damages it may not make a difference. If the remedy is designed to be coercive as opposed to compensatory, there will be another answer. One size will generally not fit all in this context and these are all points for careful negotiation.

B. Remedies

1. Termination of Lease

The problem is that termination is frequently the "nuclear" option and is rarely the best fix. Terminating the lease (unless expressly reserved by the lease) terminates the tenant's future economic obligations under the lease. It is most frequently used when the landlord already has a replacement tenant waiting in the wings. It is certainly a coercive power and raises the stakes. Caution should be used in trying to always have specific remedies provided for various types of defaults or "situations," "scenarios," "violations" or "occurrences." A termination right as the remedy may also be meaningless if everyone knows that nobody will "push the button." What if the lease is silent as to the tenant's remedy in case of the landlord's violation of a tenant exclusive? What if the lease is silent as to the consequence of a tenant's violation of a radius restriction? Would the landlord really want to terminate its tenant because it opened another nearby store? Hardly. However, consequential damages might be difficult to prove, so the absence of a remedy expressed in a lease may mean that there is no remedy at all. Unfortunately, lazy negotiations sometimes lead to that result since it may be easier to identify an obligation under a lease than to fashion a remedy that will fit.

2. Possession or re-entry without termination of the lease

This remedy, recovering possession of the premises, without terminating the tenant's obligation to pay the rent is the most commonly used Landlord remedy to leverage payment in monetary default cases. It is available as a matter of state law in the form of an expedited or summary proceeding. The tenant's right to possession is terminated, but not its economic obligations under the lease.

3. Damages

a. Past due rent and lost future rent

As a practical matter, the issue of damages typically arises after the right of possession has been addressed. This is because defaults – especially monetary defaults that stop a flow of income to the property while a tenant remains in possession – are serious, urgent matters. They cannot wait for a calculation of damages. If a tenant is not paying monetary obligations, most landlords will swiftly put the tenant in default and move to evict if the default is not cured and the tenant remains in possession. When that process concludes, or if the tenant vacates voluntarily in response to the default notice or subsequent proceedings, the next step is to assess and quantify the amount of a possible damages claim.

The starting place for analysis of a damage claim after the lease has been terminated is the default clause in the lease. Default clauses typically, but not always, provide for the maximum calculation of damages under state law. For instance, lease default remedies typically allow the landlord to recover, the sum of the past due rent at termination – which is not subject to mitigation – and the total amount of the lost future rent and charges that would accrue in the future through the term of the lease, less what the landlord actually did or could have reasonably recovered from re-letting the premises after the breach. Embedded in this calculation is the obligation of the landlord to take reasonable steps, after recovering possession, to relet the premises in order to mitigate its lost future rent damages resulting from the tenant's breach. Generally, the former tenant has the burden of proof on the issue of any reduction in the damages that could reasonably have been achieved by reletting. As a practical matter, most landlords take reasonable steps to relet their premises anyway – because it makes good business sense to do so. Nonetheless, wherever there is a claim for damages for lost future rent, the landlord's leasing team should keep good records of the efforts to relet, and should be aware of the obligation to be reasonable in reletting when evaluating new offers to lease the premises after a breach.

In order to preserve the right to claim damages through the full term of the lease, the lease should expressly so provide. Most form shopping center leases include such terms in the default clause, but not always. If all the language is not in the lease, then damages may be limited to whatever the past due rent and lost future rent is through the time the case is decided, even if the term of the terminated lease would have extended beyond that time.

Leases in which all or most of the rent is calculated as a percentage of sales present special challenges for damage calculation. First, there is no way to know what the percentage would be without sales reports, and tenants that are breaching other obligations often do not provide sales reports to allow correct calculation of percentage rent. Second, after a lease has been terminated and the tenant is gone, there are no sales to support a calculation of lost percentage rent. In such cases, it is helpful for leases to include liquidated damage provisions, noting that the losses resulting from a breach or closure would be difficult to calculate, and providing stated reasonable amount as a measure of damages for failure to pay percentage rent due. Without such a clause, calculation of damages would be an issue of proof, based on sales averages.

b. Lost profits and consequential damages

If a landlord defaults, the tenant's damages are less straightforward to calculate. This is because more monetary obligations in the lease run from tenant to landlord, not vice versa. So if the landlord defaults, the amounts of damages would depend on the nature of the breach and damages would be the amounts that would naturally and foreseeably result from the breach – obviously an issue of proof. If a landlord interferes with a tenant's business, or breaches some special obligation or covenant, the tenant may have to prove lost profits or some other form of consequential damages. Many leases present additional obstacles to such recovery, by including language that expressly waives the tenant's right to consequential damages, except those resulting from the landlord's gross negligence or intentional misconduct.

c. Late Charge, Interest and Attorneys' Fees

Late fee and interest provisions are most relevant before the lease is terminated, when determining the amount that is actually past due. Most leases provide for assessment of a modest late fee of a few hundred dollars or perhaps 5% of the amount due, if the amount due is not received within some stated reasonable time after it is due, e.g., 5 or 10 days. While most leases also provide for interest, as a practical matter, interest is much harder to calculate for a short period of time, and there is a risk that, if it is assessed in addition to a late fee, the sum of such additional amounts will be so far beyond the losses that such late payment would have caused, that such additional amount may be considered a penalty. For this reason, at least with respect to late amounts, having a simple late fee is sufficient and often preferable to having a provision for interest also. With respect to damage claims after termination, there is no need to include an interest provision, as most states allow recovery of pre-judgment where can be reasonably calculated.

If a lease dispute is litigated, the prevailing party can typically recover its reasonable attorney's fees, provided that the lease contains an attorney's fees provision providing for that. If a lease is silent on the issue, the so called "American Rule" applies, meaning that each side must bear its own attorney's fees. While most commercial lease forms include an attorney's fees clause, some purposely do not; this can occur in the case of, perhaps, a large or powerful tenant, such an anchor tenant, that uses its own form lease. Since most defaults are monetary, and most monetary obligations run only from the tenant to the landlord, some tenants omit attorney's fee clauses from their form leases specifically to discourage landlord's from litigating claims against them.

4. Equitable remedies

Of course, equitable remedies – such as specific performance or injunctive relief – provide unique and different options in the event of a default. In general, equitable remedies require a high standard of proof, not only involving a probability of prevailing, but also the prospect of some injury that would be irreparable, and that a financial award (i.e., damages) would not be adequate. Since most default issues in shopping center leases involve monetary issues, equitable remedies are relatively rare. Even where a lease might specifically provide for such relief, such as to require a tenant to operate, or to enforce standards of operation, courts are reluctant to issues such orders for lack of ability to enforce them. In many cases, landlords are better off with some kind of liquidated damages remedy, rather than having a lease provide for injunctive relief that a court will not issue.

5. Right to cure/self-help/offset

Landlords want the ability to make repairs and perform obligations required by the lease to be performed by the landlord, in order to keep the shopping center uniformly safe, clean and viable. They do not want tenants performing those obligations out of fear that the quality or design will not be maintained, that the tenant's work will interfere with others, that the tenant might implement an unnecessary upgrade, or that the landlord can perform the work at a less expensive rate. Tenants, on the other hand, have an ongoing business which they must protect. A landlord that is delinquent or slow in making repairs or performing its other obligations may interfere with that business. Thus, tenants want the ability to perform the landlord's repairs or other obligations if the landlord has not performed them within a reasonable period of time, or sooner in the event of an emergency that may threaten injury to person or property.

Once the tenant has performed the cure, it wants the ability to be quickly paid—by offsetting the costs from rent or permitting the landlord a short period to pay, with the ability to offset if the landlord fails to make payment. Landlords seem to hate offset rights more than self-help rights. They feel that offset rights do not allow the landlord the ability to challenge the amount of the costs, much less whether the tenant even had the right to perform the self-help in the first place. Landlords also are concerned about any limitation on the rental stream, which they count on to make payments for expenses and loans.

There are few rights which are more dependent on the tenant's leverage in the deal than the right to cure and offset. Tenants with great leverage may be able to demand cure rights on any default of the landlord, regardless of whether the default relates to something within the premises, and even if the problem has not technically arisen to a default under the lease. Those tenants can also demand offset rights that include interest and even "administrative charges" on costs incurred in performing the self-help action. Tenants with little leverage may have their self-help rights limited to repairs within the premises up to a certain limit, with no right to offset. In the most extreme cases, some tenants are unable to obtain any self-help rights whatsoever. This controversy continues to the SNDA, where tenants who fought long and hard for an offset right in the lease may have it eliminated in the SNDA, at least with respect to the offsets that accrued prior to foreclosure. Many landlords push for offset limits to ensure that some rental stream continues to flow at all times, and blame lenders for it when the landlords lack leverage. As a result, many tenants agree to cap certain offset rights each month (although most won't do so for payments expressly required under the lease, such as allowances or late delivery fees). This extends repayment, which may be a concern if there is not enough term left to fully recoup the costs. Many tenants also demand that interest accrue, similar to the landlord's demand for interest on late payments by the tenant.

6. Negotiated limits of remedies

When does the right to a remedy end? After a specified period of time? After the occurrence is abated? Never? What if there a multiple factors that must occur to give rise to a default and trigger a remedy, but one of the triggers is cured. (E.g. multiple store closings for a specified period of time, but one later reopens or is replaced?) It is important for the Lease to specify both the beginning and the end of a remedy. It is not unusual for the parties to provide a remedy as if a particular event will cause damage, but, in actuality, it does not. Is it reasonable for a tenant to continue have reduced rent in the event of a cotenancy violation from the loss of a named or category tenant when the replacement tenant may even be a better fit, but the replacement tenant does not actually qualify as a cure? Some parties resort to a formula or cap on damages after a certain period. The point is to think through the different potential violations. Should a tenant be able to exercise a renewal option when there is a violation of some kind that is apparently not so harmful that the tenant would not exercise a termination right or not renew? Fortunately or unfortunately, it will be the lease language that controls so it will be important to make sure the language works. Courts will enforce the bargain struck by the parties whether it subsequently turns out to be "fair" or not.

7. Effect on other party's rights

It is not uncommon to tie a party's rights to compliance with a lease. For instance, a tenant's rights to its exclusive are frequently contingent upon the tenant actually be opening and operating—even if it does not have an operating covenant. Often a lease will have language terminating a tenant's renewal options if the tenant is in default at the time for exercise or has been a "habitual" defaulting party. Naturally, interest, late charges and even increases in rent can be triggered by miscellaneous defaults.