

Assignment and Subleasing in a Changing Business Environment*

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1 *Johnson v. Yousoofian*, 930 P.2d 921 (Wash. App. 1996).

2 James C. McLoughlin, Annotation, *When Lessor May Withhold Consent Under Unqualified Provision in Lease Prohibiting Assignment or Subletting of Leased Premises Without Lessor's Consent*, 21 A.L.R.4th 188 (1983). There is a relationship between this legal principal and the obligation of a landlord to mitigate damages upon a tenant's default. 735 ILCS 5/9-213.1. If the tenant was to default and tender a subtenant to the landlord, landlord may be obligated to accept the tendered tenant in mitigation of the defaulting tenant's damages. See *Scheinfeld v. Muntz TV, Inc.*, 67 Ill.App.2d 8, 214 N.E.2d 506 (1966); *Wohl v. Yellen*, 22 Ill.App.2d 455, 161 N. E. 2d 339 (1959).

The changing business environment provides abundant evidence of the need for tenant flexibility in real estate planning. Store closings brought about by, mergers and consolidations, corporate contraction in the face of profit warnings, new business strategies, and the outsourcing of functions that were once internal all cause the retailer to focus on the disposition of excess or surplus property. On the other side of the equation, new and expanding businesses need space to house start-up and new operations. The ready availability of excess space that is under lease, but not used by another tenant creates opportunities for both parties. These opportunities come with an accompanying set of issues that must be considered in any analysis of the disposal or acceptability of surplus space.

The Lease Terms

It must first be determined that the existing lease allows assignment or subletting under any circumstances. If the lease is silent on the point, the law will generally allow the tenant to assign the lease or sublet the premises. Most modern leases address the tenant's right to assign or sublet. These provisions must be thoroughly reviewed in preparing for an assignment and subletting transaction and factored into the negotiations with the replacement user and the landlord. The clause will dictate who will have the bargaining power, the landlord or the tenant, or in some cases the assignee/subtenant.

Tenants and landlords want to address this balance of power at the outset of the lease transaction. In the initial lease negotiations, the tenant will negotiate for flexibility. National and regional retailers insist that they have the absolute right to assign and sublet, or that the landlord's approval rights be limited. The landlord, on the other hand, wants the tenant's flexibility limited so that landlord will determine who will be the occupants of its property and what the appropriate tenant mix for the shopping center may be. Without this control, the landlord may have a tenant as a competitor leasing space to potential occupants of the landlord's property.

If the parties are sophisticated and expressly agree that the lease may not be assigned or the tenant's interest sublet without the approval of the landlord which may be withheld in the landlord's sole judgment, this provision should be upheld. If, however, the lease provides that the landlord's approval is required, which it impliedly is the case in the absolute prohibition situation, many, but not all courts¹, will imply that such approval or consent may not be unreasonably withheld².

Thus, leases requiring the landlord's approval or consent, and leases while requiring such consent and also providing that such consent will not be unreasonably withheld have the same legal effect.

Leases requiring the landlord to act reasonably in granting or withholding approval may also specifically outline standards that the landlord may employ or factors that the landlord may consider in granting or refusing consent to such transaction? For example, a landlord oriented lease may provide:

Without in any way limiting Landlord's right to refuse to give the consent required in this Section ____, Landlord shall be deemed to have reasonably withheld its consent to any assignment or subletting if, in Landlord's reasonable opinion:

A. The proposed use of the premises by the assignee or subtenant is not compatible with the operation of the Shopping Center or the desired tenant mix of the Shopping Center, or would require that increased services be provided by the Landlord;

B. The financial net worth of the proposed assignee or subtenant is less than that of the Tenant;

C. The proposed assignee or subtenant is a governmental agency or an instrumentality of a governmental agency;

D. The proposed assignment or sublease would cause a violation of another lease for space in the Shopping Center or would give an occupant of the Shopping Center a right to terminate or cancel its lease;

E. The proposed assignee or subtenant's use of the Premises would involve the introduction of Hazardous Materials to the Premises;

F. The proposed assignee or subtenant is a current tenant of the Shopping Center or an entity with whom Landlord is negotiating to lease space in the Shopping Center; or

G. The Tenant is in default under any of the terms of this Lease as of the date that Tenant notifies the Landlord of the proposed assignment or subletting, or as of the effective date of the assignment or subletting.

3 *Vranas & Associates, Inc. v. Family Pride Finer Foods, Inc.*, 147 Ill.App.3d 995, 498 N.E.2d 333 (1086); *Jack Frost Sales, Inc. v. Harris Trust and Savings Bank*, 104 Ill.App.3d 933, 943, 493 N.E.2d 941 at 949 (1982).

4 *Losurdo Brothers v. Arkin Distributing Company*, 125 Ill.App.3d 267, 465 N.E.2d 139 (1984).

5 *Jack Frost Sales, Inc. v. Harris Trust and Savings Bank*, 104 Ill.App.3d 933, 946, 433 N.E.2d 941 at 950 (1982).

6 *Regent v. Dempsy-Tegler & Co.*, 70 Ill.App.2d 32, 216 N.E.2d 500 (1966).

Even if the lease is not so explicit, the tenant who seeks to assign or sublet must tender a suitable subtenant or assignee who is ready, willing and able to assume the lease³, and give the landlord a reasonable period of time to evaluate the proposed transaction⁴. The landlord has the ability to determine that tendered assignee or subtenant is a commercially reasonable substitute for the original tenant⁵.

The determination of the acceptability of the proposed subtenant or assignee may be based upon: the financial responsibility and payment history⁶ of the tendered party, including those who will enhance the credit of that party by executing a guar-

anty or providing other security for the party's performance; the type of business to be conducted by the assignee or subtenant and whether it competes with the business of the landlord or the other tenants and whether the premises are suitable for the use intended by the proposed transferee; the tenor of the enterprise to be conducted at the demised premises, including the impact upon the shopping center in which the demised premises are located; whether the use of the premises by the subtenant or assignee is legal and will be consistent with the uses permitted under the use clause of the lease; and the character of the proposed assignee or subtenant.

In many instances, the landlord's decision will be based upon subjective factors. These unmeasurable criteria may not be enough if the landlord's decision is challenged. The landlord may have to demonstrate that it relied upon objective factors or evidence, rather than its judgment alone in deciding to withhold its approval of an assignment or sublease. In any instance, the landlord must focus on the intended transferee or the transferee's use of the premises.

The lease may set out a procedure for the tenant to follow in seeking the landlord's approval of a sublease or assignment. Some leases may require that prior notice of the transaction proposed by the tenant be given to the landlord. Other leases may allow the tenant to assign or sublease at will, and merely notify the landlord after the transaction is completed. If the lease provides that the landlord must approve or consent to an assignment or sublease, the lease may also require that certain information be given to the landlord at the time that consent is sought so that the landlord will have the information needed to make an informed decision. As sample clause may read:

If Tenant desires to assign this Lease or sublet the Premises or any part thereof, Tenant shall submit to Lanlord, not less than (____) days before the proposed effective date of the transfer:

A. A request for permission to transfer setting forth the proposed effective date which shall be no less than _____ (____) days after the sending of such notice;

B. The name of the proposed subtenant or assignee;

C. The nature of the business to be conducted in the Premises after such transfer;

D. The terms and provisions of the proposed agreement to assign this Lease or sublet the Premises to such subtenant or assignee;

E. A copy of all proposed documentation pertaining to the transfer;

F. Current financial statements (audited, if available) of Tenant and the proposed subtenant or assignee; and

G. Such additional information that Landlord may reasonably request in order to enable it to make a reasoned judgment.

The assignment provision of the lease may require that the tenant give notice to the landlord some time prior to the effective date of the assignment. If this prenotice period is relatively short, perhaps ten to fifteen days, it will not likely of itself disrupt the transaction. If, on the other hand, the prenotice period is long, it may well have the practical effect of precluding assignment or subletting. Few prospective assignees or subtenants will be willing to wait sixty, or in some cases, ninety days while the landlord determines whether it will or will not consent to the transaction. Potential assignees and subtenants do not want to invest the time and money for feasibility studies and legal and architectural consultations, let alone the executive time, and forego other opportunities only to be met by a long silence and possible rejection from the landlord.

This should not, however, prevent the tenant and would-be assignee or subtenant from trying to make a deal. Perhaps the landlord can be encouraged to shorten the time for a decision. Landlords will not, however, be willing to do this for nothing. The landlord will likely want something to give up its right to ponder.

Perhaps the benefit to the landlord will come by the tenant giving the landlord a share of any bonus rental or compensation that the tenant will receive. The proposed new occupant may bring some advantage from its mere presence in the center. For example, if the proposed occupant is a hot new retailing concept, restaurant or entertainment venue that would heighten the visibility and paying traffic of a shopping center, the landlord may well want to encourage and facilitate, rather than frustrate the assignment. The entry into the center of a new high-volume business may increase the percentage rent paid to the landlord for the premises and from other tenants. If this is the case, the bargaining leverage may well shift to the tenant who has the favored user in hand ready to add zest to a flagging center.

The lease review process must look beyond the assignment and subletting clause to the other clauses of the lease that affect the ability of the tenant to assign or sublet. For example, the use clause may limit the use of the premises to the business of the original tenant, rather than allowing any lawful use. If that is the case, and the landlord refuses to amend the use clause, the tenant is left to assign or sublet only to a competitor, a step most will be unwilling to take. Additional due diligence should include a review of the use and restriction provisions of the reciprocal easement and operating agreement, and other covenants, conditions and restrictions affecting the shopping center as a whole. These also may control the use of the premises, thereby restricting the tenant's efforts to dispose of this surplus property. Even clauses that set a high standard for the type of insurance to be carried by the tenant may have a chilling effect, if the proposed replacement user has a blanket insurance program with an insurer of lower standing.

Some leases have other provisions that impact a subletting or assignment in a subtle and less direct manner. These constraints may be found in clauses that permit only certain signage by the tenant, potentially preventing the type of signs an assignee may require. The lease may limit the number of doors to the prem-

ises, thus preventing a sublease to a tenant that naturally wants its own main entrance and storefront doors. Provisions that prohibit exterior renovations may preclude an assignment to a user that requires a prototype exterior, such as a theme restaurant.

The lease is both a transfer of an interest in real estate and a contract. Typically, the tenant will be liable to the landlord under the lease just as any other contract. When a lease is assigned from the original tenant to an assignee, the parties will enter into an assignment and assumption agreement. Through this document, the lease will be formally assigned to the assignee and the assignee will assume and agree to perform the tenant's obligations under the lease. Another contract is formed. Through the assignment and assumption agreement the tenant's estate is passed to the assignee and the parties agree upon the continuing liability under the lease.

Different tenants focus on different methods to achieve profitability. Some tenants have large and valuable real estate portfolios. These real estate users focus on enhancing overall corporate profitability by supplementing operating income with gains from the disposition of surplus real estate. Other tenants, while not eager to forego real estate gains, focus on the profits of their core business. If the retail philosophy changes for example by changing the basic size of its stores, the retailer will often relocate. Profiting from the resulting real estate termination does not drive the transaction. Repositioning without loss is the goal.

Landlords, by definition, are in the real estate business. They profit by getting the maximum return that the real estate can generate. Landlords typically do not want their tenants as their competitors. For this reason, landlords may include a recapture clause in the assignment/subletting provisions, or provide that the landlord may not consent to the assignment or subletting if the landlord has other or comparable space available for lease.

Through the recapture clause, the landlord can take back the space and lease it anew to a prospective tenant, including a prospect brought to the deal by the existing tenant's efforts. Obviously, the landlord will only exercise this right if it can do so at a gain. If market rental rates have increased since the making of the lease, as is likely to be the case if the lease was executed in the late 1980s or early 1990s, the landlord may well want to recapture the space, terminate the existing lease and relet the space to the prospect brought to the property by the existing tenant at a rental rate higher than that paid by the existing tenant.

For the tenant focused on its core business rather than real estate profits, this is an acceptable result. Tenants should, however, negotiate with the landlord to have their costs of the deal paid out of the excess of the rent paid to the landlord by the replacement tenant over the rent that would have been paid by the original tenant.

If the replacement user deals directly with a landlord, tenant inducements will usually be negotiated. The landlord will give a period of free rent, the cost of some tenant improvements, and perhaps reimburse the tenant for other costs to get the tenant into the project. These costs are then included in the rent. Depending on market conditions, the sublandlord or assignor will likely not give these inducements to the replacement user. While a period of free rent may be available to

allow time for the refitting of the space, in today's economy it is unlikely that the replacement user will receive a tenant improvement allowance from the original tenant or have the original tenant undertake to refit the space to the assignee's specifications. This factors back to whether the replacement user is getting a market deal.

If the lease is relatively recent, market conditions may not have changed much. As a result, the rent paid (and now sought to be received) by the original tenant will include both the pure rent for use of the space and a component designed to repay the landlord for the cost of the tenant improvements given to the original tenant, improvements that the replacement user will at least remodel, or perhaps demolish. Thus, if the replacement user pays the same rent that the original tenant is obligated to pay, the replacement user will be paying the amortization of the original tenant's improvements and often paying out of pocket for its own refurbishment of the space. Will that arrangement result in the payment of above-market all-in cost of the space for the replacement user? This analysis must be made.

The rent paid under the lease includes basic rent, adjustments such as contributions for landlord's real estate taxes, insurance and operating expenses, and sometimes percentage rents. While an assignor or sublessor may be willing to give a short rent concession to allow the replacement user to open for business before being obligated to pay rent, sometimes that concession only relates to basic rent. Rent adjustments or additional rent to reimburse the landlord for real estate taxes and operating expenses may commence at execution or shortly thereafter.

Percentage rents create a difficult situation. The landlord is entitled to percentage rent based upon the sales of whoever the space user may be. For this reason, the original tenant will seek to receive from its replacement the percentage rent that it must pay to the underlying landlord. The replacement user may object if the percentage rent factor is not appropriate for this type of user. Different types of retailers operate on different margins. A percentage rent that is appropriate for a lower volume but high margin seller may be totally unacceptable to a lower margin, high volume seller.

Generally the underlying lease is taken as it is, with its economic terms. If the original tenant and assignee or subtenant approach the landlord to try to change those terms, the landlord may want some compensation in exchange.

In the typical new leasing transaction, tenant improvement costs are partially or totally paid by the landlord and repaid by the tenant as part of rent. The landlord is not part of the subleasing or assignment transaction to pay these costs. Without the landlord, who else is available to pay these costs? Only the assignor or assignee. Since the assignor is not in the real estate business, it will not receive a return on these costs other than the relief it obtains from the cost burdens of the rent and other charges relating to the surplus property. If the assignee pays these costs, it may be paying more than the market rental value for the property, unless the rent is below current market rates. Except for those cases where the surplus property is a "bulls eye" location for another retailer or is otherwise key to the assignee's operation, leasing space directly from the landlord may be a better economic alternative for a prospective tenant. This economic reality makes assignment and subleasing economically unattractive for many.

In making a new lease, a retail tenant knows how long it will take to develop and mature its sales in the market of the new leased premises. Other users have a business plan that helps predict how long they will need the space based upon projections of business expansion. The assignee or subtenant typically takes the lease as it finds it. Unless separate negotiations are conducted with the landlord, whatever the balance of term there may be in the lease is what will be available to the assignee or subtenant. If term length is crucial, the tenant and assignee will have to make a joint proposal to the landlord to recast to term of the underlying lease. This of course shifts the leverage largely to the landlord.

Options to Renew

The potential taker of the space must carefully analyze the remaining term of the lease, including options. The first level of due diligence in this area is to make sure that the options may be exercised by the assignee. Because of the concessions made by landlords to highly creditworthy national retailers, leases will sometimes provide that the renewal right may not be exercised by an assignee or subtenant. While the landlord may be willing to extend itself to the national retailer or other high credit tenant to attract that tenant to the property for the drawing power and prestige associated with its presence, that star power may not be associated with the assignee. Especially where the tenant has negotiated for free assignability, the renewal of the lease may be personal to the original tenant.

The sublease situation presents an additional and different renewal term issue for the subtenant. Typically, the subtenant is not in privity of contract with the landlord, and therefore cannot exercise the renewal right. Stated otherwise, the landlord is generally not obligated to recognize the subtenant's exercise of the renewal option. While the sublease itself may obligate the sublandlord to exercise the renewal option at the direction of the subtenant, what happens if the sublandlord breaches its covenant, or perhaps cannot be found to exercise the renewal option that is critical to the sublessee's operation at the premises?

One device that may be employed is to make the subtenant the attorney in fact for the sublandlord for the sole purpose of exercising and enforcing the renewal rights given to the tenant under the lease. This appointment is coupled with an interest and should be so stated and be irrevocable. A sublease provision creating this attorney in fact relationship follows:

If Subtenant notifies Sublandlord of Subtenant's election to exercise an option to renew the term of this Sublease and concurrently cause the renewal of the term of the Lease, Sublandlord shall immediately take all steps required under the Lease to exercise the next option to renew the term of the Lease and provide to Subtenant evidence of such exercise. If Sublandlord does not exercise the next option to renew the term of the Lease and provide Subtenant with evidence of such exercise within ____ (____) days after Subtenant's notice to Sublandlord of Subtenant's exercise of such option to renew, Sublandlord hereby appoints Subtenant as its attorney in fact, which appointment is coupled with an interest and is therefore irrevocable, to exercise such renewal option under the Lease in the name, place and stead of the Sublandlord.

Alternatively, or perhaps as a suspenders and belt approach to the protection of this valuable right, if the subtenant is able to obtain an estoppel or nondisturbance agreement from the underlying landlord as part of the subleasing transaction, consideration should be given to seeking the agreement of the landlord to recognize the exercise of this renewal right by the subtenant. If the landlord is willing to acknowledge the subtenant's rights in this regard, the estoppel or nondisturbance agreement should so state and the uncertainty will be greatly reduced for the subtenant.

While by its nature, the assignment will confer upon the assignee the renewal terms available under the lease, in the sublease situation, the lease term and sublease term may not be symmetrical. It is frequently the case that the sublease terms, both initial and renewal, will not begin and end at the same time as the lease terms.

The sublandlord will want adequate time to process the subtenant's renewal notice by making the renewal notification to the underlying landlord. For this reason, it is frequently necessary for the subtenant to give the renewal notice four to eight weeks before the notice is due to the underlying landlord. The subtenant will want evidence that the sublandlord in turn gave the renewal notice to the underlying landlord. Failing the receipt of that evidence that the renewal notice has been given, the subtenant will want time to react by giving its own notice to the landlord either as attorney in fact for the tenant/sublandlord, or pursuant to the recognition arrangement set out in the estoppel or nondisturbance agreement between the subtenant and the landlord.

From the sublandlord's perspective, it is important that the time remaining in the initial and renewal terms at end of the sublease terms is appropriate to allow the premises to be vacated before the holdover penalties apply under the underlying lease. Also, the sublandlord does not want to have dead rent time at the end of the sublease term when rent is not being paid under the sublease and rent is to be paid under the underlying lease.

The sublessee has rid itself of the financial cost of the surplus lease. It does not want to have more of that cost in later years. Once the cost of the subleasing transaction is booked, future operations should not be taxed by later dead rent periods.

Nondisturbance Agreements and Estoppels

Since the subtenant is in possession of the space and the sublandlord is in an intermediary position with direct privity with the landlord, the subtenant must be certain that the sublandlord takes no action that will prejudice the subtenant's rights. Most obvious is a termination of the underlying lease. The landlord and tenant could freely agree to terminate the lease. This event would have obvious adverse consequences upon the subtenant's interest. For this reason the subtenant should negotiate for a nondisturbance agreement with the underlying landlord. Most leases, however, do not require the landlord to engage in any such negotiations or give any such protection to the subtenant. Indeed, many landlords will not cooperate in this effort and will not give either the sublandlord or the tenant any document or agreement that is not required by the express terms of the underlying lease.

Typically, the assignee will only agree to assume the lease liability accruing after the assignment, and will not agree to be responsible for any pre-assignment defaults. While this may be the agreement of the assignor and assignee, it is not binding upon the landlord. If there are preassignment defaults by the assignor, the landlord can resort to all of its rights and remedies under the lease and applicable law. To guard against that possibility, the assignee will often obtain an estoppel certificate from the landlord. Through the estoppel, the assignee has the comfort that the landlord will not claim the existence of a pre assignment tenant default. Some leases at least require the giving of a generic estoppel certificate, or the landlord may be willing to give a very bland estoppel if a request is made by the tenant. At a minimum, the subtenant or assignee wants certain information confirmed. First, it must be confirmed that the lease with which the parties are dealing is indeed the correct lease, with all amendments, and that such lease, as amended, is in full force and effect. The taker of the lease also wants to know that there are no pending defaults under the lease, or if so what those defaults may be. The assignee or subtenant would like to receive a simultaneous copy of any notices given by the landlord to the tenant.

If possible, the sublessee/assignee would like to have the estoppel confirm other information, such as the length of the term, its commencement date and termination date, the number and length of extension options, the time within which notice of the exercise of an extension option is to be given, the amount of rent, taxes, CAMs and other costs payable by tenant, and the date through which such amounts have been paid. Some subtenants would like to go further to rewrite the lease through the estoppel, by modifying or excising offensive provisions. Landlords understandably resist these efforts, unless there is some benefit to them of opening negotiations with the successor occupant of the premises.

Estoppel certificates may seek the landlord's knowledge of certain facts. For example, an estoppel may ask the landlord to state whether it knows of any pending or threatened litigation, including eminent domain or building code matters, relating to the property, and whether the property is contaminated with hazardous substances. Landlords are reluctant to give these statements, especially, those relating to environmental matters or the condition of the premises. The estoppel can, however, be used to change the notice address to the tenant, and to obtain the landlord's agreement to accept a notice of renewal or extension from the assignee or subtenant, if the notice is otherwise given in conformity with the requirements of the lease.

An example of an estoppel for a sublease transaction follows on the next page.

ESTOPPEL CERTIFICATE

_____, 200_

_____ ("Subtenant")

Re: Lease ("Lease") dated as of _____, _____ made by and between _____ ("Landlord") and _____ ("Tenant") as amended, modified or supplemented by _____ (collectively the "Lease") relating to the property commonly referred to as _____, _____, _____, and which is part of a shopping center (the "Shopping Center").

Ladies and Gentlemen:

Subtenant has entered, or is contemplating entering, into a Sublease Agreement (the "Sublease") with Tenant, under which Subtenant will sublease the premises demised by the Lease, as more particularly described in the Sublease (the "Premises"). It is a condition to Subtenant's obligations under the Sublease that Tenant obtain this Estoppel Certificate. To enable Tenant to satisfy such condition, and for other good and valuable consideration, Landlord hereby certifies to Subtenant as follows:

1. Landlord has not assigned or otherwise transferred its interest as landlord under the Lease, except as described above.

2. The initial term of the Lease commenced on _____, _____, and will expire on _____, _____.

3. The Tenant has _____ options to renew the term of the Lease each for a period of _____ years.

4. The Lease as described above constitutes the entire agreement of Landlord and Tenant with respect to the Premises, is true, correct and complete, has not been modified or amended, and is in full force and effect.

5. Tenant has commenced payment of monthly fixed rent under the Lease and such rent has been paid for the period ending on _____, _____.

6. Landlord is not in default in its obligations under the Lease, and to the Landlord's knowledge, there are no defaults of Tenant under the Lease and to the Landlord's knowledge there are no existing circumstances which with the passage of time, or the giving of notice, or both, would give rise to a default under the Lease.

7. To Landlord's knowledge, no hazardous or toxic waste, substance or material, or contaminants, oil, pesticides, or radioactive materials have been generated, stored, handled or otherwise dealt with on the Premises.

8. Landlord has not received any written notice of any pending or threatened litigation, including eminent domain proceedings, relating to the Premises or the Shopping Center, and Landlord has no knowledge of any state of facts that could result in such litigation.

9. Concurrently with the giving of any notice to Tenant Landlord shall give a copy of such notice to Subtenant at the address set forth above.

The certifications contained herein are made in the knowledge that Subtenant, as a prospective subtenant of the Premises, will place substantial reliance thereon.

Very truly yours,

_____, a

By: _____

Its: _____

The subtenant should, attempt to have the landlord agree to give to the sublessee or assignee copies of all notices that are given to the tenant, and agree not to terminate, amend or modify the underlying lease without the subtenant's prior written consent. This protects the foundation upon which the sublease is built.

Leases typically give the tenant the ability to terminate the lease upon the happening of events beyond the control of the parties. Examples of such right are found in the casualty and condemnation clauses. If, for example, the premises are materially damaged, or more than an inconsequential amount of the premises are taken by eminent domain, the tenant may be able to terminate the lease. Especially in the subleasing situation, the tenant's natural reaction to such an event or opportunity would be to exercise its termination right, thereby eliminating any further possibility of liability to the landlord.

The subtenant is in a different situation. Presumably, the subtenant is conducting its business operations at the premises and may want to continue to do so. If there is a material damage to the premises as a result of a casualty, or a taking of a material part of the premises, the subtenant wants to control the decision of whether or not the lease should be terminated. To prevent the termination of the underlying lease without the subtenant's approval or participation in the termination decision, the sublease must limit the sublandlord's ability to act. The sublandlord should agree to give any notices it receives from the landlord to the subtenant, and to not take any action to amend, modify or terminate the underlying lease without the subtenant's prior written approval.

Since the assignee's or subtenant's rights are derivative of the rights of the tenant under the underlying lease, the assignee or subtenant must confirm the exact nature of those rights. This is typically done through the use of a simple device,

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the estoppel certificate requested from the landlord.

The first question to be considered is whether the landlord is required to give an estoppel. Many leases do not require the landlord to do so. Institutional and sophisticated heavy users of space, knowing that subleasing and assignment are possible, build this requirement into their form leases. Even if the landlord is not required to give an estoppel, the tenant's request for one may be honored, if the requested estoppel is not aggressively drafted.

Typically, the subtenant is not in privity of estate with the underlying landlord. The subtenant's rights are through the sublessor. Since there is no direct relationship between the landlord and the subtenant, and the subtenant's rights are built upon the sublandlord's rights as tenant under the lease, the subtenant will lose its rights if the underlying lease terminates for any reason. As a result, a subtenant will want a direct contractual relationship with the underlying landlord to continue its tenancy under the terms of the sublease if the underlying lease should be terminated. This is accomplished through a nondisturbance and attornment agreement entered into between the subtenant and the underlying landlord.

Through this device, the landlord agrees to recognize the subtenant's rights under the sublease if the tenant's rights under the lease should be terminated, or if the underlying lease should terminate. This protects the subtenant from the loss of its possessory rights if the underlying lease is terminated because of a default by the tenant or for some other reason, without the subtenant's consent or approval. Of course, the subtenant must not be in default under its obligations under the sublease, and the landlord will typically not want to be responsible for the prior defaults of the sublessor under the sublease. Even with its shortcomings, the nondisturbance agreement is an essential part of any sublease transaction, if it can be obtained. Leases may not require the landlord to give the NDA, and because it substantially impacts upon the landlord's rights in the event of the termination of the underlying lease, landlords are reluctant to enter into this agreement without some consideration.

The assignment and subleasing situation is the only alternative that the tenant seeking to rid itself of surplus lease obligations can utilize, short of buying its way out of the lease or disaffirming the lease in bankruptcy. That there is a market for these transactions is evident by the thousands of leasehold dispositions occurring annually.