Defaults under Commercial Leases

Termination or forfeiture of a commercial leasehold is legally justified where there is a breach of a material covenant or condition of the lease or a violation of applicable law authorizing termination. Although there are numerous grounds to terminate a commercial lease, they generally fall within two categories: monetary and non-monetary.

Monetary grounds occur where a party, usually the tenant, fails to meet a financial obligation due the other party, usually the landlord, under the lease or applicable law. In addition to a tenant's failure to pay rent when due, other monetary grounds for termination would include a tenant's failure to pay its portion of common area maintenance, taxes or the costs of repairs or improvements for the demised premises. Florida courts typically uphold a landlord's termination of a lease based upon monetary grounds, provided however, that the requisite notice has been served and the time to cure has expired.

Non-monetary grounds are more problematic and are disfavored by Florida courts. On the tenant's behalf, a lease may be terminated if the landlord breaches a material obligation due the tenant under the lease or applicable law. One example could be where the landlord breaches its covenant of quiet enjoyment, resulting in a constructive eviction of the tenant. This may occur if, during construction of an adjoining space, the tenant's operations are so impaired and interrupted that it cannot conduct any business whatsoever. Another example could be where the landlord is obligated to make material repairs to the demised premises, but fails to do so after receiving the requisite notice from the tenant. Examples of non-monetary grounds may include the lapse of a tenant's liability insurance required under the lease, the assignment or subletting of the premises without the landlord's consent and the appointment of a receiver over the tenant.

However, a non-monetary ground for termination will not be judicially enforced, unless there is evidence that the tenant's or landlord's interests have been materially prejudiced and a forfeiture will not result in an unconscionable or inequitable result.

Waiver of Defaults

By accepting of the full amount of rent that is due with knowledge of the tenant's breach of the lease for nonpayment of rent, the landlord will be deemed to have waived any right to terminate the lease and retake possession of the premises as a result of the tenant's failure to pay rent. This statutory waiver follows the common law rule that a party to a contract may waive a default thereunder by express agreement or by conduct.

However, most leases contain "anti-waiver" provisions stating that the landlord's acceptance of any rent or any act of forebearance shall not be deemed a waiver of any rights that the landlord has as of that date. Notwithstanding an "anti-waiver" provision, at least one Florida court has held that the landlord's acceptance of late rent was not only a waiver of the tenant's default for failure to pay rent, but was also a waiver of the anti-waiver provision itself. In that case, however, the landlord accepted the late rent payments without protest and never notified the tenant that it was in default of the lease.

Florida's parol evidence rule also provides some protection against a party to a lease alleging that its terms were waived by an oral agreement. The rule is that, if the terms of a contract are unambiguous and the contract is a complete agreement, those terms are not subject to modification, variance or contradiction by parol (oral) evidence. If the lease agreement is ambiguous as to the parties' intent on the subject matter in question, parol evidence will be admissible on the issue. Since the rule only applies if the parties' agreement is unambiguous and complete, it is important that the lease expressly state that it is "the entire agreement between the landlord and the tenant and all other oral or written understandings and agreements are merged into the lease and are deemed void."

Notice of Default

Florida Statutes and most leases require one party to a lease to give the other party notice of a material default and an opportunity to cure the default. If after proper notice, the defaulting party fails to cure, the non-defaulting party may terminate the lease. Unless the lease states otherwise, the time period for the notice depends upon the term of the tenancy. Under Florida law, any tenancy is deemed a "tenancy at will" unless it is in writing signed by the landlord. If the tenancy is reflected by a written instrument, but the term of the tenancy is unlimited, the tenancy is also deemed to be a tenancy at will.

If the tenancy is at will, its duration is determined by the period of time in which rent is payable. If rent is paid weekly, the tenancy is week to week. If rent is paid monthly, the tenancy is month to month. If rent is paid quarterly, the tenancy is quarter to quarter. If rent is paid yearly, the tenancy is year to year. A tenancy at will may be terminated by giving written notice as follows:

(1) Year to year - not less than three months notice prior to any annual period;

(2) Quarter to quarter - not less than 45 days notice prior to the end of any quarter;

(3) Month to month - not less than 15 days notice prior to the end of any monthly period;

(4) Week to week - not less than 7 days notice prior to the end of any weekly period.

If the tenancy is not at will, notice must be given in accordance with the terms of the lease, but not less than 3 days written notice for a default in the payment of rent. If the lease is silent on the matter, at least 15 days written notice must be given to cure any other

material breach of the lease. Notice must be served in the manner required under the lease. If the lease is silent on the matter, notice must be by actual delivery to the tenant or, if the tenant is absent from the demised premises, by leaving a copy at the premises.

If a tenant desires to terminate a commercial lease for the landlord's failure to make repairs, the tenant must follow the procedure set forth in the lease. Where the lease is silent on the issue, but it expressly places the obligation to make the repairs upon the landlord, the tenant must give the landlord at least 20 days written notice. However, the landlord's failure to make the repairs must render the premises completely "untenable." The tenant's notice must demand that the landlord make specifically described repairs and expressly state the tenant will withhold rent for the next rental period and thereafter until the repairs completed. If the landlord fails to comply with the notice, the tenant may then abandon the premises, retain the rent withheld, terminate the lease and avoid any liability for future rent or charges.

Proving Defaults

Although a landlord's or tenant's termination of a lease must comply with the pre-requisites of the lease and Florida law, proving the presence of lawful grounds to terminate is a separate issue of concern.

Non-monetary defaults can be difficult to prove at times. A tenant's violation of a restrictive covenant or use clause can be a fact intensive issue for a court to decide. The court will need to determine whether the tenant's actual use complies with the scope of the use clause and, more importantly, whether the actual use is materially interfering with the rights of other tenants and/or the landlord's interests. Although the parties and witnesses will testify on these issues, a properly authenticated surveillance video "speak a thousand words."

Monetary defaults are usually straight forward, but may become unclear under certain circumstances. For example, assume that a lease requires rent to be paid on the first of each month and, after receiving an appropriate notice from the landlord, the tenant orally requests an extension of time to make the payment under the notice. The landlord orally refuses and proceeds with an eviction action. The tenant, in defense, deposits the rent in the registry of the court and defends on the grounds that the landlord had orally agreed to the extension. If the landlord had made a contemporaneous memorandum of the conversation or written the tenant a confirming letter the day the extension was refused, the landlord would be in a much stronger evidentiary position to respond to the tenant's defense.

Lending institutions are faced with this "oral extension" defense frequently. In

response, many lending institutions have internal procedures that require all loan officers having any oral communications with their borrowers to maintain contemporaneous telephone logs and send confirming letters of important discussions. This practice serves two functions. First, it provides a written instrument for the parties to refer back to in the event of a good faith misunderstanding. Second, it produces physical evidence of the facts at the time they occurred. This physical evidence, if made contemporaneous with the conversation and in the normal course of business operations, is generally admissible in court. When faced with a “he said-she said” defense, the party who also has a contemporaneous document evidencing the conversation will more often than not prevail in the dispute.

Self Help

A common example of a landlord using "self-help" to retake possession of demised premises is where a landlord unilaterally changes the locks during the night. Except under very limited circumstances, that action could subject the landlord to liability for damages under the lease and Florida law.

A landlord may retake possession of leased premises in three exclusive ways: (1) the landlord pursues a court action, such as an ejectment action or an eviction lawsuit; (2) the tenant voluntarily surrenders possession of the premises; or (3) the tenant abandons the premises. "Self-help" is only available where the tenant either surrenders possession or abandons the premises.

To prevent any dispute over whether or not the tenant voluntarily surrendered the premises, a surrender should be reflected in a written surrender agreement signed by the tenant. Otherwise, the landlord should proceed with the judicial process or determine whether the circumstances constitute an abandonment.

In considering whether an abandonment has taken place, the landlord should be certain that, at a minimum, the statutory presumption of abandonment may be present before "self-help" is used to retake possession. This presumption arises if: (a) the landlord reasonably believes the tenant has been absent from the premises for 30 consecutive days; (b) the rent is past due; (c) proper notice has been served; and (d) at least 10 days have elapsed since service of the notice. If all of these elements are not present, the presumption not be available to the landlord. In that event, the landlord will have the burden to prove in court that the premises were, in fact, abandoned. Evidence of an actual abandonment may include the termination of all utility services, the removal of the tenant's

property from the premises, and the tenant having all mail forwarded to another location.

Going Dark

Any landlord faces a serious dilemma when an anchor tenant or major tenant "goes dark." For example, a shopping center landlord has a ten year lease with an anchor tenant. With five years left on the lease, the tenant determines that its monthly operating losses for its store at the leased premises well exceed the amount of the monthly rental. Further, it has been offered a long-term lease within one mile at a location projected to be extremely profitable. The tenant closes its store at its current location (thereby "going dark"), but it continues to timely pay all monthly rentals in accordance with the lease. The anchor tenant's "going dark" has a widespread negative impact on the shopping center's other tenants, as well as the overall marketability of the shopping center. The landlord must determine whether it may declare a breach of the anchor tenant's lease for "going dark." The answer depends on whether the lease expressly or impliedly includes a covenant of continuous operation.

Assuming there is no such express provision in the lease, the court must interpret the entire lease to determine whether the parties intended it to include an implied covenant of continuous operation. If the court finds that there was no such intent, the anchor tenant's "going dark" will not be deemed a breach of the lease, provided it continues to timely pay rent.

Courts have considered a variety of facts and circumstances to determine whether a lease implies such a covenant in the absence of an express covenant. Does the lease provide for a large portion of the annual rent to be based upon a percentage of gross sales? Is the tenant the only anchor tenant for the entire property? Is the base rent fairly below the market rent for the premises in consideration of the landlord receiving a

percentage of sales as additional rent? Does the lease affirmatively require (as opposed to permit) the tenant to use and operate the premises for a particular purpose? Did the landlord incur significant expenses constructing the premises specifically for the tenant's use? Was the landlord's construction of the premises a pre-condition to the tenant becoming obligated under the lease? Was the landlord required to transfer to the tenant any investment or tax credits for the construction of the premises? Does the lease restrict the tenant from assigning or subletting the lease without the consent of the landlord? Does the lease prohibit the landlord from leasing any adjacent premises to a competing business? Did the lease require (again as opposed to permit) the tenant to commence operations within a specific period of time? Does the lease grant the tenant the right to vacate the premises during the term of the lease upon giving notice?

Whether the parties to a lease intended the tenant to be bound by an implied covenant of continuous operation depends in large part upon circumstantial evidence. If the landlord intends to prevent any tenant from "going dark," the lease should contain an express covenant of continuous operation.

Appointment of Receivers

Some leases provide for the appointment of a receiver over the premises or the leasehold in the event of a breach or default. Whether or not a lease expressly provides for the appointment of a receiver, a court may exercise its discretion in this regard to preserve the premises from irreparable harm or to otherwise prevent irreparable harm to the parties or the public. The appointment of a receiver has been upheld in a variety of situations.

One case involved a landlord who declared a breach of a 99-year commercial lease for the tenant's failure to pay municipal and county taxes. The breach occurred only two years into the lease period. The landlord terminated the lease after giving the tenant written notice of default and a 30 day opportunity to cure by paying the delinquent taxes. The landlord thereafter filed a lawsuit requesting that a receiver be appointed pursuant to two provisions in the lease. One provision granted the landlord a first lien on the rents and profits resulting from the tenant's use of the premises. Another provision specifically provided for the appointment of a receiver to protect the landlord's interests upon a default by the tenant. The Florida Supreme Court affirmed the trial court's appointment of a receiver to protect the landlord's interests and to enforce the provisions of the lease. The court, however, stated that its conclusion might have been different had the tenant offered or tendered the delinquent taxes to avoid an inequitable forfeiture of the leasehold.

Injunctions for Lease Covenants

A temporary injunction is an extraordinary remedy. The movant must prove all essential elements for a temporary injunction with competent, admissible evidence. Those elements are as follows: (1) the likelihood of irreparable harm; (2) the unavailability of an adequate remedy at law; (3) a clear legal right to the relief requested and a substantial likelihood of success on the merits; and (4) the injunction is in the public interest.

In the context of landlord-tenant cases, injunctions have been granted to enforce specific, unambiguous restrictive covenants for the exclusive use of the premises. These restrictive covenants are more commonly known as non-competition provisions. To be enforceable, a restrictive covenant in a lease must be clearly expressed in positive terms. Furthermore, the party seeking the injunction must prove that it will be irreparably harmed unless the non-competition clause is enforced by the court.

A lease provision that granted a tenant the "privilege" to operate a particular type of business did not clearly and positively express an intent that the tenant would be able to prohibit the landlord from leasing to a competing business. Hence, the court did not grant an injunction.

Generally, a tenant is not entitled to an injunction against the landlord initiating an eviction action pending resolution of the tenant's declaratory judgment action to interpret the terms of the lease. This is because the same issues raised in the tenant's declaratory judgment action can be asserted as defenses in any eviction action. As a result, the tenant has an adequate remedy at law and cannot prove all essential elements for an injunction.

Injunctions have been granted in favor of landlords preventing a tenant from

violating a specific use clause in a lease. For example, an automobile dealership was enjoined from erecting lights on its lot that were detrimental to the adjoining drive-in theater owned by the lessor. The dealership was enjoined because its lease specifically prohibited its use of the premises in any way that was detrimental or competitive with the lessor's adjacent property. The lease also prohibited the dealership from erecting any sign or lights that would in any way obstruct the view of the theater's sign or would be objectionable to the drive-in theater. The lighting used by the dealership was found to be a substantial interference with the lessor's theater as contemplated by the restrictive covenant in the dealership's lease.

Injunctions have also been issued for the enforcement of implied and expressed covenants of continuous operation. Where a lease expressly required the tenant to remain open for business "year round," except for holidays and after ordinary business hours, and the rent was based upon a percentage of sales, a mandatory injunction was entered requiring the tenant to remain open in accordance with the lease. This injunction was affirmed based upon the court's determination that further breaches of the covenant could not be adequately compensated by an action at law and the injunction was necessary to protect and maintain the character of the entire property for the benefit of all of its tenants.

Landlord's Common Remedies

Unless otherwise stated in the lease, a landlord in Florida has three options when a tenant defaults under the lease.

First, the landlord may re-take possession of the premises for the account of the landlord. If this is done, the landlord releases the tenant from any further obligations under the lease.

The second option is for the landlord to re-take possession of the premises for the tenant's account. In the event the landlord does so, the tenant remains liable for all obligations under the lease. However, if the premises are re-let, the damages to be assessed against the tenant will be the difference between the rentals and any reasonable expenses incurred to re-let the premises.

The landlord's third option is to simply do nothing and sue the tenant as the rentals become due under the lease. If the subject lease has an acceleration clause, the landlord may accelerate the entire balance of the rent to be immediately due and sue for that amount. In that case, reduced to present value.

Whether the tenant has the ability to pay a monetary judgment will weigh heavily on the landlord's election of which option to pursue. It may be that the tenant is not collectible. In that case, the tenant may agree to voluntarily surrender the premises for the landlord's account within a short period of time so that the landlord may re-let the premises and minimize its lost rent. On the other hand, the tenant may be a publicly traded company that has a multi-million dollar net worth and the rental market has declined since the lease was signed. In that event, the landlord may desire to accelerate the rent, undertake protracted litigation and seek a monetary judgment for the full amount of rent

due. These types of strategy decisions are best analyzed after reviewing all available information on the tenant's financial condition and its potential defenses.

If a corporate tenant goes out of business and defaults on its lease, the landlord may obtain a monetary judgment against the corporate tenant only to learn that it no longer has any assets to satisfy the judgment. If the corporation had substantial assets at one time, it is prudent to determine the disposition of those assets. Given the right facts, the individual directors and shareholders of the corporate tenant, or other persons or entities, may be liable for the landlord's judgment.

As a general principle of Florida, if the assets of a corporation are transferred to another person or entity without that transferee paying adequate consideration in return for the assets, that transferee may thereby become liable to the corporation's creditors to the extent of the assets transferred. In addition, the creditor may be able to set aside the transfer and levy upon the assets transferred or other substitute property of the transferee.

A corporation's shareholders may be liable for the corporation's debts to the extent that they received a distribution of the corporation's assets at a time when they knew or should have known that the corporation had outstanding debts. Florida law holds that, in such an event, the shareholders are personally liable since they are deemed to have received the corporate assets as trustees for the benefit of the corporation's creditors. Similarly, Florida Statutes will hold corporate directors personally liable for any unlawful distributions made to the shareholders which the directors affirmatively authorized. This typically occurs when directors declare distributions to shareholders where the corporation is insolvent at the time or is rendered insolvent by the distributions.

Florida courts will also hold a corporation's shareholders liable for the corporation's

debts where it can be shown that the corporation was organized or used to mislead its creditors, to perpetrate a fraud on the corporation's creditors or the corporation has been used for some illegal purpose. However, the mere ownership of a corporation by one or a handful of shareholders is an insufficient reason to pierce the corporate veil.