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Coronavirus Considerations for Landlords and Tenants

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Companies everywhere are working diligently to analyze potential risks during these challenging times. The growing number of business disruptions and state-ordered shutdowns in the wake of the coronavirus pandemic is putting a strain on commercial landlords, their lenders and tenants. Lease agreements should be analyzed to determine if there is language addressing what landlords and tenants can and cannot do to avoid breaching their leases. As rent becomes due, a number of landlords and tenants are questioning their respective obligations and rights. Each lease agreement is different and may contain unique provisions, so parties should consult with counsel for additional guidance. Below is a list of provisions that landlords and tenants should consider.

1. Continuous use/go dark/operating hours

If a lease agreement contains minimum hours of operation or continuous operation covenants, tenants should notify their landlords if they elect to close or reduce operations in response to government orders and/or concerns for the safety and health of employees and customers. This is particularly relevant for retail tenants, but may apply to some office or industrial tenants as well. If the lease contains a force majeure clause (see below), the tenant can likely rely on such provision to avoid being in default and should inform its landlord accordingly.

2. Force majeure

Force majeure clauses provide landlords and tenants with some relief if they are unable to perform their obligations due to certain events, which are often specified to include acts of God, strikes, government actions or other causes that are unforeseeable or outside the reasonable control of the parties. Landlords and tenants should review their force majeure clauses carefully to determine whether emergency measures taken in response to the coronavirus may excuse or delay performance. Notably, however, most force majeure clauses do not excuse payment of rent or other monetary obligations. As a result, tenants are generally not relieved from paying rent even if a state-ordered shutdown qualifies as a force majeure event. Read our Applicability of Force Majeure and Related Doctrines alert for additional information.

When negotiating a new lease, prospective landlords and tenants should consider including language allowing the deadline for certain key events, such as completion of initial tenant improvements or the rent commencement date, to automatically extend as a result of a pandemic-related delay. However, parties should be careful if they choose to add this language under a standard force majeure provision, since any consequences of the coronavirus pandemic are unlikely to be considered "unforeseeable" at this point.

3. Damage, destruction and other casualty

Commercial leases usually include a provision which outlines the respective obligations of the landlord and tenant in the event the leased premises are damaged or destroyed by fire or other casualty during the term of the lease.

Landlords are typically required to repair and restore the premises following a casualty event, but often have some level of discretion in deciding how to proceed depending on the extent of the damage and/or destruction. The landlord's obligation, for example, may depend upon its receipt of property insurance proceeds or the extent of the damage or the length of the term remaining under the lease. Some leases may grant the landlord and/or the tenant the right to terminate the lease in certain scenarios, such as when the damage is extensive or occurs near the end of the lease term, or if the casualty causes the premises to be untenantable.

In general, if the landlord elects to repair and restore the premises, the tenant remains obligated to pay rent during the period of restoration – provided, however, that some tenants are able to negotiate a proportionate rent abatement of rent during the period following the casualty event when the premises are untenantable and/or the landlord is repairing the property until the premises are restored.

Whether or not the damage, destruction or casualty provision of a lease will be applicable during the coronavirus crisis – in light of building closures and shelter-in-place orders in place throughout the country – will depend on the specific language of the lease. Casualty provisions are typically written to cover damage caused by fire, floods or other natural disasters, but not cases where the physical building remains intact, such as the case may be during a pandemic. Because every lease is different, it is worthwhile to confirm the specific language of the provision before engaging the other party.

4. Hazardous materials clauses

Many commercial leases contain hazardous materials clauses, which generally prohibit the use, storage or manufacture of hazardous materials and/or substances on the premises by the tenant and require the tenant to indemnify landlords from and against any loss or damage resulting from the tenant's failure to comply with the provision. The definition of hazardous materials or hazardous substances varies lease-by-lease, but usually includes hazardous or toxic wastes or materials or similar substances, as defined by environmental laws and regulations. Sometimes leases also impose a similar obligation on the landlord, requiring it to comply with environmental laws and indemnifying tenant from any costs associated with the presence of hazardous materials in the premises or building that were not introduced by the tenant. However, this is often specifically negotiated by a tenant into the lease and is not considered standard language.

Some tenants may argue that the presence of the coronavirus vin the building would violate the hazardous materials clause. The efficacy of this position depends on the precise language of the lease, since the definition of hazardous materials does not normally include bacteria, viruses or other diseases. However, tenants may argue that in cases where landlord provides or arranges for the cleaning and/or janitorial servicing of the premises and building, the landlord is thereby obligated to take certain measures to prevent the spread of the coronavirus throughout the building, including heightened cleaning requirements, minimizing the number of guests and vendors allowed into the building, testing building staff, screening body temperatures and posting notifications and preventive steps.

5. Covenant of quiet enjoyment

Leases frequently include a covenant of quiet enjoyment, whereby the landlord covenants that the tenant's use of the premises will not be disturbed provided the tenant has complied with its obligations under the lease. In the event a landlord elects to close the building in which a tenant's premises are located (absent government intervention), it may be considered a breach of quiet enjoyment. On the other hand, if the building is closed to the public, but the tenant is still permitted to access the building for its own use, the covenant is not breached. But landlords should also consider whether limited closures and restrictions may constitute a breach of other lease provisions such as landlord's obligations to provide certain amenities or services (see below).

As more states and courts have passed eviction moratoriums, some have explicitly prohibited landlords from harassing tenants or engaging in behavior that constitutes interference with a tenant's quiet enjoyment of their property. Although these fact patterns appear mostly in the context of residential leases, commercial landlords should be aware that attempting to evict or force out non-paying tenants or engaging in other self-help measures can result in penalties.

6. Surrender obligations

If a lease will expire during the coronavirus pandemic, tenants should consider surrender provisions and the obligation to remove furniture and other personal property from the leased premises. In the event it is impossible for a tenant to remove its personal property and fully vacate the premises, or the tenant is expecting to be liable for holdover costs, a well-drafted force majeure clause will hopefully excuse a potential tenant default if the building is closed by the landlord or government authority. But there are open issues if the tenant's failure to surrender the premises is due to other causes.

7. Interruption of services and other landlord obligations

Most commercial leases stipulate the services the landlord is obligated to provide to the tenant as well as landlord's maintenance and repair obligations throughout the term of the lease. For example, the landlord is often responsible for performing structural repairs to the building, maintaining common areas and providing elevator, HVAC, water and janitorial services to the premises. Public utilities, such as gas and electric, are not usually provided by the landlord itself; instead, the landlord is required to ensure that the utilities are available at the premises, and the tenant either pays its share of utilities or procures and pays for its own utilities directly with the service provider. Note that as of April, several states have suspended utility shut-offs for nonpayment as an effort to allow residential tenants to continue living in their homes while they are impacted by the coronavirus pandemic. The applicability of such orders to commercial leases will vary state-to-state.

If the landlord fails to provide services or perform its maintenance obligations under the lease, the tenant is typically required to notify the landlord of the failure, and the landlord is entitled to a cure period to remedy the failure. Sometimes, however, leases include what is known as an "interruption of services" provision, entitling the tenant to rent abatement in the event of a material disruption of utilities or services to the premises. What constitutes a material disruption will vary by lease, but is typically one that lasts a minimum number of days, prevents the tenant from using the premises for its business and is not caused by the tenant. Note, however, that some leases do not provide for rent abatement in this scenario and, instead, have the parties opt to rely on property and/or business interruption insurance against this type of risk. In the absence of an interruption of services provision or other remedy, tenant would be required to continue to pay rent during any period of interruption caused by the coronavirus pandemic.

Finally, in addition to an interruption of services provision, a lease may contain a landlord default clause, giving the tenant some form of remedy in the event the landlord fails to perform its obligations under the lease and the failure continues for a certain period of time following written notice from the tenant. Remedies vary, but may include options for the tenant to perform self-help and seek reimbursement from the landlord for its costs, bring an action in equity or law, or recover damages from the landlord.

8. Business interruption insurance

There has been quite a bit of discussion in the industry regarding the status of business interruption insurance policies. While each insurance policy is unique, most policies require some kind of physical loss or damage to the property and many exclude events such as pandemics from coverage. Note that in some jurisdictions, courts have considered the insured's loss of access to its premises as a type of qualifying physical loss, so one should not automatically write-off certain losses as uninsurable. Moreover, several states have pending legislation which would force insurers to extend commercial property and/or business interruption insurance coverage to include coronavirus-related losses, though no laws have been enacted yet.

As of April, there is pending litigation in several jurisdictions, including California, Washington, DC, and Florida, challenging insurers' refusal to cover losses stemming from coronavirus-related business interruptions. Additionally, motions have been filed requesting consolidation of some cases into a single federal district court, which could result in an industrywide ruling.

Other insurance policies, such as professional liability and pollution liability, may be applicable to the coronavirus pandemic, depending on the circumstances, so it is important to get assistance reviewing the language in your policy to make sure there are no missteps before deciding whether to file a claim. In addition, there are policies that specifically cover interruptions due to communicative diseases or infections. However, they are quite costly (8 – 10% of the coverage) and are rarely purchased as a result.

Once a potential coronavirus-related loss is suspected, the insured should provide notice to the insurer as soon as practicable. Notice requirements will vary based on the insurer, so it is important to refer to the specific provisions within the policy to determine how proper notice is to be given. It is best practice to closely track any losses incurred as a result of the coronavirus and to start an ongoing communication with insurers about losses and extra costs as they are incurred so the insurer cannot later try to argue that they were not properly informed.

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Key Contacts

Adrienne Beaudoin Deshmukh **Reston**	**adeshmukh@cooley.com** **+1 703 456 8709**
Michelle Garcia Schulman Reston	mschulman@cooley.com +1 703 456 8123

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