

3 Things To Watch As COVID-19 Real Estate Litigation Looms

By **Andrew McIntyre**

Law360 (July 1, 2020, 4:09 PM EDT) -- Commercial landlords and tenants have to a large extent not brought their disputes over payment of rent to court during the COVID-19 pandemic, but lawyers say several factors — including uncertainty about assistance under the CARES Act — are likely to usher in a wave of litigation soon.

Experts say tenants are likely to have more difficulty making rent later this summer, given that the Paycheck Protection Plan assistance from the Coronavirus Aid, Relief and Economic Security Act expired at the end of June and, if President Donald Trump signs an extension, would end roughly five weeks from now. And commercial landlords are also in the tricky position of being restricted by their lenders.

And in the case of disputes over leases at shopping centers, tenants may find they have additional claims against their landlords, given that shopping center leases often have co-tenancy provisions.

Here, Law360 looks at three things to watch for as COVID-19 litigation looms.

Shopping Mall Tenants May Have Additional Claims

Shopping center leases are unique in that they generally have co-tenancy provisions, and that could give tenants more options for arguments in court.

The idea is that a retailer leasing space at a mall wants to make sure other stores are also open to ensure foot traffic. If other stores at the mall close, tenants may have an argument against the landlord.

"Tenants can argue that the landlord hasn't fulfilled its [co-tenancy] obligation," said Perrie Weiner, a partner at Baker McKenzie. "Landlords should be mindful to work things through with their tenants."

Weiner is representing tenants — one of which has roughly 250 stores — in a dispute with landlords over breach of contract. He said that while leases generally have not taken into account pandemics, in many cases there is a viable defense for tenants who haven't paid rent, one of which is the co-tenancy argument.

But while tenants may have a co-tenancy claim, they need to make it clear to judges that COVID-19 actually prevented them from paying rent.

Weiner also suggested that landlords might be better off settling disputes out of court, since it may be difficult to find another tenant if they evict their current tenant.

And supply and demand, as well as the desirability of the location, are also factors, Weiner said.

"Judges won't take kindly to landlords playing hardball," Weiner said. "At top-tier shopping centers, landlords will play more hardball with their tenant. At shopping centers that are not as desirable, landlords have to be more reasonable."

Landlords May Have to Take Action Against Their Lenders

Landlords have been burning the midnight oil for months in attempts to reach agreements with tenants outside of court, and while some owners have been able to offer concessions to their occupants, others have found they cannot, due to language in their documents with lenders.

Gayle Klein, a principal at McKool Smith PC, said that has created a vicious cycle that concerns the tenant, landlord and lender and that owners may start to take action against their lenders, seeking permission to grant concessions to tenants.

As with landlord-tenant disputes, owner-lender disputes are still largely occurring outside of court, but that could change soon, experts say.

"I am seeing a lot of posturing, but no triggers being pulled," said Jason Kellogg, a partner at Levine Kellogg Lehman Schneider & Grossman LLP, referring to borrower-lender disputes. "Guns are being drawn, but I think everybody's a little bit hesitant to pull the trigger just yet."

There is another piece of the puzzle, though. Owners who are trying to work with their borrowers on payment of rent, and who in turn are running up against problems with their lenders, could in the future buy an insurance policy that would help the landlord with the initial landlord-tenant dispute.

Insurance to this point generally has not covered pandemics, but that's changing, and owners and lenders are watching that closely.

"Underwriters are looking at that. Lenders are looking at it very carefully," said Robert Reichman, a partner at Greenspoon Marder LLP. "There's definitely going to be a market for this type of insurance."

Expiration of PPP Loans Could Accelerate Litigation

While many landlords and tenants have been able to reach agreements over the last couple months, many of those agreements have worked because of the PPP loans from the CARES Act. While it's likely Trump will sign an extension to the program, the extended PPP relief would end in early August, and that means many of the agreements may need to be modified over the coming weeks, lawyers say.

"We're at the very beginning of it," Baker McKenzie's Weiner said, speaking of litigation. "A lot of [tenants] got PPP relief under the CARES Act to get them through. As that runs dry, tenants will be less likely to pay rent."

Kellogg said many of the three-month agreements he helped landlords and tenants reach are now expiring, and it may be tricky finding new agreements once the PPP loans have also expired.

"Tenants are using some of that [PPP] money, obviously, to carry through with the deals that they've made," Kellogg said. "If that money runs out, it's likely to just make things more contentious."

While the PPP loans' looming expiration is one factor, timing is another.

Mark Levy, a partner at Brinkley Morgan, said landlords and tenants have been holding off on litigation as they look for more clarity both on the pandemic and the access to courts. But many are finding no clarity in sight, particularly with spikes in COVID-19 cases as states start to reopen their economies. That's meant a recent increase in litigation, Levy said, and he expects to see more.

"I've been monitoring it and have seen an uptick," said Emilie Cooper, a partner at Haynes and Boone LLP. "People come to the point where they're unable to make a deal and are saying, 'Let's move forward with other recourse.'"

Weiner expects a "tremendous" rise in litigation once the PPP relief runs out.

And Tad O'Connor, a partner at Kasowitz Benson Torres LLP, also anticipates an increase in litigation.

"Many of the clients I'm advising in the commercial real estate and hospitality industries are working their way behind the scenes though disputes that are likely to end up, one way or another, in litigation," O'Connor said. "Much like what we saw with the 2008 global financial crisis, I think lawsuits will be a lagging indicator of the extreme stress so quickly placed on these industries."

--Additional reporting by Andrew Kragie. Editing by Kelly Duncan and Jill Coffey.