THE PROBLEM-SOLVING TOOL FOR RETAIL LAW

RETAIL LAW STRATEGIST

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NEW!

Q&A

This feature summarizes discussions among commercial real estate lawyers about issues that arise in their practice. Those discussions are hosted by Joshua Stein (a Partner with Latham & Watkins LLP and a member of this newsletter's editorial board) and Robert M. Safron (a Partner with Patterson Belknap Webb & Tyler LLP). The editorial staff of this newsletter prepared the summary below. You may e-mail your anonymous question or comment to smcevily@icsc.org.

QUESTION: In your experience, is it universally necessary to present the *original* letter of credit (L/C) when making a drawing on the L/C? I always thought that it was an absolute requirement, but I recently heard that one can submit a sight draft of an L/C and the issuer will pay, even without the original L/C. Have you ever done this? If so, how do you make sure that no one submits a fraudulent sight draft or misdirects the L/C proceeds? Would it be

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Defaults and Remedies in Retail Leases

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Introduction

The slow economy has many retail tenants evaluating store closures, abandoning store openings and even seeking bankruptcy protection. Leases for the subject stores have a material impact on these decisions. This article briefly summarizes the key issues affecting landlord and tenant defaults and their respective rights and obligations under common lease provisions.

What Is a Default?

Obviously, a failure to perform a lease obligation constitutes a default. However, many leases contain notice and cure rights in favor of both parties. Most leases also contain detailed provisions governing the method for delivering notices, including a notice of default, between the parties. Until the non-breaching party gives the proper notice and opportunity to cure, an actionable default has not technically occurred. Leases may also carefully limit what type of non-performance constitutes a default by including "materiality-qualifiers." Furthermore, the failure to insist on strict performance of all lease provisions could lead to a waiver of the right to enforce them in the future. Carefully drafted leases address all of these issues by specifically defining the actions or inactions that constitute defaults, providing a clear procedure for providing notice of defaults and even providing that a waiver of one default does not waive the right to insist on performance in the future.

Typical Lease Remedies

Retail leases are contracts *and* instruments affecting the possession of real property. As such, general contract remedies are available to the non-breaching party. However, in most default situations, the tenant still has possession of the premises that the landlord would like to recover. As with all contract breaches, the non-breaching party must make reasonable attempts to mitigate its damages. In the lease context, this generally means attempting to re-let the premises.

Depending on the language of the lease, if the landlord repossesses the premises and/or re-lets it, those acts could terminate the lease and the tenant's obligations to pay any future rent not yet due. Some leases, particularly those with less sophisticated "local" tenants, contain an acceleration clause that allows the landlord to pursue all rent remaining on the lease immediately upon a default; however, many tenants usually will not agree to this. Instead, an experienced tenant may agree that, should the landlord repossess the premises, such action will

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sufficient protection if the L/C identifies the account into which payment will be made? What has your experience been?

ANSWER: We have presented many letters of credit (L/Cs) for payments that we are holding as security deposits. Most L/Cs require the original to be presented with a sight draft. It depends on what the L/C states is necessary for payment. We have been able to have the issuing bank accept a fax copy of the L/C along with a copy of a sight draft, especially when the L/C department of the bank is located in an out-of-town branch. If we represent the landlord, we give the tenant the form we want; then we review the proposed draft of the L/C and try to get the issuing bank to give us what we want in order to make the payment easier. Our success depends on the issuing bank. The L/Cs do not state the account into which the money will be wired.

When obtaining an L/C as part of some security requested by a lender, there is usually no requirement, even for a sight draft. Rather, the L/C just states that upon presentment to the issuing bank, the L/C would be paid to the beneficiary—in this case, the lender. Although we have been the beneficiary of many L/Cs, we have never dealt with the issue of a bank's concern about fraud. We just send the L/C (original or fax) with a sight draft (using the exact language written in the L/C) stating that the tenant is in default. The L/C is signed (but not notarized) by the authorized person of the beneficiary entity; we also include a letter signed by the authorized person explaining to the issuing bank where the money should be wired. Provided the beneficiary complies strictly with the requirements to be paid, the issuing bank usually pays the L/C in 24 to 48 hours. Here is a sample:

We hereby issue this irrevocable Letter of Credit No. _____ in your favor for the account of _____ (the applicant), for _____ (U.S. Dollars) available by your draft(s) drawn on us at sight, accompanied by the following: the original of this letter of credit and amendments, if any. In addition, presentation of such draft may also be made by fax transmission to fax No. _____ or such other fax number identified by _____ in a written notice to you. To the extent a presentation is made by fax transmission, you must (i) provide telephone notification thereof to _____ (phone No._____) prior to or simultaneously with the sending of such fax transmission and (ii) send the original of such draft to _____ by overnight courier, at the address provided below for presentation of documents, provided however, that _____s receipt of such telephone notice or

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not be deemed a termination of the lease, and the landlord may make such renovations as it deems necessary to re-let the premises for the benefit of the tenant's account. The landlord would retain any positive difference between the old and new rent, and the tenant would pay any negative difference.

Both parties must consider the terms of re-letting. The landlord will want to re-let to the original tenant on any reasonable terms, whereas the tenant may want the landlord to re-let to the first willing tenant. At the very least, the landlord must retain the right to reject potential replacement tenants who are not creditworthy or whose business does not fit the appropriate tenant mix for the shopping center. The original tenant will also want such a re-letting to terminate its obligations under the original lease; the landlord will want the original tenant to remain as a virtual guarantor of the tenant's obligations.

Bankruptcy

Pre-Bankruptcy

In addition to the many challenges faced by the landlord upon default by the tenant, the landlord will have to climb an even steeper hill if the tenant files for bankruptcy protection. A landlord can use several methods, outlined below, prior to the tenant's filing bankruptcy, however, to possibly avoid bankruptcy altogether:

- Terminate the lease prior to the filing of a bankruptcy petition. This requires a landlord to be proactive and aware of the tenant's financial condition at all times. A diligent landlord will act quickly upon an event of default and pursue the applicable termination and eviction action. Termination of the lease alone is not sufficient. The landlord must also take possession of the premises. If the tenant is still in possession on the date of the bankruptcy petition, the automatic stay can prevent the landlord from evicting the tenant.
- The landlord obtains a guaranty from a solvent third party that is not closely related to the tenant-debtor. The Bankruptcy Code only prohibits action against the debtor and the debtor's estate. An action on a guaranty against a non-related third-party guarantor is not prohibited, and may give the landlord a viable option for collection.

When a tenant files for bankruptcy protection, the "automatic stay" effectively halts all collection and/or eviction proceedings against the tenant-debtor. The debtor's interest in the lease will become "property of the bankruptcy estate."

- A judgment for possession. Pursuant to 11 U.S.C. § 362(b)(22), the automatic stay does not bar an eviction action if the landlord obtained a judgment for possession prior to the filing of the bankruptcy petition. Under some circumstances, a tenant-debtor may obtain a limited 30-day stay, but only if the debtor satisfies any arrears in rent by the end of such 30-day period. Again, a landlord must be proactive in its management of the premises, and should also consider negotiating with the tenant to reduce the past-due amount in exchange for a voluntary judgment for possession.

Bankruptcy

If the landlord is not successful in avoiding the bankruptcy, it should be aware of certain basic bankruptcy rules.

When a tenant files for bankruptcy protection, the "automatic stay" effectively halts all collection and/or eviction proceedings against the tenant-debtor. The debtor's interest in the lease will become "property of the bankruptcy estate." The effect of this is that the landlord's self-help and eviction rights are halted. Even if the landlord was successful in obtaining a judgment, the automatic stay precludes the landlord from enforcing the judgment.

A basic understanding of the most common steps in bankruptcy can assist the landlord in protecting its interest. Upon the filing of a bankruptcy petition by a commercial tenant, the bankruptcy trustee or the debtor-tenant is required to:

1. Begin performing the tenant's obligations under the lease immediately after filing, unless the court extended the time for doing so for up to 60 days for cause, pursuant to 11 U.S.C. § 365(d)(3);
2. Assume or reject the lease within 120 days after the order for relief, unless the court extended that time (the landlord's written consent is required to extend that time an additional 90 days), pursuant to 11 U.S.C. § 365(d)(4); and
3. Surrender the property to the landlord at the end of the 120-day to 210-day period, unless the lease had been assumed or the period extended with the landlord's agreement, pursuant to 11 U.S.C. § 365(d)(4).

The debtor-tenant also has the option to assign the lease to a third party if

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Changing Strategies to Maximize Landlord Bankruptcy Claims

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The rule that a landlord's claim for damages when its lease is rejected is limited to one year's rent, plus the pre-filing arrearage, is not as absolute as many tenants have argued and many landlords have accepted. Recent bankruptcy cases have recognized damages that are not subject to the § 502(b)(6) cap. There are damages that, while recognized and the financial impact is felt by the landlord upon lease rejection, do not, according to these court decisions, result from the termination of a lease within the meaning of § 502(b)(6) and, therefore, are not subject to the cap. While not all bankruptcy courts agree, some courts are focusing closely on the key phrase: "resulting from the termination of a lease of real property."

Section 502(b)(6)(A) of the Bankruptcy Code provides in pertinent part, as follows:

> (b) The court ... shall determine the amount of such claim ... except to the extent that ...
>
> (6) such claim is the claim of a lessor for damages resulting from the termination of a lease of real property, such claim exceeds—
>
> (A) the rent reserved by such lease, without acceleration, for the greater of one year, or 15 percent, not to exceed three years, of the remaining term of such lease, following the earlier of—
>
> (i) the date of the filing of the petition; and
>
> (ii) the date on which such lessor repossessed, or the lessee surrendered, the leased property.

11 U.S.C. § 502(b)(6)(A).

Typically, one thinks of such damages as the loss of future rent. In the context of capping the loss of future rent, a number of bankruptcy decisions have addressed the definition of "rent" for purposes of calculating the § 502(b)(6) cap. For example, *In re McSheridan*, 184 B.R. 91 (B.A.P. 9th Circuit 1995) (defining rent to include charges (i) designated as rent in the lease, (ii) related to the value of the leased property, and (iii) payable periodically), is often cited.

The assumption that all damages suffered by the landlord when its lease is rejected are subject to the § 502(b)(6) cap was successfully challenged in *In re El Toro Materials Company, Inc.*, 504 F.3d 978 (9th Cir. 2007). That case involved a tenant who had a duty to maintain the property in compliance with law, but nevertheless stockpiled "goo" from its mining operations—namely, debris deposits remaining after washing sand from the mined materials that created the goo in question (an activity that apparently was anticipated in the lease).

The cost to remove the goo was estimated at $23 million, the magnitude of which dwarfed the monthly rent due of $28,000. The Ninth Circuit in *El Toro* simply reasoned that the rejection claim for rent is limited under § 502(b)(6), as landlords can re-let the leased premises and collect rent from others to compensate for the loss of rent triggered by lease rejection. However, the Ninth Circuit found that the ability to re-let does not mean that a landlord should also be prohibited from claiming for "collateral damage" beyond the rent loss. Otherwise, the Ninth Circuit reasoned that a bankrupt tenant could burn down the leased premises and then assert that the rejection cap limited its liability to the landlord to the § 502(b)(6) cap, despite the value of the property destroyed.

The Ninth Circuit described the existence of the goo as collateral damage that the landlord sustained and found it to be separate from rental damages, which the Bankruptcy Code anticipates that landlords are in the unique position of being able to mitigate, by leasing the premises to another during the remainder of the lease term cut short by lease rejection.

The court explained its rationale of what damages are capped by § 502(b)(6) as follows:

> One major purpose of bankruptcy law is to allow creditors to receive an aliquot share of the estate to settle their debts. Metering these collateral damages by the amount of the rent would be inconsistent with the goal of providing compensation to each creditor in proportion with what it is owed. Landlords in future cases may have significant claims for both lost rental income and for breach of other provisions of the lease. To limit their recovery for collateral damages only to a portion of their lost rent would leave landlords in a materially worse position than other creditors. In contrast, capping rent claims but allowing uncapped claims for collateral damage to the rented premises will follow congressional intent by preventing a potentially overwhelming claim for lost rent from draining the estate, while putting

landlords on equal footing with other creditors for their collateral claims.

The statutory language supports this interpretation. The cap applies to damages "resulting from" the rejection of the lease. 11 U.S.C. § 502(b)(6). Saddleback's claims for waste, nuisance and trespass do not result from the rejection of the lease—they result from the pile of dirt allegedly left on the property. Rejection of the lease may or may not have triggered Saddleback's ability to sue for the alleged damages. But the harm to Saddleback's property existed whether or not the lease was rejected. *Id.* at 980–981.

The *El Toro* court says that a "simple test" can be formulated to determine whether the damages are subject to the cap:

A simple test reveals whether the damages result from the rejection of the lease: Assuming all other conditions remain constant, would the landlord have the same claim against the tenant if the tenant were to assume the lease rather than rejecting it. Here, Saddleback would still have the same claim it brings today, had El Toro accepted the lease and committed to finish its term: The pile of dirt would still be allegedly trespassing on Saddleback's land and Saddleback still would have the same basis for its theories of nuisance, waste and breach of contract. *Id.* at 981.

This "simple" test leaves many issues unresolved. For example, how would this test apply to damages suffered by a tenant's failure to maintain the roof or sewage system, clear the walkways and parking areas of snow and ice, allow the parking lot to deteriorate, or insure the premises from casualty? The Ninth Circuit in *El Toro* did distinguish the future maintenance and utility payments capped under § 502(b)(6) by stating:

McSheridan also holds that damages flowing from the failure of a party that has rejected a lease to perform future routine repairs or pay utility bills are based on lost rent, rent-like payments or other damages directly arising from a tenant's failure to complete a lease term, ..."*Id.* at 982.

capped. 184 B. R. at 95, 102. As the tort claims at issue here are not based on a failure to perform routine maintenance, we do not address the propriety of that holding. *Id.* at 982.

When the court did "not address the propriety of that holding," it meant that the Ninth Circuit chose to limit its ruling strictly to the issues in dispute with this particular property and the landlord's claim. *McSheridan* was overruled only "[t]o the extent that *McSheridan* holds § 502(b)(6) to be a limit on tort claims other than those

El Toro *may have more impact because it was a decision that overruled the* McSheridan *case in part, and refrained from addressing the lack-of-maintenance issue.*

What the Ninth Circuit saw as simple, however, may not be so easily applied. What did the Ninth Circuit mean by "all other conditions remain constant"? If one considers obligations that an assuming tenant would owe, *El Toro* leaves unclear the question of whether such obligations are to be measured solely at the time of assumption (and be limited to continuing duties), or whether they include all obligations that are found in the lease. If the determination is a "snapshot" and not the various duties over time, then it is important that a lease clearly require a tenant to keep the premises in good repair and condition at all times during the lease term and in compliance with all applicable laws, including, without limitation, environmental laws. That way, the bankrupt tenant assuming the lease would have the duty to make what can be very costly repairs and cleanup.

The petition to the U.S Supreme Court for the *El Toro* case gives us more background information as to the lease dispute. Apparently, El Toro's landlord, Saddleback Community Church, with the end of the lease term approaching, sent a default notice to the tenant for stockpiling waste, giving Saddleback 30 days to dispose of the waste. Instead, the tenant filed for bankruptcy and rejected the lease. The landlord filed a proof of claim for $23 million for cost to remove the goo and El Toro responded, objecting to the amount and asserting that all of the landlord's damages were limited by § 502(b) (6). El Toro remained in possession of the leased premises until nearly the end of the seven months remaining in the lease term at lease rejection.

El Toro may have more impact because it was a decision that overruled the *McSheridan* case in part, and refrained from addressing the lack-of-maintenance issue. But, by no means is it the first case to hold that the § 502(b)(6) cap is not a cap on any and all damages that a landlord may suffer and bring a claim against the bankruptcy estate. Michael Busenkell dealt with this issue in his article, published just after the *El Toro* case was rendered: "Does § 502(b)(6) Cap Repair and Maintenance Damages?" 26-Nov. *American Bankruptcy Institute Journal* 34 (2007), cites many cases that found such result.

One result of the *El Toro* decision is that security deposit amount negotiations may change. That is, if there is no absolute bar to recovering more than one year's rent in bankruptcy, then there is less merit to the argument from tenants that it is useless to have a security deposit or letter of credit for a larger amount, as

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certain conditions are met pursuant to 11 U.S.C. § 365(f)(1). If the lease is assumed, the trustee must cure any existing defaults and provide "adequate assurance" of future performance to the landlord. For leases in a "shopping center," the landlord is entitled to "adequate assurance" that (1) the financial condition and operating performance of any assignee be similar; (2) percentage rent will not decline substantially; (3) all other provisions of the lease apply, such as exclusive use clauses; and (4) the tenant mix or balance at the shopping center not be disrupted. "Adequate assurance" that a landlord will be compensated for any pecuniary loss is a condition to the assumption of a lease of real property in a shopping center.

If the lease is assumed, a landlord-creditor must continue its vigilance and monitor the bankruptcy case closely, and should consult with a bankruptcy attorney. In most cases, if the lease of commercial property provides for the landlord to recover its attorney fees upon breach by the tenant, the landlord is entitled to recover, as an expense of administration, fees necessary to enforce the landlord's post-petition rights in the bankruptcy case. The language used by the lease may affect the landlord's ability to recover these fees. Ideally, the lease should provide that the tenant is obligated to pay these fees as they are incurred by the landlord.

Sample Lease Provisions

Several sample lease provisions relating to events of default and consequent remedies follow. These provisions assume that the tenant (a) agreed to operate continuously and (b) is obligated for the payment of percentage rent.

"Event of Default" Defined. Tenant shall be in default of its obligations pursuant to this Lease (each, an "Event of Default") upon the occurrence of one or more of the following:

1. Failure of Tenant to pay any one or more of the installments of Rental, or any other sum provided for in this Lease as and when the same become due;
2. The removal, attempt to remove or permitting to be removed from the Premises, except in the usual course of trade, the goods, furniture, effects or other property of Tenant or any assignee, or sub-tenant of Tenant;
3. The levy of an execution or other legal process upon the goods, furniture, effects or other property of Tenant brought on the Premises or upon the interest of Tenant in this Lease;
4. The filing of a petition in bankruptcy, a petition for reorganization by or against Tenant;
5. The appointment of a receiver or trustee, or other court officer, for the assets of Tenant;
6. The execution of an assignment for the benefit of creditors of Tenant;
7. The vacation or abandonment by Tenant of the Premises;
8. The use of the Premises for any purpose other than for the Permitted Use;
9. Failure of Tenant to exercise diligent effort to produce the maximum volume of sales;
10. The assignment by Tenant of this Lease or the re-letting or subletting by Tenant of the Premises or any part thereof without the written consent of the Landlord;
11. The failure of Tenant to execute and return to Landlord or its counsel any subordination agreement required by a Mortgagee within twenty (20) days of Tenant's receipt of such agreement; or
12. The violation by Tenant of any other of the warranties, representations, terms, conditions, or covenants contained in this Lease, other than the obligation to pay Rental and failure of Tenant to remedy such violation within ten (10) days after written notice thereof is given by Landlord to Tenant.

Acceleration. Upon the occurrence of an Event of Default, the Annual Basic Rental, the Annual Percentage Rental and any Additional Rental provided for in this Lease for the balance of the Term, or any renewal term or other extended term, and all other indebtedness to the Landlord owed by Tenant, shall be and shall become immediately due and payable at the option of the Landlord and without regard to whether or not possession of the Premises shall have been surrendered to or taken by Landlord. The Annual Percentage Rental for which Tenant remains prospectively liable under the provisions hereof shall be a sum equal to the greatest amount of Annual Percentage Rental paid by Tenant for any Rental Year since the commencement date multiplied by the number of years remaining in the Term at the time of such termination. Tenant agrees to pay Landlord, or an agent on Landlord's behalf, a reasonable attorney fee, as incurred, in the event Landlord employs an attorney to collect any rents due hereunder by Tenant; or to protect the interest of Landlord in the event Tenant is adjudged a bankrupt; or legal process is levied upon the goods, furniture, affects or personal property of Tenant upon the Premises; or upon the interest of Tenant in this Lease or in the Premises; or in the event Tenant violates any of the terms, conditions or covenants on the part of Tenant herein contained. In order to further secure the prompt payments of said rents, as and when the same mature, and the faithful performance by Tenant of all and singular terms, conditions and covenants on the part of Tenant herein contained, and all damages and costs that the Landlord may sustain by reason of the violation of said terms, conditions and covenants, or any of them, Tenant hereby expressly waives any and all

rights to claim personal property as exempt from levy and sale, under the laws of the State or of any other state in the United States.

Remedies. Upon the occurrence of an Event of Default, Landlord, without notice to Tenant in any instance (except where expressly provided for below) may do any one or more of the following:

1. With or without judicial process, enter the Premises and take possession of any and all goods, inventory, equipment, fixtures and all other personal property of Tenant situated in the Premises without liability for trespass or conversion, and may sell all or any part thereof at public or private sale. Tenant agrees that five (5) days' prior notice of any public sale and five (5) days' prior notice of the date after which any private sale shall be held shall constitute reasonable notice. The proceeds of any such sale shall be applied, first, to the payment of all costs and expenses of conducting the sale or caring for or storing said property, including all attorney fees; second, toward the payment of any indebtedness, including (without limitation) indebtedness for Rental, which may be or may become due from Tenant to Landlord; and, third, to pay to Tenant, on demand in writing, any surplus remaining after all indebtedness of Tenant to Landlord has been fully paid;

2. Without terminating this Lease, enter upon and take possession of the Premises and expel or remove Tenant and any other person who may be occupying the Premises or any part thereof, make such alterations and repairs as may be necessary in order to re-let the Premises, and re-let the Premises or any part thereof for such term and at such rental and upon such other terms and conditions as Landlord in its sole discretion may deem advisable. Upon each such re-letting, the rentals received by Landlord shall be applied: first, to the payment of any indebtedness other than rent hereunder due from Tenant to Landlord; second, to the payment of any costs and expenses of such re-letting, including brokerage fees and attorney fees and costs of such alterations and repairs; third, to the payment of any rent due and unpaid hereunder, and the residue, if any, shall be held by Landlord and applied in payment of future rent as the same may become due and payable hereunder. If such rentals received from such re-letting during any month shall be less than the rent to be paid during that month by Tenant hereunder, Tenant shall pay any such deficiency to Landlord upon demand. No such re-entry or taking of possession by Landlord shall be construed as an election on its part to terminate this Lease unless a written notice of such intention shall be given to Tenant; and any attempt by Landlord to mitigate its claim for damages against Tenant by re-letting the Premises shall not be construed as a waiver of its right to damages under this section;

The language used by the lease may affect the landlord's ability to recover these fees. Ideally, the lease should provide that the tenant is obligated to pay these fees as they are incurred by the landlord.

3. Perform, on behalf and at the expense of Tenant, any obligation to Landlord under this Lease which Tenant has failed to perform and of which Landlord shall have given Tenant notice, the cost of which performance by Landlord, together with interest thereon at the Default Rate from the date of such expenditure, shall be deemed Additional Rental and shall be payable by Tenant to Landlord upon demand;

4. Elect to terminate this Lease and the tenancy created hereby by giving notice of such election to Tenant, and may re-enter the Premises, without the necessity of legal proceedings or process, and may remove Tenant and all other persons (if Tenant is still in possession) and property from the Premises, and may store such property in a public warehouse or elsewhere at the cost of and for the account of Tenant without resort to legal process and without Landlord being deemed guilty of trespass or becoming liable for any loss or damage occasioned thereby; or

5. Exercise any other legal or equitable right or remedy authorized by applicable law.

Damages. If this Lease is terminated by Landlord pursuant, Tenant shall be liable to Landlord for Termination Damages. "Termination Damages" shall mean the aggregate of (a) an amount or amounts equal to the Rental which, but for termination of this Lease, would have become due during the remainder of the Term, less the amount or amounts of Rental, if any, which Landlord shall receive during the remainder of the Term from others to whom the Premises may be rented (other than any Additional Rental received by Landlord as a result of any failure of such person to perform any of its obligations to Landlord) and (b) any damages which may be suffered by Landlord and all reasonable costs, fees and expense including, but not limited to, attorney fees, costs and expenses, incurred by Landlord in pursuit of its remedies hereunder, or in renting the Premises to others from time to time. Any suit or action brought to collect any such Termination Damages for any month or months shall not in any manner prejudice the right of Landlord to collect any Termination Damages for

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any subsequent month by a similar proceeding.

If such termination shall take place after the expiration of two (2) or more Rental Years, then, for purposes of computing the Termination Damages, the Annual Percentage Rental payable with respect to each Rental Year following termination (including the Rental Year in which such termination shall take place) shall be equal to the average Annual Percentage Rental payable with respect to each complete Rental Year preceding termination. If such termination shall take place before the expiration of two (2) Rental Years, then, for purposes of computing Termination Damages, the Annual Percentage Rental payable with respect to each Rental Year following termination (including the Rental Year in which such termination shall take place) shall be conclusively presumed to be equal to twelve (12) times the average monthly payment of Annual Percentage Rental due prior to such termination or if Tenant has not paid any Percentage Rental during this period, then the Annual Basic Rental for each year of the unexpired term shall be a sum equal to twenty-five percent (25%) of the Annual Basic Rental. Termination Damages shall be due and payable immediately upon demand by Landlord following any termination of this Lease. If this Lease is terminated, Landlord may re-let the Premises or any part thereof, alone or together with other premises, for such term or terms (which may be greater or less than the period that otherwise would have constituted the balance of the Term) and on such terms and conditions (which may include concessions or free rent and alterations of the Premises) as Landlord, in its absolute discretion, may determine, but Landlord shall not be liable for, nor shall Tenant's obligations hereunder be diminished by reason of, any failure by Landlord to re-let the Premises or any failure by Landlord to collect any rent due upon such re-letting.

No reference to any specific right or remedy shall preclude Landlord from exercising any other right or from having any other remedy or from maintaining any action to which it may otherwise be entitled at law or in equity.

Remedies Cumulative. No reference to any specific right or remedy shall preclude Landlord from exercising any other right or from having any other remedy or from maintaining any action to which it may otherwise be entitled at law or in equity. No failure by Landlord to insist upon the strict performance of any agreement, term, covenant or condition hereof, or to exercise any right or remedy consequent upon a breach thereof, and no acceptance of full or partial rent during the continuance of any such breach, shall constitute a waiver of any such breach, agreement, term, covenant or condition. No waiver by Landlord of any breach by Tenant under this Lease or of any breach by any other Tenant under any other Lease of any portion of the Shopping Center shall affect or alter this Lease in any way whatsoever. ■

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Landlord Bankruptcy

the security deposit or letter of credit "always" is returned to the tenant as an asset of the bankruptcy estate.

The *El Toro* case also reasons that because the cap is defined in terms of future rent, Congress intended that the kind of damages that are subject to the cap are those that are in the nature of lost rent. This reasoning appears to open the door for landlords to argue that damages for breach of any lease covenant other than payment of rent are not subject to the cap. For example, consider a covenant by the tenant to restore the premises to the condition they were in at lease commencement. When the tenant takes occupancy, it alters the premises to suit its specific needs (e.g., removes the ceilings and HVAC and installs a switching station). Before the lease expires by its own terms, assume that the tenant files for bankruptcy, rejects the lease and fails to restore the premises—perhaps even abandoning its personal property, creating a high clean-up cost for the landlord. In that case, the tenant arguably committed no tort or nuisance, but merely breached an agreement to restore the premises. Only time and future cases will determine how the extent of the § 502(b)(6) cap is applied in various factual circumstances. ■

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Legislative News

Around the Nation...

Federal

Cap-and-Dividend Plans Offer Retail No Relief

As part of its 2010 budget proposal, the Obama Administration is expected to outline a plan to raise the cost of fossil fuels significantly (coal, oil and natural gas). In an effort to respond to climate change fears, the federal government will have to choose between a straight tax (levied against the carbon content of fossil fuels) or an indirect auction of "allowances" giving the possessor the right to "pollute" the air with carbon dioxide (generated by burning fossil fuels).

Of course, any increase in the cost of fossil fuels will increase the cost of electricity, gasoline and home heating for millions of businesses and individual consumers. Therefore, a debate has arisen over how best to rebate to low-income and middle-income consumers the increase in their cost-of-living attributable to the tax or auction. There are no current plans to create a rebate program for small-to-medium businesses, although some major industries are looking for rebate money.

The carbon auction approach has been called "cap-and-trade" because the government would set a ceiling, or "cap," on the amount of carbon dioxide the nation could produce and then allow a market to develop for exchanging carbon-emitting allowances among firms. The low-income rebate concept is being called "cap-and-dividend" and the idea is to send a portion of the carbon tax (or auction) revenues back to citizens while keeping a significant portion for deficit reduction.

The Congressional Budget Office has estimated that the revenues from a tax or auction could reach as high as $300 billion by the year 2020, under some scenarios.

Obama Budget Includes Details for Cap-and-Trade, Aggressive Emission Targets

At press time, President Barack Obama's 10-year budget includes an assumption of the availability of carbon revenues beginning in 2012, as was widely expected. The budget also includes detailed language for a federal cap-and-trade program, and recommends that greenhouse gas (GHG) emissions be reduced 14 percent below 2005 levels by 2020 and 83 percent below 2005 levels by 2050.

Colorado

Colorado has seen a host of "anti-growth" legislation introduced. However, it appears that the bills are dying quickly. So far, legislation severely restricting urban renewal development, HB 1070, was heard and defeated. ICSC joined with NAIOP (National Association of Industrial and Office Property) and the Colorado Municipal League to defeat this measure, which would have prohibited any land that was classified as vacant or agricultural from being included within an urban renewal district. The bill restricted URAs (urban renewal areas) to metropolitan in-fill developments, thus eliminating the ability of Colorado's suburban counties to take advantage of the economic opportunities that such developments can bring.

Minnesota

Minnesota's economic forecast is predicted to worsen since March. Currently, Minnesota is $5.2 billion in the red, and government officials believe that the debt could rise to $7 billion. An expansion of the state-wide sales tax to include clothing is on the table.

Washington State

HB 1947 is a local option-street-utility tax that allows municipalities to assess properties (shopping centers) based on the traffic they generate.

Puerto Rico

Puerto Rico Senate Bill (SB) 88 proposes amendments to the Closing Law of Dec. 1, 1989. The legislative assembly is evaluating the measure. If approved, SB 88 would allow retailers to open on Sundays, as they would on any other day, between 6 a.m. and midnight (instead of the current 11 a.m. to 5 p.m. Sunday schedule). Furthermore, this measure intends to eliminate double compensation for employees who work in retail stores on Sundays.

Council for Development Finance Agencies (CDFA) Launches Tax-Increment Finance Online Resource Center

Tax-increment financing (TIF), also known by a variety of similar names such as RAD, TAD and TIRZ, is the leading economic development finance tool nationwide. Currently, 49 states and the District of Columbia have tax-increment-type statutes in place with hundreds of projects financed annually. Understanding the various rules, regulations, limitations and relative flexibility of these statutes is a vital part of making sound decisions when using TIF to spur development, redevelopment and new investment in the community.

Visit the CDFA Web site online resource center, which has an interactive, cutting-edge information database (http://www.cdfa.net/cdfa/tifmap.nsf/index.html). The Web site also has a detailed review of the current state statutes and related regulations governing the use of TIF and similar special district financing tools throughout the country.