Subleasing and assignments are essential instruments for tenants to reduce the size of their space and reduce costs for space they no longer need. Landlords often disfavor subleases and assignments because they lose control over who occupies their space. Subleases also raise issues for lenders to landlords who may become nervous about the quality of tenants. Subleases come in a variety of forms, all of which need to exist within the operational parameters and other restrictions imposed by the master lease. If subleases are carefully drafted, they can serve the interests of landlord, tenant, subtenant, and lender. Otherwise, these complex documents give rise to multiple levels of friction and possibly litigation. This program will provide you with a practical guide to the various forms of subleases and assignments, key issues for landlords, tenants, and subtenants, and tips to avoid drafting traps.

Day 1 – June 20, 2017:

- Drafting and negotiating subleases and assignments of leases
- Subleasing v. assignments – when is each used or allowed?
- Types of subleases – leases without reference to master lease v. incorporation by reference to master lease v. custom-made sublease
- Standards of “reasonableness” in obtaining landlord consent to assignment or sublease
- Identifying and mitigating risks to tenants and subtenants in subleasing
- Landlord and lender concerns in subleases

Day 2 – June 21, 2017:

- Drafting the most provisions in subleases and tips to avoid later dispute
- Space recapture, profit sharing, and other landlord remedies
- Restrictions on use in subleases and subtenant risks
- Non-disturbance agreements with landlord and lender
- Remedies of subtenant on tenant to landlord default
- Most important provisions of assignments of leases

Speakers:

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Chapter 13 ASSIGNMENTS AND SUBLEASES

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§13.01 AN APPROACH TO ASSIGNMENTS AND SUBLEASES

The assignment and sublease provisions are among the most important and heavily negotiated parts of any lease. They are a focal point of the unavoidable “zero-sum game” landlord/tenant tension: the control gained by one is the control lost by the other. These provisions are very likely to have significant economic consequences; again, one gains only at the expense of the other. An assignment or sublease may enable a tenant to grow or contract in response to its business needs, and it may facilitate or frustrate an advantageous sale. On the other hand, a landlord that cannot control its space may be unable to enhance the quality and value of its property, or to take care of

1See Stein, Assignment and Subletting Restrictions in Leases and What They Mean in the Real World, Real Prop., Tr. & Est. L.J. at 1 (Spring 2009), is the best place to start; Pinckard & Kiesey, Assignments and Subleases (With Forms and Dialogue) (Part 1), Prac. Real Est. Law. at 47 (May 2009), and (Part 2), at 7 (July 2009); Goodman & Nash, Lease Assignments and Subletting: The Perspective of Landlord and Tenant, Real Est. Fin. J. at 72 (Spring 2001); Fisher, Drafting and Negotiating Commercial Lease Assignments and Subletting Clauses (with Forms), ALI-ABA Course Materials J. at 59 (Oct. 1991), and Flores, Drafting Lease Transfer Provisions That Work,13 Prac. Real Est. Law. at 35 (Mar. 1997).
the needs of its existing tenants.

The landlord and tenant each enunciate general principles expressing legitimate interests. The landlord believes that it has a longer or greater commitment to the project than the tenant. It alone is in the real estate business and it alone should control the premises; for example, without control over assignments and subleases, the shopping center owner cannot assure the tenant mix that contributes to the success of its development, and an office building owner cannot provide for the expansion needs of its other tenants, or even be certain who occupies its building. The tenant believes that it has bought the premises for the term, and that any use or user that complies with the lease should be allowed; without the ability to assign its lease, a tenant may be unable to sell or expand a profitable business, or reduce its losses in an unprofitable business.  

Unfortunately, the clearly divergent legitimate interests often engender arguments as righteous and contentious as they are unnecessary. When the relevant concerns are correctly identified, the assignment and sublease provisions can be designed appropriately and applied. The real concerns in an assignment of a single-tenant lease are much fewer than in an assignment of an office lease, and very much fewer than in an assignment of a retail lease. To complicate matters, assignments of various types of retail leases present different concerns. However, mere repetition of the general principles will never lead to an agreement.

The real estate professional must always ask “does the landlord care who occupies the premises so long as the other provisions of the lease (such as the payment of rent) are observed?” The essential phrase in the question is “so long as the other provisions of the lease are observed.” If one occupant does what is required and refrains from what is prohibited as well as another, they are interchangeable. Put differently, if a tenant defaulted, any replacement that the landlord would accept is presumably an acceptable assignee. Thus, the real estate professional recognizes the close relationship between the use and the assignment and sublease provisions of a lease and, ultimately, the default and mitigation provisions.

In a single-tenant lease, the answer is almost always “no.” If the assignee or subtenant complies with the lease, the landlord should be indifferent to the face in the door. There are no other tenants whose needs for the common areas must be respected, and no synergy among tenants that must be preserved.

In an office lease, the answer is probably “no,” the landlord does not care who occupies the premises so long as the other provisions of the lease are observed; this is, however, not true with regard to first floor retail or financial institution tenants about whose appearance and operations the landlord is certainly concerned. The blas “no” assumes that the office lease prohibits certain undesirable occupants as discussed in §11.03[A]. Generally, however, office tenants' demands on common areas and parking areas are fairly uniform. Of course, the landlord will be concerned about densely populated premises, and may limit the number of occupants based on the area of the premises. Burdensome demands on occupants' services are addressed by charges for overtime and excessive use. Parking demands for both occupants and visitors relate to the number of occupants, and that is controllable. Thus, the office building landlord is more concerned with the uses than the single-tenant building landlord, but less so than the retail landlord.

When asked whether it cares who occupies its premises, the retail landlord is likely to answer emphatically, “absolutely yes.” The assignment of the retail lease implicates several other provisions such as percentage rent, operating covenants, cotenancy, radius restrictions, insurance, use and signage. Among retail tenants and among retail projects, however, there are gradations. On one end is the anchor tenant (a recognized department store, for example) in a regional mall.

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2See Klein, How to Purchase a Leasehold (with Form), 8 Prac. Real Est. Law. at 75 (Mar. 1992), for a discussion and form of purchasing a commercial lease.
and on the other is a nameless support service (shoe repair, for example) in a strip center. The latter is fungible; the other is not, because tenants will not be as strongly attracted to an unanchored mall. Between a mall and a strip center, a community center may have a supermarket as an anchor. Another well operated supermarket could replace it, but three home furnishing stores could not. However, in a theme center featuring home furnishings, a grocery store is useless. Finally, an upscale mall will require a certain quality of tenant that a midrange mall will not, and a factory outlet shopping center will require “name brand” tenants that a neighborhood shopping center will not. The concerns of the retail landlord are matched by those of the retail tenant. Unlike an office or industrial tenant, the retail tenant cannot readily move its business because it loses the value of its location. Unlike those tenants, a retail tenant can reap the value of its business only by selling it and assigning the lease as part of the sale; a sublease of retail space (but not a concession arrangement) is rare because the tenant has no need for the premises, and there is little likelihood of returning to them once it gives up its business.

Lastly, even if the landlord loses control of the premises because of uncontrollable assignment rights, it can indirectly regain some control through other provisions of the lease. More than any other provision, the assignment provision is affected by other parts of the lease. Those provisions include: recapture or profit sharing discussed in §13.10; a reservation of extension or expansion option rights; exclusives only to the original tenant; limitations on signage or alterations that effectively narrow the range of users; use, trade name, and operating covenants; a radius provision; minimum sales requirements; and the percentage rent rate (and its adjustment upon assignment or sublease).

This chapter first defines the relevant terms and then approaches assignments and subleases as processes in which the legal and practical requirements of both landlord and tenant dictate the possible lease provisions. The real estate professional can never forget that the marketplace dictates the lease; a desirable tenant in a coveted location will give up more than it will for a less desirable one, and all tenants are coveted for undesirable premises. In this chapter, for ease of expression, the term “transfer” refers to both an assignment and a sublease.

§13.02 ASSIGNMENT AND SUBLEASE DEFINED

An assignment is a disposition of all the assignor's rights in the lease and its interest in the premises. An assignment may be made of all the rights in all of the premises, or it may be of all the rights in part of the premises; in the latter event, it is called an assignment pro tanto or a partial assignment. Assignments are usually made by tenants. Similar dispositions by landlords occur in connection with sales or encumbrances of the premises. An assignment does not release the tenant, but rather its liability continues; even if it were inclined to do so, a landlord would be ill-advised to release a tenant without its lender's consent. An assignment rids the tenant of the

3Levey, Don't (Sell or) Die Without the Landlord's Permission: Leasing Restrictions Confounding Transfers of Business (with Forms), 15 Prac. Real Est. Law. at 43 (Jan. 1999).

4Technically, one does not assign a lease; rather, one assigns one's interest in a lease. The tenant's interest is possession; the landlord's interests are rent and the reversion. Common parlance uses the expression assignment of lease and this book does also. However, the technical difference is very much alive. Cedar Point Apartments, Ltd. v. Cedar Point Inv. Corp., 693 F.2d 748 (8th Cir. 1982), cert. denied, 461 U.S. 914, 103 S. Ct. 1893, 77 L. Ed. 2d 283 (1983), on remand, 580 F. Supp. 507 (E.D. Mo. 1984), judgment aff'd as modified, 756 F.2d 629 (8th Cir. 1985).

5See Barbuti, Assignments, Pro Tanto and Why to Avoid Them, 22 Prac. Real Est. Law, at 21 (Sept. 2006) which also has a very clear discussion of the distinctions.
lease if the assignee performs, but does not necessarily give the tenant any useful rights if the assignee does not perform.

A sublease is the tenant’s creation of a lease-within-a-lease. The tenant transfers less than all its rights in all of the premises or in the part of the premises. The relationship of the tenant and its subtenant is like the relationship of the landlord and the tenant. The most important analogy between the original landlord and the tenant-sublandlord is that each has a reversion, that is, the right to repossess the leased or subleased premises when the lease or sublease ends.

The safest and most common reversion is effected by a sublease for a term that is one day less than the balance of the tenant-sublandlord's term. Many other attempts to retain a reversion have caused litigation and split the jurisdictions. The tenant's reservation of a right to terminate the sublease on the occurrence of a stated event (usually subrent default); the tenant's reservation of greater rent than the rent prescribed in the master lease; and the tenant's reservation of a right of re-entry on the subtenant's default. Once again, a sublease for at least one day less than the sublandlord's term is the surest way to avoid an inadvertent assignment. Although Arkansas has an unusual rule that determines whether an agreement is a sublease or an assignment based upon the judicial finding of the intention of the assignor/sublandlord or assignee/subtenant, the characterization of the agreement as a sublease by the tenant and subtenant will not change its legal effect in most courts.

The distinction between an assignment and a sublease has been made for centuries:

An assignment is properly a transfer, or making over to another, of the right one has in any estate; but it is usually applied to an estate for life or years. And it differs from a lease only in this: that by a lease one grants an interest less than his own, reserving to himself a reversion; in assignments he parts with the whole property, and the assignee stands to all intents and purposes in the place of the assignor.

Important consequences follow from these definitions. If a tenant is forbidden to assign its
lease but is not prevented from subleasing the premises, the tenant may use a sublease to bring about a result almost identical to an assignment. All the tenant must do is keep a reversion. If the tenant does not keep a reversion, the transaction is an assignment, and the lease is breached.

Unless the landlord agrees to be bound by the sublease, a subtenant has no relationship with the landlord; rather, a subtenant has rights against, and obligations to, the tenant. For example, it pays rent to the tenant, not the landlord. If the tenant forfeits its lease with the landlord, the subtenant cannot avoid the loss of its sublease; on the other hand, an amendment of the lease between the landlord and the tenant does not bind the subtenant unless it agrees to the amendment. If the prime lease is amended after the sublease in such a way as to delay the tenant's possession, the tenant cannot demand that the subtenant accept the delayed possession of the premises, and the subtenant is excused from performance.

The sublease depends on the continued existence of the lease. If a tenant grants its subtenant an option to renew based upon the tenant's option in its lease, the subtenant does not have any ability to renew the lease on behalf of the tenant, but is entirely dependent upon the tenant for extension of the lease. Of course, if the tenant refuses to exercise its renewal option so as to enable the subtenant to take advantage of the rights that were granted to it, the tenant may be liable to the subtenant. The subtenant's lot is a hapless one. For that reason, the subtenant asks for an agreement in the form set forth in §13.14; by this recognition agreement, the subtenant protects its possession by means of an agreement with the landlord.

By the same token, the landlord has no relationship with the subtenant. As a result, except for the possibility of merger discussed in §33.10, the landlord can safely ignore the subtenant. However, the landlord may want the subtenant as its own tenant if the landlord-tenant lease is terminated. To assure itself of a lease with the subtenant, the landlord may ask the subtenant to enter into an attornment agreement such as that in §13.14; by this agreement, the subtenant agrees to treat the landlord as its landlord under the landlord-subtenant lease if the landlord-tenant lease is assumption after an assignment, the tenant changed the transaction to a sublease, and the court allowed the “new” sublease.


19 See Sholtus v. Andrews, 800 P.2d 1044 (Kan. Ct. App. 1990), in which a Kansas court said that a subtenant had no right to demand notice from a landlord of an eviction suit because it has no relationship with the landlord.

20 The protection afforded a landlord by the absence of privity with a subtenant has been overcome when principles of fairness require a subtenant to have remedies against the landlord. Tidewater Investors, Ltd. v. United Dominion Realty Trust, Inc., 804 F.2d 293 (4th Cir. 1986), recharacterized a sublease as an assignment and gave the subtenant privity of contract with the landlord to allow recourse to the landlord.
Because restrictions against assignment and subleases are restraints on alienation, courts construe the restrictions strictly and in favor of free alienability. As a result, a tenant may be able to achieve indirectly what it cannot achieve directly. A covenant not to assign a lease is often not breached by a sublease of the premises, a transfer of a corporate tenant’s stock, a transfer of a partnership interest in a partnership tenant, a mortgage of the lease, bankruptcy of the tenant, execution of judgment on the lease, or death of the tenant. A covenant not to sublease the premises is not breached by an assignment of the lease, or by a variety of arrangements by which the premises are shared; in fact, a covenant not to sublease the premises (as opposed to a covenant not to sublease all or any part of the premises) is not breached by a sublease of part of the premises. Clearly, the wary landlord must protect itself against the wily tenant.

With these thoughts in mind, the real estate professional on behalf of a tenant will consider whether an assignment is more appropriate than a sublease. In either case, the tenant remains liable (although occasionally an assignor will be released if the assignee has very good credit). An assignment will usually not work if the market rents are below the lease rent or if the base year is before the year of the assignment because the assignee would be paying more than it needs to pay. Of course, the tenant could offer a subsidy to effect an assignment. If the subsidy is paid when the assignment is done, the tenant-assignor is at risk of the assignee's default, and if the subsidy is paid over time, the assignee is at risk of the assignor's non-payment. These risks can be avoided with some collateral or other assurance of payment. When the assigned lease is below market, the assignee may pay “key-money” for it. With either structure, the imposition of transfer taxes should be checked and, if applicable, allocated.

To a tenant, the sublease is usually preferable because it keeps control of the lease and has ready remedies if the subtenant defaults. An assignment with a leasehold mortgage or collateral assignment to assure the assignee's performance can be used, but it is cumbersome and probably also requires the landlord's consent.

The proposed transferee, on the other hand, will prefer an assignment and the resultant direct relationship with the landlord, without dealing with the tenant. In the direct relationship, the assignee will control the lease (and amendments or renewals of it), and will have rights to services directly from the landlord and not indirectly via the tenant. Finally, the risk of the tenant's bankruptcy and rejection of the lease is avoided with an assignment. The subtenant's risks can be mitigated to a degree with a recognition agreement as discussed in §13.14, but it will usually require the subtenant to pay market rates on the lease as a condition of recognition, and the rate is likely to be greater than the sublease rate.

Once the transaction is decided, the tenant and transferee (whether assignee or subtenant) still have homework. The lease must be reviewed for any recapture or profit sharing rights (see §13.10), and then for the proper means of getting the landlord's consent, the required information regarding the transferee, the form of the transfer documents, and the time frames for submissions and responses.

The tenant's due diligence includes consideration of its risks of an assignee's extension of the term or expansion of the premises (if those rights are provided), and may necessitate an amendment of the lease to delete those rights, a covenant by the assignee not to exercise them, or an agreement from the landlord that it is not bound by an extension or expansion. The tenant must also decide whether it wants to remove any leasehold improvements it has made, or to remove or leave personal property. If the tenant has financed its leasehold improvements or inventory, it will

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have to deal with those lenders. 22

The most important—and least understood—aspect of assignments and subleases is that neither of them releases the original tenant's liability under the lease. Unless the original tenant wins the landlord's agreement to release it, the original tenant remains obligated under the lease. 23 However, a landlord that amends the lease with the assignee with respect to essential elements such as rent and term may effect a novation—i.e., a new lease—and release the assignor's liability. 24 These results are the unavoidable conclusions from the concepts of privity of estate and privity of contract, which are discussed in §§13.03[A] and [B]. The next two sections are helpful but not essential for the discussion that follows. Although they deal with important legal technicalities, some real estate professionals may not find these technicalities interesting.

§13.03 PRIVITY

To understand fully the legal significance of assignments and subleases, one must first understand the ancient legal concept of privity. When applied to leases, privity means a mutual interest in the promises of a lease. A person that is in privity with another is entitled to enforce the other's promises. Privity arises in one of two ways or in both ways: privity of contract (which is a relationship derived from contract law) and privity of estate (which is a relationship derived from real property law). The promises that may be enforced by one with privity of contract may be different from those that may be enforced by one with privity of estate. Therefore, the nature of the privity is very important.

[A] Privity of Contract

When a landlord and tenant enter into a lease, they are bound to one another both by privity of contract and by privity of estate. They are mutually interested in the same lease, and they are mutually interested in the same premises. They may each enforce the express provisions of the lease by virtue of privity of contract, just as they may each enforce the promises that arise from privity of estate.

When a tenant assigns its interest in a lease 25 its assignee has privity of estate with the landlord; 26 they have a mutual interest in the premises. They are not in privity of contract unless the assignee assumes the tenant's obligations in the lease, and the landlord agrees to be bound to the assignee. Thus, the landlord and assignee can enforce only those promises that exist by virtue of privity of estate, as discussed in §13.03[B]. However, an implied assumption may be found when a successor by purchase of the tenant's assets occupies the premises, pays rent to the landlord, and obtains utilities in its name, even though the landlord has not given its required

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22This discussion has benefited from materials prepared by Nancy A. Connery, Esq., of New York City.

23Siragusa v. Park, 913 S.W.2d 915 (Mo. Ct. App. 1996). Of course, the assigning tenant may have defenses against a later claim by its former landlord, such as that the landlord’s settlement with the assignee terminated the assignor-tenant's liability. Co Le'Mon, L.L.C. v. Host Marriott Corp., 2006 WL 1485235 (Ohio Ct. App. May 31, 2006).


25In this section, the assignment is presumed to be one of the entire leasehold interest.

26The rules are conceptually the same for an assignment (or more commonly a sale) by the landlord.
27 A tenant that assigns its lease has no right to re-enter the premises if its assignee defaults; that is solely the landlord's prerogative. However, the original tenant is still liable for the rent.

Collateral assignments, as opposed to absolute assignments, are intended to give a lender a security interest in a borrower's lease, and not to create privity of contract. However, a Missouri lender that took an assignment of a tenant's lease as collateral for the tenant's loan and that (presumably inadvertently) assumed the tenant's obligations under the lease was liable to the landlord by privity of contract. 29 A California lender came to the same end when its subsidiary assumed a ground lease pending the lender's foreclosure after the tenant-borrower was in default. The assuming subsidiary remained liable after the foreclosure. 30 On the other hand, a Mississippi bank avoided liability for cleanup costs after an environmental incident because it had a “true” collateral assignment. 31 If the lender “forecloses” the assignment and becomes the landlord's tenant, the lender will be bound to those covenants that arise from privity of estate discussed in §13.13, of which the foremost is the obligation to pay rent.

In a California case, a nonassuming assignee was held not to be liable for rents after its possession ended, even though it was held to be liable to arbitrate the issue. 32 This recognizes the general rule regarding rent obligations, but holds, in effect, that a covenant to arbitrate binds nonassuming assignees. However, there seems to be an inconsistency in this case insofar as it requires arbitration of a liability that cannot be imposed upon the nonassuming assignee. Another California court concluded, however, that a landlord and subtenant are bound by privity of estate to an arbitration provision in the prime lease because it is a “real covenant.” 33

When a tenant subleases the premises, it has privity of contract and privity of estate with its subtenant. Their positions are analogous to the positions of the original landlord and tenant. The original landlord and the subtenant have no privity of estate or privity of contract with one another. Each of them has rights only against the tenant. For example, a landlord's acceptance of rent from a subtenant does not convert a sublease into an assignment. 34 The better practice, of course, is to provide specifically in the lease that the landlord's acceptance of rent from a subtenant is not acceptance of the sublease.

[B] Privity of Estate

To recapitulate, privity of contract allows enforcement of the contract or lease provisions.

28 Italian Fisherman, Inc. v. Middlemas, 313 Md. 156, 545 A.2d 1 (1988). An assignee has no right by virtue of the lease to recover its attorneys' fees in a dispute with the tenant/assignor merely because the lease enables the landlord to do so. Satellite Gateway Commc'n's, Inc. v. Musi Dining Car Co., 110 N.J. 280, 540 A.2d 1267 (1988).
29 South Lakeview Plaza v. Citizens Nat'l Bank, 703 S.W.2d 84 (Mo. Ct. App. 1985).
31 MidSouth Rail Corp. v. Citizens Bank & Trust Co., 697 So.2d 451 (Miss. 1997).
33 Melchor Inv. Co. v. Rolm Sys., 3 Cal. App. 4th 587, 4 Cal. Rptr. 2d 343 (Cal. App. 6th Dist. 1992); this is questionable law.
Privity of contract arises by being either the landlord or tenant, or one that succeeds either of them and assumes its predecessor's obligations.

Privity of estate allows enforcement of only those promises that “run with the land,” that is, promises that touch and concern the land. These technical expressions are as amorphous today as they were when they arose several centuries ago. Briefly, a promise may be said to touch and concern the land if it relates directly to the nature, quality, value, use, enjoyment, and operation of the premises.

These promises have been found to run with the land for the benefit of the landlord's successors (by whom the promises may be enforced): promises as to rent; restrictions on the tenant's right to transfer its interest; rights to terminate the lease by notice or cancel the lease in the event of sale; agreements to pay taxes, make repairs, or pay insurance; exculpations of the landlord from damages arising from the condition of the premises, and rights to confess a judgment against the tenant. These promises have been found to run with the land as burdens upon the landlord's successors (against whom the promises may be enforced): covenants of quiet enjoyment; promises to return a deposit; payments owed to the tenant upon termination of the lease, and the tenant's options to extend the lease or purchase the premises.

The successors of the tenant have had the benefit of these promises (and may enforce them

The “land” in these expressions is best understood as the interest that the landlord, tenant, and their successors have in the premises.

The Restatement §16.1 states the rule of the burden of performance after transfer: (1) A transferor of an interest in leased property, who immediately before the transfer is obligated to perform an express promise contained in the lease that touches and concerns the transferred interest, continues to be obligated after the transfer if: (a) the obligation rests on privity of contract, and he is not relieved of the obligation by the person entitled to enforce it; or (b) the obligation rests solely on privity of estate and the transfer does not terminate his privity of estate with the person entitled to enforce the obligation, and that person does not relieve him of the obligation; (2) a transferee of an interest in leased property is obligated to perform an express promise contained in the lease if: (a) the promise creates a burden that touches and concerns the transferred interest; (b) the promisor and promisee intend that the burden is to run with the transferred interest; (c) the transferee is not relieved of the obligation by the person entitled to enforce it; and (d) the transfer brings the transferee into privity of estate with the person entitled to enforce the promise; (3) the transferee will not be liable for any breach of the promise which occurred before the transfer to him; (4) if the transferee promises to perform an express promise contained in the lease, the transferee's liability rests on privity of contract and his liability after a subsequent transfer is governed by subsection (1) (a). It also states the rule of the benefit of promises: (1) a transferor of an interest in the leased property retains the benefit of an express promissory obligation under the lease, which benefit he held before the transfer, to the extent the benefit is not assigned by the transferor and does not run with the transferred interest; (2) a transferee of an interest in the leased property is entitled to the benefit of an express promissory obligation under the lease to the extent the benefit is assigned to him by the transferor or it runs with the transferred interest; (3) the benefit of an express promissory obligation under the lease runs with the transfer of an interest in the leased property if: (a) the promise touches and concerns the transferred interest; (b) the promisor and promisee intend that the benefit is to run with the transferred interest; (c) the transferor does not withhold the benefit of the promise from the transferee; and (d) the transfer brings the transferee into privity of estate with the person obligated to perform the promise.

Thus, the grantee by deed can enforce a lease made by its grantor as a result of privity of estate, MHW Ltd. Family P'ship, Farrokh, 693 N.W.2d 66 (S.D. 2005).
against the landlord): the return of a security deposit; the purchase of improvements added by the tenant; the right to extend the term; the right to purchase the premises; the right to remove improvements to the premises, and the right to prohibit the landlord from competing with the tenant's business, although there are contrary decisions. These promises burden the successors of the tenant and are enforceable against them: payment of rent; payment of assessments or taxes; restrictions on transfers or use; the liability of the tenant to renewal of the lease; the liability of a tenant for the loss of improvements made by it; and the landlord's right to cancel the lease.

The general rule that the promise to pay rent runs with the land will illustrate two more consequences of privity of estate. If a landlord and tenant enter into a lease, they have privity of contract and privity of estate. If the tenant assigns its interest to an assignee that does not assume the lease, the landlord and assignee have only privity of estate. Since the promise to pay rent runs with the land, the assignee must pay rent under the lease or lose the land. The promise is said to run with the land as a burden. On the other hand, in this example, if the landlord sells the land to a buyer that does not assume the lease, the buyer—that has only privity of estate with the assignee—may enforce the promise to pay rent. The promise to pay rent is said to run as a benefit to the land.

Thus, one that has only privity of contract can determine its rights by reference to the lease. One that has only privity of estate has the benefits and burdens that run with the land. One that has neither privity of contract nor privity of estate is without rights. These distinctions explain several lease provisions in the context of assignments and subleases; they explain why landlords, tenants, and subtenants scramble for privity of contract and the substantial benefits that arise from express contractual arrangements.

§13.04 AN ABSOLUTE PROHIBITION

With some exceptions, the general rule of transfer (used in this chapter to mean collectively assignments and subleases) is that they are permitted unless they are expressly prohibited; therefore, if the lease is silent, the tenant may assign its lease or sublease its premises. The real estate professional must know that, aside from restrictions in the lease, there are common law exceptions to this general rule, and there may be statutory restrictions on assignments or subleases.

Statutory prohibitions affecting assignment are usually related to short-term leases, although the relevant Texas statute affects all leases, but may be modified by agreement. Some statutes prescribe free alienability in the absence of a contrary agreement. A prohibition of assignment is often implied when the basis for the lease is a special personal service or skill. Sharecropping is a common example because the landlord's share is related to its tenant's skill. However, percentage leases (which some retail tenants consider to be modern sharecropping) do not imply a restriction on assignments. The notion that the nature of the tenant has a bearing on the strictures surrounding assignment finds its way into shopping center leases, in which the

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38But see Annot., 25 A.L.R.3d 897, Covenant restricting use of land, made for purpose of guarding against competition, as running with land (1969) for contrary authority.
40Restatement §15.1.
43See Restatement §15.1, n. 2.
44The Restatement §15.1(2) recognizes this exception.
tenant mix is important to the shopping center's success.  

The Restatement §15.1 takes this view:

The interests of the landlord and of the tenant in the leased property are freely transferable, unless:

1. a tenancy at will is involved;
2. the lease requires significant personal services from either party and a transfer of the party's interest would substantially impair the other party's chances of obtaining those services; or
3. the parties to the lease validly agree otherwise.

If the landlord is not satisfied that there is a legal restriction against assignment and subletting, and perhaps even if it is, the landlord will first suggest a provision that maintains its complete control of the premises:

FORM 13-1

ASSIGNMENT—AN ABSOLUTE PROHIBITION

Tenant will not assign this Lease in part or in full and Tenant will not sublease all or part of the Premises.  

Although this provision is condoned by Restatement §15.1(3) and a California statute, judicial constructions of this prohibition are so restrictive that this form does not prevent assignments by operation of law and management arrangements. Even this form needs to be enhanced in the ways described in §13.08.

This absolute prohibition usually evokes a prompt response from the tenant, because it needs rights to transfer for flexibility in business planning. For a small tenant, these rights give the operators an opportunity to retire from business without working to the end of their lease; since death does not release a sole proprietor, an assignment right may avoid a crushing estate liability. To a chain store tenant, these rights are important if it merges with another chain store whose existing locations overlap the tenant's locations; assignments and subleases may be used to dispose of unneeded stores. For any enterprise, the extent of these rights may determine the ability to incorporate, take in partners, sell corporate stock, and sell the lease as part of a sale of all its assets. Thus the tenant usually objects to such a provision.

Someone else objects to this absolute prohibition: the tenant's guarantor. Taking over a failing tenant's business may be the only way for a guarantor to limit or avoid its losses. For the same reason, a guarantor insists on notice of the tenant's default and an opportunity to cure it.

Some real estate professionals argue that a strict prohibition may intimidate an unsuccessful retail tenant, and ultimately hurt the landlord. Such a tenant will lose interest in its operations and the shopping center, will not bring an attractive prospective assignee to the landlord's attention, and may simply move out, leaving unpaid rent and a vacancy.

The landlord will typically respond to these objections with a sincere expression of the importance of its control over the premises for some of the reasons mentioned in §13.01. In a shopping center, the landlord will have chosen its tenants with a careful view toward a good

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45 Resolving Disputes Under Percentage Leases, 51 Minn. L. Rev. at 1139 (1967).
46 Stern v. Thayer, 56 Minn. 93, 57 N.W. 329 (1894), appears to support a provision such as Form 13-1. However, since courts often paraphrase or characterize provisions instead of stating them verbatim, one can never be sure what the leases actually said.
tenant mix; it may even have granted some tenants the exclusive right to conduct a certain business. Uncontrolled transfers threaten these plans. Moreover, since different businesses pay percentage rent at different rates, the landlord may lose money if a tenant paying at a low rate with high volume (for example, a supermarket) assigns its lease to a business with a low volume (for example, a gourmet food shop) that pays at the same low percentage rent rate. Lastly, the landlord will say that some tenants draw customers to the shopping center and thus increase the sales of all tenants, while some tenants attract customers only to their own businesses and do not enhance the business of other tenants.

In an office building, the landlord will not want a transfer to another of its existing tenants in the office building if that tenant's lease is about to expire, because the landlord would prefer to re-lease its own space to its own tenant.

In a single-tenant lease, the landlord has less concern, but still wants to be certain that a responsible entity occupies its building.

Finally, there are economic realities of which both landlord and tenant should be aware. Despite the current trend toward shorter terms, adjustments of rent, and recapture or profit-sharing provisions, a lease may have such a low rent or other favorable terms that the lease is itself an asset. Landlords and tenants differ on the ownership of that asset. Landlords point out that tenants are not in business to make money on their leaseholds; tenants respond that they are no more particular than landlords about their sources of revenue, and that the landlord did not offer to take back the lease if it turned out to be a liability.

In the improbable situation that an absolute prohibition is desired and no standard of reasonableness is to be imposed on the landlord, the provision should emphasize its intention, saying, perhaps:

**FORM 13-2**

**ASSIGNMENT—LANDLORD'S RIGHT TO BE ARBITRARY AND CAPRICIOUS**

Tenant will not assign this Lease in whole or in part and will not sublease the Premises in whole or in part without Landlord's prior written consent. Landlord may withhold its consent arbitrarily and capriciously. Landlord and Tenant have fully bargained for this provision with the intention that Landlord has absolutely no obligation to consider a proposed assignment or sublease.

In an effort to keep its options open, a landlord may provide that it may withhold or grant its consent “in its sole and absolute discretion.” A Tennessee court considered a lease that had two standards, one that its consent “shall not be unreasonably withheld,” and another that its consent could be withheld “in its sole and absolute discretion.” The court reconciled these to mean “the landlord may withhold consent in his sole discretion provided that such discretion is not unreasonably exercised.” Similarly, a federal court applying Alabama law held that a “sole discretion” standard did not mean “arbitrarily or unreasonably” when the landlord demanded additional payments for its consent to a proposed sublease. These decisions cast doubt on “sole discretion” provisions.

After their discussion, which may be quite animated, the following compromise may be

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48 See §13.11.
§13.05 REQUIREMENT OF LANDLORD’S CONSENT

The compromise is:

**FORM 13-3**

**ASSIGNMENT—REQUIRING LANDLORD’S CONSENT**

Without Landlord’s prior written consent, Tenant will neither assign this Lease in part or in full, nor sublease all or part of the Premises.

The landlord does not believe it has made a great concession; it has gone no further than to state the obvious proposition that the landlord and tenant may modify their agreement by the tenant’s offer, and the landlord’s acceptance, of a new tenant or a subtenant. The tenant is encouraged because its real estate professional recalls a principle from a business law class to the effect that parties to a contract cannot act unreasonably. The tenant concludes that the mere requirement of the landlord’s consent implies that the landlord cannot unreasonably withhold its consent.

Although the ground is constantly shifting, most states seem to allow a landlord to withhold its consent arbitrarily if no standard is stated and freely negotiated. 52 A clear emerging trend

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51 See Sobel, *Negotiating a Sublease or Assignment Clause*, Prob. & Prop. at 44 (Mar./Apr. 1990), for a discussion of the landlords’ and tenants’ interests in the standards for consent, and recapture and profit-sharing provisions.

52 A 1984 study found 12 states that allowed arbitrary withholding of consent: Alabama, Alaska, Arkansas, California, Colorado, Florida, Idaho, Illinois, Kansas, Louisiana, Massachusetts, and Ohio. The survey also found 12 states that did not. *Reasonable Consent Forced on Owner*, Com. Lease L. Insider at 3 (Feb. 1984). *Colorado in Cafeteria Operators L.P. v. AmCap/Denver Ltd. P’ship*, 972 P.2d 276 (Colo. Ct. App. 1998) (but noting that a freely negotiated right to be arbitrary would be sustained according to the Restatement §15.2(2)), and California have since changed their positions. The California experience is discussed in this section. Georgia and Indiana also allow landlords to be arbitrary in considering a proposed assignment or sublease, *First Fed. Sav. Bank v. Key Mktgs., Inc.*, 559 N.E.2d 600 (Ind. 1990) (the Indiana Supreme Court refused to imply a standard of reasonableness in construing a provision that was clear and unambiguous, stating that it could not “place the court at the negotiating table with the parties”); *Vaswani v. Wohletz*, 196 Ga. App. 676, 396 S.E.2d 593 (1990). Texas does not require a landlord to be reasonable unless it has agreed to do so. *Reynolds v. McCullough*, 739 S.W.2d 424 (Tex. App. San Antonio 1987), *writ denied* (Tex. 1988), and *reh’g of writ of error overruled* (1988); the decision was based upon the fact that Texas has a statute regarding assignments and the landlord’s consent. If a landlord in Hawaii has reserved the right to give its approval “at its discretion,” it is not required to be reasonable in doing so. *Kapiolani Commercial Ctr. v. A&S P’ship*, 68 Haw. 580, 723 P.2d 181 (Haw. 1986). The highest court of Massachusetts has affirmed its position allowing arbitrary withholding of consent in *21 Merchants Row Corp. v. Merchants Row, Inc.*, 412 Mass. 204, 587 N.E.2d 788 (1992). The tenant asked for consent to an assignment of its lease as part of loan collateral; the assignment would have allowed the lender to assign further without restriction. Despite the obvious disadvantage to the landlord of such an assignment, the court affirmed its general principle. Arizona seems to have joined the growing minority. *Tucson Med. Ctr. v. Zoslow*, 147 Ariz. 612, 712 P.2d 459 (Ariz. Ct. App. 1985) (adopting Restatement §15.2(2)). Ohio has also changed its position. *F&L Ctr. Co. v. Cunningham Drug Stores, Inc.*, 19 Ohio App. 3d 72, 19 Ohio B. 156, 482 N.E.2d 1296 (Ohio Ct.
requires the landlord to be reasonable if no standard is stated. 53 These states 54 express as the

Appl., Cuyahoga County 1984). The Florida case law seems to sidestep the issue of “reasonableness” and to use the implied covenant of good faith and fair dealing to consider the landlord's conduct, because when “one party has the power to make a discretionary decision without defined standards...a ‘covenant of good faith’ will be ‘implied’ to protect the contracting parties' reasonable commercial expectations.” Speedway Super America, LLC v. Tropic Enters., Inc., Sunoco, Inc. (R&M) & Mascot Petroleum Co., Inc., 966 So.2d 1, 2007 Fla. App. LEXIS5799, 32 Fla. L. Weekly D 1032. Furthermore, Maryland has changed its position, last enunciated in 1961, on the basis of its disfavor for restraints on alienation and a covenant of good faith and fair dealing in contracts. Based upon an implied covenant of good faith and fair dealing, a Maryland appellate court held that a “silent consent” clause implies a standard of reasonableness. The decision was given effect as to the litigants before the court and prospectively; leases entered into before the court's decision were subject to the old rule. Julian v. Christopher, 320 Md. 1, 575 A.2d 735 (1990). Although the subject of the dispute was a residential apartment upstairs from tavern premises under the same lease, the court did not limit itself to residential cases. See generally Kehr, The Changing Law of Lease Assignments, 11 Real Est. Rev. at 54 (1981); Guerra, The Approval Clause in a Lease: Toward a Standard of Reasonableness, 17 U.S.F.L. Rev. at 681 (1983).

53 Annot., 21 A.L.R.4th 188, When lessor may withhold consent under unqualified provision in lease prohibiting assignment or subletting of leased premises without lessor's consent (1983).

rationale of this newer rule that a lease is a contract, not a conveyance, and that it is governed by
the contract principles of good faith and commercial reasonableness. The reasoning in some of
these cases has been criticized. In several, the courts need not have gone into the issue of
reasonableness, because the cases could have been decided simply on the basis of the landlord's
bad faith.\textsuperscript{55}

The real estate professional should be aware of the application of the covenant or duty of
good faith and fair dealing (as described in §11.08) to a proposed assignment or sublease. This
duty has precluded a landlord's arbitrariness when no standard is prescribed in an Oregon case,\textsuperscript{56}
but not in a Washington case.\textsuperscript{57} Since the boundaries of this duty are unclear, breach of it is best
avoided by a clear statement of what “reasonable” means.

The anfractuous California experience with this issue is instructive. In late 1983, a California
appeal court abandoned hundreds of years of common law precedents—and the decisions of
the California Supreme Court—to rule that landlords have an obligation to be reasonable when
considering assignments proposed by their tenants.\textsuperscript{58} In January 1984, another California
appeal court followed with a similar decision.\textsuperscript{59}

Less than a year later, the second court declined to follow its earlier decision, and returned to
the traditional rule.\textsuperscript{60} In refusing to impose a reasonableness standard, the court said that “to hold
that there is a triable issue of fact concerning whether the[landlords] unreasonably withheld their
consent when they had already contracted for that right, creates only mischief by building further
uncertainty in the interpretation of an otherwise unambiguously written contract.” The court
suggested that the legislature was the only proper forum in which the unbroken line of judicial
precedent should be broken.

One critic considered these cases and suggested that the judicial failure to distinguish good
faith (which is a subjective standard requiring only a sincerely believed basis for objection) from
reasonableness (which is an objective standard shown by reference to the shared experiences of
all people) shows a lack of reasoning.\textsuperscript{61}

The California Supreme Court agreed to hear the matter. When it spoke, its voices were
neither clear nor harmonious.\textsuperscript{62} The majority concluded that in a commercial lease permitting
assignments only with the landlord's prior consent, a landlord may withhold its consent only if it
has a commercially reasonable objection to the assignee or the proposed use. Two justices

\begin{itemize}
  \item The Connecticut Supreme Court has changed its law to impose upon a landlord a duty of good
        faith and fair dealing when considering an assignment. \textit{Warner v. Konover}, 210 Conn. 150, 553
  \item The Alabama and Florida cases involved the landlords' demands for additional money; in
        the California case, the landlord refused to consider the proposal at all.
  \item Pacific First Bank by Wash. Mut. v. New Morgan Park Corp., 319 Ore. 342, 876 P.2d 761
        (Ore. 1994).
  \item Johnson v. Youssofian, 84 Wn. App. 755, 930 P.2d 921 (1996), review denied, 132 Wn. 2d
  \item Zankel, \textit{Commercial Lease Assignments and the Age of Reason: Cohen v. Ratinoff}, 7 Real
\end{itemize}

The Ninth Circuit had foreseen the California Supreme Court's decision. \textit{Prestin v. Mobil Oil
Corp.}, 741 F.2d 268 (9th Cir. 1984).
dissented, adopting for their opinion a part of the appellate court decision that the majority had reversed.

For the real estate professional, the decision made its most important observations in two footnotes. In footnote 14, the majority opinion noted that the question of an absolute restriction was not presented, but that the *Restatement* §15.2(2) would validate such a prohibition “if freely negotiated.” The *Restatement* does not give an example of a freely negotiated provision. If a prohibition is agreeable, it would seem that the lease at minimum should explain the circumstances that gave rise to the agreement for that provision, and should state any consideration or “trade-off” that induced the tenant to accept it. Because most real estate professionals agree that tenants will rarely, if ever, agree to an absolute provision, another approach is needed.

An alternative is presented in footnote 17 of the opinion. There, the California Supreme Court said “nothing bars the parties to commercial lease transactions from making their own arrangements respecting the allocation of appreciated rentals if there is a transfer of the leasehold.” 63 The California Supreme Court gave its imprimatur to these provisions. Most real estate professionals will be wary of reserving all of the appreciated rentals for the landlord unless the provision is “fully negotiated,” as discussed in the preceding paragraph. In practice, a tenant with no benefit from the highest appreciated rentals will not be motivated to get the best terms in its assignment. **Section 13.10** discusses recapture and profit-sharing provisions. 64

At about the same time as this case was decided by the California Supreme Court, an intermediate appellate court in California upheld the landlord's right to be arbitrary when its only motivation was to improve its financial position; 65 the viability of that decision seemed doubtful.

A California intermediate appellate court held in 1989 that a recapture provision (similar to that in §13.10) allowing a landlord to terminate a lease of premises when its tenant requests consent to sublease is an unreasonable restraint on alienation and void as a matter of public policy, and that the landlord breaches its duty of good faith and fair dealing when it recaptures the premises. The provision in question allowed termination if permission was requested, and thus gave the landlord complete control over subleases (and presumably all dispositions of the leasehold). However, illustrating the vagaries of the judicial reasoning in this area, in a long and

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63 In *Carma Developers (Cal.), Inc. v. Marathon Dev. California, Inc.*, 2 Cal. 4th 342, 6 Cal. Rptr. 2d 467, 826 P.2d 710 (1992), the California Supreme Court upheld recapture clauses. See §13.10.


interesting opinion, the Third Appellate Department sitting as the California Supreme Court reversed, and held that a recapture provision is not an unreasonable restraint or alienation, and that the landlord's exercise of its recapture rights is not a breach of the covenant of good faith and fair dealing.

All of the decisions and much of the voluminous literature written about them were silenced in 1989 when the California legislature took up the gauntlet dropped in 1984.

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1995.210(a) Subject to the limitations in this chapter, a lease may include a restriction on transfer of the tenant's interest in the lease.

(b) Unless a lease includes a restriction on transfer, a tenant's rights under the lease include unrestricted transfer of the tenant's interest in the lease.

1995.220. An ambiguity in a restriction on transfer of a tenant's interest in a lease shall be construed in favor of transferability.

1995.230. A restriction on transfer of a tenant's interest in a lease may provide that the transfer is subject to any express standard or condition, including, but not limited to, a provision that the landlord is entitled to some or all of any consideration the tenant receives from a transferee in excess of the rent under the lease.

1995.250. A restriction on transfer of a tenant's interest in a lease may require the landlord's consent for transfer subject to any express standard or condition for giving or withholding consent, including, but not limited to, either of the following:

(a) The landlord's consent may not be unreasonably withheld.

(b) The landlord's consent may be withheld subject to express standards or conditions.

1995.260. If a restriction on transfer of the tenant's interest in a lease requires the landlord's consent for transfer but provides no standard for giving or withholding consent, the restriction on transfer shall be construed to include an implied standard that the landlord's consent may not be unreasonably withheld. Whether the landlord's consent has been unreasonably withheld in a particular case is a question of fact on which the tenant has the burden of proof. The tenant may satisfy the burden of proof by showing that, in response to the tenant's written request for a statement of reasons for withholding consent, the landlord has failed, within a reasonable time, to state in writing a reasonable objection to the transfer.

The legislature enunciated the public policy “to enable and facilitate freedom of contract by parties to commercial real estate leases,” and expressly disapproved contrary judicial

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The California statute created different rules to recognize the various judicial decisions that have recently held sway with regard to the landlord's duties when a lease is silent about its standards for consent. As a result, landlords and tenants are in theory bound by the legal principles that were in effect at the time their leases were made, presumably the principles they assumed would apply in the absence of their contrary agreement. For leases executed before September 23, 1983, the landlord may unreasonably withhold its consent. For leases executed between September 23, 1983, and December 31, 1989, the landlord may not unreasonably withhold its consent. For leases executed after December 31, 1989, the landlord may not unreasonably withhold its consent unless a contrary agreement is made. Of course, the statute condones contrary agreements.

Many of the reported cases have involved situations in which the tenant did not seek its landlord's consent before making the assignment or sublease. In the landlord's suit for breach of the lease, the tenant asked the court to determine the suitability of the transferee and to find that no breach had occurred because the landlord could not have reasonably refused if the tenant had asked. The courts rule—and tenants should learn—that it is imperative for a tenant to present a transferee and give the landlord an opportunity to refuse the proposal. A landlord need not consider a transferee that occupies the premises before the matter is presented to it. An assignment without required consent, even though an apparent formality because the landlord had no reasonable basis to object, is a default permitting termination.

§13.06 REQUIREMENT OF CONSENT NOT TO BE UNREASONABLY WITHHELD

As §13.05 suggested, a standard of reasonableness may be inferred even if it is not expressed. In those states that do not make that inference, and in most negotiations, when pressed by the tenant for some compromise on the issue of consent, the landlord yields and proposes:

FORM 13-4

ASSIGNMENT REQUIRING LANDLORD'S CONSENT WHICH WILL NOT BE UNREASONABLY WITHHELD OR DELAYED

Without Landlord's prior written consent, which Landlord agrees will not be unreasonably conditioned, withheld or delayed, Tenant will neither assign this Lease in whole or in part nor sublease all or part of the Premises.

This provision equates delayed and withheld consent. As a practical matter, a prospective assignee or subtenant will be lost if a response is not prompt. By including delay in this provision, the tenant assures itself that the landlord will make a decision, and that it will not wait until the

68 For discussions of the California legislation, see Murray & Hamrick, Assignment and Subletting in Commercial Leases: The Impact of the New Civil Code Sections, 13 Real Prop. L. Rep. at 65 (Cal. CEB Apr. 1990); Westreich, New Legislation Permits Commercial and Other Nonresidential Landlords to Prohibit and Place Standards on Lease Assignments and Sublettings, 5 Cal. Real Est. Rep. at 83 (Apr. 1990); Stipanov, Assignment and Subletting of Commercial Leases under the New Statutory Scheme, 8 Cal. Real Prop. J. at 18 (Fall 1990).


70 See Frome, Drafting Landlord Consent to Assignment and Subletting Clauses (with Sample Clauses), Prac. Real Est. Law. at 7 (May 2002), for a thorough discussion of the landlord's and tenant's positions on the issues.
opportunity has passed only to grant its consent. In a Colorado case, the lease provided that the landlord would not unreasonably withhold its consent. Nevertheless, the landlord delayed for so long that the tenant lost the deal. The court held for the tenant, ruling that the landlord could not let an unreasonable amount of time pass without a response. When this provision is included, the tenant finally has meaningful rights. The landlord no longer has its (rapidly vanishing) common law right to withhold its consent arbitrarily and capriciously.

This means that the landlord may not withhold its consent for reasons of “personal taste, sensibility, or convenience.” In a leading case, the philosophical principles of an orthodox Jewish institution compelled it to refuse to consent to a subleasing to Planned Parenthood Foundation of America; the court said that subjective criteria are not sufficient, and that “[t]o the extent that rejection of a proposed subtenancy is based upon the supposed need or dislikes of the landlord, a policy of judicial disapproval of such subjective criteria is discernible.”

The landlord’s personal taste is not the only irrelevancy when reasonableness is the standard. The landlord cannot condition approval on receipt of additional rent. The landlord cannot refuse to consent because: it may lose one of its tenants in another building by consenting to that same tenant as a subtenant; the proposed subtenant would compete with it; of the assignee’s race; it wishes to prevent the assignee’s competition with the landlord’s store; or the landlord’s president “didn’t like [the proposed assignee].” Generally speaking, the landlord cannot reasonably go beyond the terms of the lease in determining whether to give its approval; by the same token, the tenant’s request for concessions beyond the scope of the lease enables the landlord to refuse its consent. A helpful commentary on the meaning of “reasonableness” concludes that the landlord is unreasonable if it is “trying to get a better deal than the landlord

76 Krieger v. Helmsley-Spear, Inc., 62 N.J. 423, 302 A.2d 129 (1973) holding that the reasonable consent clause “is for the protection of the landlord in its ownership and operation of the particular property—not for its general economic protection.”
81 But see United States v. Toummin, 102 U.S. App. D.C. 325, 253 F.2d 347 (1958) (landlord appears not to have been bound by terms of the lease).
negotiated with the original tenant when the lease was signed.” It emphasizes the importance for a landlord to avoid the appearance of simply wanting more money. Another review of the case law discussing leases, among other real estate agreements, concludes that, in the absence of a specific holding, “it will be difficult to predict the outcome with any certainty” when a court considers what is reasonable.

In an effort to state objective standards of reasonableness, the following criteria have emerged as the basic issues for the jury's consideration of the landlord's good faith and commercial reasonableness:

1. Financial responsibility of the proposed assignee or subtenant;
2. Identity or business character of the proposed assignee or subtenant;
3. Legality of the proposed use; and
4. Nature of the use and occupancy.

The California Law Review Commission sets forth these criteria for assessing reasonableness of consent:

1. Credit rating of assignee or sublessee;
2. Similarity of proposed new use to old use;
3. Nature, quality, and character of assignee or sublessee;
4. Requirements of assignee or subtenant for utilities or services from the landlord;
5. Anticipated volume of business of assignee or tenant (in leases requiring percentage rent); and
6. Overall impact of assignee or sublessee on common facilities, other tenants in the building, or adjacent property of landlord.

To these criteria, a Canadian commentator would add:

1. The time elapsed since the last change in the business operated at the premises;
2. The name of the proposed transferee's business;
3. The “drawing power” of the proposed transferee;
4. The consideration being paid to the transferor (because a high price payable over time may affect the proposed transferee's ability to carry on its business); and
5. The resulting tenant mix.

That commentator would also insist upon a transfer of all the premises for the full balance of the term.

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84 Johnson & Gold, *Is it Reasonable to Agree to be Reasonable?*, Real Est. Fin. J. at 32 (Spring 2002).
[A] Landlord Found Unreasonable

Courts considering the issue of reasonableness have held that a landlord's refusal to consent to a transfer was unreasonable in these situations:

1. An assignee proposed to bind itself to each and every provision of the prime lease, its financial status was secure, and the landlord's general manager refused consent based primarily upon his subjective belief that a representative of the proposed assignee should have contacted him to discuss its financial status prior to making the application to assign. In its decision, the appeals court stated that “such subjective concerns and personal desires cannot play a role in landlord's decision to withhold its consent to an assignment of a lease, and the hearing court properly held that the defendant had unreasonably withheld its consent.”

2. A refusal to consent based on the assignee's financial condition must have a sound basis: the landlord's receipt of financial statements that “evidence a company that was losing money, but had some cash in the bank” was insufficient—especially because the landlord had tried to make a direct lease with the proposed assignee.

3. In a situation in which the sublease fully protected the landlord's bargain under the prime lease, the court stated: “The landlord has no reasonable basis for withholding consent if the landlord remains assured of all the benefits bargained for in the prime lease.”

4. A proposed assignee corporation was financially responsible, having incorporated with $25,000 cash and an approved, SBA-guaranteed $200,000 loan; a $5,000 security deposit had been tendered; the landlord had been given a security assignment of all fixtures and inventories; a personal financial statement and copies of the SBA loan agreements had been provided, and the type of business to be conducted by the assignee was identical in nature to that of the tenant. The court held: “The trial court had before it considerable evidence that the proposed corporation was financially responsible, and no evidence that it was financially irresponsible.”

5. A landlord did not inquire into any aspect of the suitability of a proposed tenant, but claimed only that it was given insufficient time to respond to the proposal under the circumstances. Specifically, the landlord claimed that it was not unreasonable for it to require additional time to respond to the sublease proposal, because the four unions that formed the corporation owning the building had a policy against any subleasing, and it was unreasonable to expect that the executive committee of the corporation could convene, deliberate, and act to change

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the policy within such a short time. The jury found that the landlord did not reasonably withhold consent to sublease because of insufficient time to act.

6. A landlord refused to consent to the assignment of a lease to another tenant in the same building who required additional space and was renting on a month-to-month basis. The court held: “Where provision is made in a lease permitting assignment of rights thereunder, limited only by the requirement of prior consent of the lessor, such consent may not be withheld unless the prospective assignee is unacceptable, using the same standards applied in the acceptance of the original lessee.”

7. A landlord that refused to consent to an assignment because of the assignee's doubtful creditworthiness was unreasonable when the assignee's performance was guaranteed by a substantial business person.

8. An Indiana appellate court found that a landlord had been unreasonable in basing a refusal to consent to an assignment on the use provision: the lease prescribed a music store and the proposed assignee was a carpet store. Since the landlord sought many different users after the tenant moved out, it was clear that the landlord had no allegiance to the music store use. Thus, it had acted unreasonably. Here again, the obligation to use reasonable efforts to mitigate implies an obligation to be reasonable to avoid a default, even if it means a change in the use.

9. A Missouri tenant sued the landlord following the landlord's refusal to consent to a sublease of part of the premises for the purpose of erecting a cellular telephone antenna. The lease provided that the landlord would not unreasonably withhold its consent. At the time in question, the tenant had 68 years left on a 99-year commercial lease for a 5-acre tract. The tenant negotiated with the cellular company to sublease 4,900 square feet of the parcel, and the tenant's attorney wrote to the landlord seeking its consent. The landlord rejected the proposal, “because it would not be in our best interest,” without even reviewing a copy of the proposed sublease. The tenant further questioned the landlord as to the reason for the refusal, and was told that consent would be given only if the original lease was renegotiated. The court held that there was sufficient evidence to support a finding that the refusal to consent was arbitrary and unreasonable, and thus the judgment for the tenant was affirmed.

10. In an Illinois case, a landlord declined a proposed subtenant that wanted an option to extend the term of the lease. The appellate court refused to hold “that a desire for an option precludes a jury from finding that a subtenant was ready to take a lease, when there was testimony that he wanted the property and was willing to negotiate for an extension of the lease and there was no evidence that an extension would not have been possible.” The case virtually holds that a landlord is unreasonable if it is not willing to give an extension of the

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lease to a proposed assignee or subtenant.

11. In an Iowa case, the tenant rented half a commercial building under a five-year lease. The lease provided that any assignment or subletting required consent of the landlord, but that consent would not be unreasonably withheld. The tenant relocated its business out of town and sought to pay its monthly rent obligation until it could find an assignee or sublessee. The tenant subsequently offered to buy out the lease, but this offer was rejected. The next year, a company sought to rent the property for a tool storage facility. The company dealt with the landlord and not the tenant. The landlord never notified the tenant of the company's interest. The prospective new tenant then rented another building in the area. When the tenant learned of the situation, the tenant stopped making rent payments, claiming that the landlord had breached its duty to the tenant. When the landlord filed an action to recover unpaid rent, the tenant brought a counterclaim. The court affirmed the decision of the trial court that the landlord had not exercised reasonable diligence to relet the premises, as it had the duty to mitigate damages following the tenant's abandonment of the premises. The landlord was required to follow through with the interested company and inform the tenant of the company's interest in the premises.

12. A Colorado landlord who refused the assignment proposed by its tenant because the landlord's president “didn't like [the proposed assignee],” could not collect rent from the tenant after it defaulted, because the landlord had failed to mitigate its damages by acting unreasonably and refusing the proposed assignee. 99

13. A Washington court considered a shopping center landlord unreasonable when it declined a proposed assignment from a home improvement center to a Value Village store because of the “image” and the “tone” of the shopping center. 100 The court recognized the permissibility of such subjective factors in a landlord's decision, but gave much greater weight to objective factors such as financial strength, responsibility, and the lawfulness of the use.

14. A Massachusetts landlord was found to have been unreasonable when it refused to consent to a sublease at or below market rent. The court observed that the profit-sharing provision did not obligate the tenant to maximize its profits on a sublease, but only provided for the situation in which it did have a profitable sublease. 101 This sort of issue is addressed by the limitations on transfers provision in Form 13-5.

15. A Louisiana landlord was not reasonable in withholding its consent to a potential competitor. The lease restricted the tenant's use to certain medical purposes. After the original landlord sold the shopping center to the owner of a nearby medical campus, the tenant sought consent to an assignment to an occupational medical clinic. The landlord declined because of the competition with its own business. The landlord was found to have been unreasonable because “reasonableness” was determined by the original landlord's expectations (which would not have included competitive effects), and because the reason for refusal was personal to the landlord. 102

16. Applying New Jersey law, the Court of Appeals for the Third Circuit confirmed a trial court ruling that a landlord had been unreasonable (in violation of the lease) when it refused to consent to a sublease because it would have had several leases ending at the same time


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The landlord's unnecessary delay in responding to a proposed assignment has been found unreasonable by a California court. 104

The Alabama Supreme Court easily concluded that “it is unreasonable for a landlord to withhold consent to an assignment of a lease in order that the landlord may extract higher rent than contracted for in the lease agreement.” 104.1

[B] Landlord Found Reasonable

A landlord's refusal to consent to the assignment of a lease has been found to be reasonable in the following cases:

1. A California landlord properly refused an assignment that would place the landlord in a less beneficial financial position than it had bargained for and could expect to continue from the present lessee under a percentage lease agreement. It was undisputed that the landlord would suffer substantial financial detriment upon the proposed assignment, while the tenant stood to gain at least $1,250 per month above the minimum rent it would be required to pass through to the landlord. The court stated: “To force Lessor to accept the minimum $2,750 figure of the original lease while Lessee pockets $1,250 per month for providing an assignee who cannot generate more than $2,750 for Lessor is out of touch with commercial reality. Refusing to consent to highway robbery cannot be deemed commercially unjustified.”

2. Prior to the assignment of a lease to a spin-off division of a Fortune 500 company, the landlord was not provided with any financial information concerning the assignee. The landlord did not have any projections of the proposed assignee's cash flow with which to determine whether there would be money left over, after paying the existing debts, to maintain the premises, pay taxes, and pay the rent. The court stated in its opinion: “A landlord is entitled to know something about projected income as well as about existing assets, as least when the assets are so encumbered.” 105

3. In Colorado, it was reasonable for a landlord to reject a proposed assignment when there was evidence to support the trial court's finding that the landlord refused to approve the assignment because it believed that a specialty restaurant of the type the proposed assignee planned to run would not be successful at that location. However, in reaching its decision, the court noted that “landlords have no right to refuse to permit an assignment on purely racial grounds.” It further stated that “arbitrary considerations of personal taste, convenience, or sensibility are not proper criteria for withholding consent under” a lease provision that

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104.1 The Pantry, Inc. v. Mosley, 126 So. 3d 132 (Ala. 2013).
105 National Distillers & Chemical Corp. v. First Nat'l Bank, 804 F.2d 978, 981 (7th Cir. 1986).
requires consent to an assignment.\textsuperscript{106}

4. In a Minnesota case, the landlord's refusal to consent to an assignment to a competitor of an existing tenant was “a valid and reasonable business concern.”\textsuperscript{107} In a similar Minnesota case, the hospital-landlord was found reasonable in refusing a competitive sublease when its arrangements with its physician-tenants, including allowances to the physicians, were meant to enhance the hospital's business. The court noted that a landlord was reasonable in withholding consent to a sublease that would defeat the purpose of the lease.\textsuperscript{108}

5. A federal district court in Florida held that a landlord could rightly refuse to consent to a sublease that was extended approximately 26 years beyond the date of the primary lease. The court stated that the landlord's refusal to consent to this assignment “was based on commercial reasonableness and was made in good faith.”\textsuperscript{109}

6. A landlord is not unreasonable to withhold its consent if it doubts the financial strength of the proposed assignee, using the standard of a reasonable person in the position of a landlord owning and leasing commercial property. An Idaho court found that a “reasonable person” was justified in having apprehensions about a proposed assignee's obligations when the proposed assignee provided incomplete financial information, and there was a risk that guaranties would be canceled.\textsuperscript{110}

7. It is reasonable for a landlord to refuse a proposed sublease because of its wish to enhance the potential for percentage rentals contemplated by the primary lease. A North Carolina court concluded that the landlord's desire to maintain a restaurant operation in the premises, in light of the nature of the building and the desire for percentage rentals, constituted reasonable grounds for withholding consent.\textsuperscript{111} During lease negotiations, the landlord will frequently insist that the percentage rent an assignee pays be commensurate with the assignee's business; that is, as a condition to an assignment the percentage rent rate may be increased. The tenant's response is often that such an adjustment makes an assignment more difficult at the time when the tenant most needs or wants to make an assignment. Put differently, the lease is less attractive to an assignee that does not get the benefit of a low percentage rent rate. This is no different from the recurrent question of who gets the bonus value in the lease. One way around the issue is a negotiated division of the profits on assignment or sublease; see §13.10.\textsuperscript{112}

8. A guarantee of rent payments is not enough to compel a landlord to accept an assignee if the tenant's performance of its other obligations (such as promises to repair the premises and indemnify the landlord against certain claims) is not assured.\textsuperscript{113}

9. A Hawaiian landlord justifiably refused consent to an assignment to an undercapitalized corporation when the principals would not guarantee the lease.\textsuperscript{114}

\textsuperscript{110}Fahrenwald v. La Bonte, 103 Idaho 751, 653 P.2d 806 (Idaho Ct. App. 1982).
10. A California landlord that operates a store in its center may be able to withhold its consent to a sublease to a competitor but a Louisiana landlord is not.

11. Landlords can base their decisions on the use provision. Of course, if the use is not specified, the landlord may be hard-pressed to object to the proposed use. At the other end of the spectrum are cases with restricted uses; in one such case, a Louisiana landlord's refusal to consent to assignment to an orthodontist was sustained when the use was specified as general dentistry only. A specification of a French restaurant operated by someone with five years' experience defeated a proposed assignment to an East Indian restaurant. A landlord can reasonably refuse when it is given no information about the proposed use.

12. When a Minnesota law firm, which occupied part of an office building and was obligated to make its law library available to other tenants in the building, proposed to assign its lease to a bank, the landlord was held to be reasonable in withholding its consent until it was assured that the proposed assignee could furnish that same law library service.

13. A Nebraska appellate court held that a landlord had not acted unreasonably in refusing to give its consent to an assignment and sublease when it believed that the subtenant would not generate as much percentage rent as the tenant; in that case, the tenant paid nearly three times the base rent as percentage rent.

14. A Mississippi landlord was reasonable to refuse its consent to an assignment unless the tenant cured environmental problems caused at the premises by a prior tenant's installation of underground storage tanks that the tenant-assignor had used, or the assignee agreed to do so; the case turned on the ownership of the leaking underground storage tanks.

15. In a Nebraska case, the landlord brought a detainer and forcible entry action after the tenant assigned the lease without first obtaining the landlord's permission. The landlord leased the premises to a supermarket operation that subsequently assigned its interest to another party, which then sublet the premises to the current tenant. The assignment and sublease were both executed without the consent of the landlord, in violation of the lease provisions prohibiting such actions. The landlord did not want the subtenant as a tenant and challenged the subtenant's right to possess the premises. The subtenant argued that the landlord was unreasonable in refusing to consent to the assignment and sublease, and alternatively that the landlord had waived the consent provision by acting in bad faith in withholding consent. The court held that a landlord can only withhold consent in good faith

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122 *Wright v. Rub A Dub Car Wash, Inc.*, 740 So. 2d 891 (Miss. 1999).
based on a reasonable objection to the assignment or sublease. The tenant bears the burden of establishing that the landlord acted in bad faith, and in this case did not meet that burden.

16. The Supreme Court of Alaska declined to rule that the landlord's insistence on a share of the sublease rent was unreasonable; rather, it said that the landlord had in effect refused to consent to the proposed sublease and that a trial was necessary to determine reasonableness. The case arose out of the supermarket tenant's desire to replace a bank subtenant (to which the landlord had previously consented although with a reservation of his rights) with another bank subtenant. The court observed that a refusal to consent because of competition with other tenants or because of a reduction in gross sales (and thus percentage rent) could be reasonable. 124

17. An Iowa court found that the landlord had not been unreasonable in refusing to consent to a sublease to a grocery store that would have necessitated substantial alterations to the premises, and perhaps affected the rights and businesses of other tenants. 124.1

18. An Alabama shopping center landlord was found to have reasonably withheld its consent to a sublease when it based its decision on the concerns of other tenants about the compatibility of the proposed use of the subleased premises as an electronic bingo parlor arcade. The court also noted that the tenant had not provided evidence of the proposed subtenant's experience or financial condition. 124.2

[C] Additional Retail Issues

Retail landlords commonly employ prohibitions of assignments or subleases that result in a subdivision of the premises.

In the case of leases requiring percentage rent, the landlord should be certain that the percentage rent is as appropriate for the assignee's use as it was for the assignor's use. If a jewelry store replaces a chain drug store, the percentage rent should be increased to correspond more closely to the percentage commonly required in jewelry stores, that is, from 1 to 5 percent to 5 to 10 percent according to the schedule in §6.06[C]. This is a recurrent problem when a tenant with high volume but low percentage rent rate assigns or subleases to a low volume user with no change in the rate. 125 A related problem arises when a tenant's assignee is in the same business as the tenant, but the landlord believes the assignee is not likely to be as successful as the tenant. In the absence of a restriction against assignment or proof that the landlord entered into the lease in reliance on the tenant's special skill, the landlord cannot prevent the assignment. 126

There are several steps that landlords can take (in addition to adjusting the percentage rate) when a percentage rent lease is assigned. The landlord can: add the last percentage rent paid (on a

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125 Carter v. Safeway Stores, 154 Ariz. 546, 744 P.2d 458 (Ariz. Ct. App. 1987) (involving a supermarket's sublease to a clothing store). Waterbury v. T.G.&Y. Stores Co., 820 F.2d 1479 (9th Cir. 1987), involved a similar experience of a California landlord. Although the lease provided that the percentage rent of an assignee would be the assignor's average percentage rent, the assignor was so successful that the landlord regretted its change to the percentage rent provision. It should have said the percentage rent payable by the assignor was the greater of that due under the lease or the average percentage rent paid by the assignor.
monthly basis) to the minimum rent; adjust the minimum rent to market rate at the time of the assignment, or adjust the minimum rent by a cost of living factor from the date of the term commencement until the date of the assignment. A California case held that a landlord was reasonable to withhold its consent to an assignment when the proposed assignee had no prospect of generating the percentage rent that the existing tenant had paid.\textsuperscript{127}

The conditions imposed by the Bankruptcy Code to assignments of shopping center leases, as discussed in §11.07[B], are nearly insurmountable; a landlord can propose those “impartial” standards to avoid a stalemate, and win a strong position in the guise of conciliation.

[D] Additional Office Issues

Assignments of office leases require somewhat less care by the landlord than do assignments of shopping center leases. Although many office uses make substantially the same demands on an office building, there are some uses that are more burdensome than others. They include business or secretarial schools, personal finance companies, employment agencies, and messenger services. Landlords may want to refuse an assignment to an entity with immunity such as a foreign consulate because of the obstacles to actions against them, as discussed in §3.12. Many landlords specifically prohibit assignment to governmental agencies. The reasons for this disfavor are variously that government entities create high traffic with users of government services that other tenants believe demean their building; governmental agencies have the inclination and ability to enforce their rights under a lease; governmental agencies may hold over after the term under the power of eminent domain, or governmental agencies burden building systems by densely populating their premises. An office building landlord will resist assignments or subleases that convert a single-tenant floor to a multi-tenant floor. Office building landlords should be certain to consider a proposed assignee’s use before consenting to an assignment; merely requiring office use is not sufficient.\textsuperscript{128}

In an effort to provide a safe-harbor for the landlord’s refusal to consent to a proposed assignment or sublease, an office lease might provide:

**FORM 13-5**

**ASSIGNMENT—OFFICE LEASE (LIMITATIONS ON TRANSFERS)**

Landlord’s consent to a proposed Transfer shall not be unreasonably withheld; however, in addition to any other grounds available under this Lease or under applicable Law for properly withholding consent to a proposed Transfer, Landlord’s consent will be deemed reasonably withheld if in Landlord’s good faith judgment: (i) the proposed Transferee does not have the financial strength (taking into account all of the Transferee’s other actual or potential obligations and liabilities) to perform its obligations with respect to the proposed Transfer (or otherwise does not satisfy Landlord’s standards for financial standing with respect to tenants under direct leases of comparable economic scope); (ii) the business and operations of the proposed Transferee are not of comparable quality to the business and operations being conducted by direct tenants of Landlord in the Building; (iii) the proposed Transferee intends to use any part of the Premises for a purpose not permitted under this Lease; (iv) either the proposed Transferee, or any person that directly or indirectly controls, is controlled by, or is under common control with the proposed Transferee occupies space...

\textsuperscript{127} John Hogan Enterprises Inc. v. Kellogg, 231 Cal Rptr. 711 (Ct. App. 1986).

\textsuperscript{128} See Saltz, Landlord Impediments to Subleasing and Assignment: Issues with Landlord’s Consent, Prob. & Prop. at 37 (July/Aug. 2007) for the tenant’s perspective on these restrictions.
in the Building or has negotiated with Landlord within the preceding one hundred eighty (180) days (or is currently negotiating with Landlord) to lease space in the Building; (v) the proposed Transferee is of a character or reputation or engaged in a business that is not consistent with the quality of the Building as shown by Landlord's direct leasing activities; (vi) the use of the Premises or the Building by the proposed Transferee would, in Landlord's judgment, significantly increase the pedestrian traffic in and out of the Building, would generate increased loitering in Common Areas, would increase security risk, or would require any alterations to the Building to comply with applicable Laws; (vii) the proposed Transfer would result in more than three subleases on each full floor of the Premises being in effect at any one time during the Term; (viii) any ground lessor or mortgagee whose consent to such Transfer is required fails to consent to it; (ix) at the time Tenant delivers the notice of the proposed Transfer, an Event of Default exists; (x) the terms of the proposed Transfer will allow the Transferee to exercise a right of renewal, right of expansion, right of first offer, or other similar rights held by Tenant (or will allow the Transferee to occupy space leased by Tenant pursuant to any such right); (xi) the proposed Transfer would cause Landlord to be in violation of another lease or agreement to which Landlord is a party or would give an occupant of the Building a right to cancel or modify its lease; (xii) the proposed Transfer would be on economic terms (based upon effective rental rates) more favorable to the Transferee than the economic terms then being accepted by Landlord for comparable direct leasing transactions in the Building, or (xiii) the proposed Transferee has the power of eminent domain, is a governmental agency, or an agency or subdivision of a foreign government.

Because this list limits the tenant's ability to assign its lease or sublease the premises, the tenant has several concerns:

(a) item (ii) is nebulous, subjective, and unnecessary in view of the use provision in the lease (which is addressed sufficiently within (iii));

(b) item (iv) seems like a fair effort for the landlord to protect its vacant space from the tenant's competition, but is not appropriate if the landlord cannot meet the proposed transferee's needs (such as a small space, a short term, or immediate availability), so it may need to be limited;

(c) item (ix) makes a favorable first impression, but in fact the existence of the tenant's default is precisely the time when a tenant needs to assign or sublease, and is no different from what the landlord will be doing if the tenant is evicted.

(d) item (x) will certainly vary by the size of the premises and the remaining term, but there is no reason for the tenant's benefits to be stopped so that its assignment rights (which are the only relevant ones since a subtenant will not have privity with the landlord) are useless (and as to the parenthetical provision, the tenant cannot be expected to vacate space it has leased);

(e) item (xi) might be limited to leases in existence when the tenant signed its lease (and disclosed to tenant) so that subsequent leases do not abridge its rights;

(f) item (xii) will certainly preclude any sublease since they are nearly always at less than the tenant's rate, but this is very difficult for a landlord to delete because of fear of competition with its vacant space, although it may be modified to allow short term subleases for a small part of the premises;

(g) item (xiii) is very broad and should be resisted, especially if the landlord has any such tenants in the building, or if owners of comparable buildings have such tenants.
The landlord may be disturbed to learn how burdensome it can be to be reasonable. Thus, the landlord often endeavors to limit its liability if it fails to be reasonable, by the means discussed in §13.07.

§13.07 LIMITING THE TENANTS' REMEDIES

Some landlords have paid dearly for the unreasonable exercise of their rights to prevent an assignment or sublease. These claims usually arise when a tenant loses an advantageous sale of its business because the landlord withholds consent. When the landlord withholds its consent to an assignment or sublease that is part of the tenant's effort to avoid default, the tenant's claim is that the landlord failed to mitigate its damages, as discussed in §31.04. 129

In one case, the tenant approached the landlords for consent to an assignment in connection with a sale of the tenant's business. The landlords, who were not bound by a "reasonableness" standard in the lease, required a renegotiation of rent and other lease provisions. When the tenant could not get consent for an assignment, it changed its sales contract into one that involved a sale of its corporate stock. The landlords claimed that their consent to a sale of stock was also necessary, although the lease did not say so. When the sale of the business was lost, the tenant sued the landlords on a theory of tortious interference with the sales contract. In upholding the tenant's lower court victory, a California appellate court noted that the landlords' concern about the assignment was "only incidental to their predominant motive of terminating the existing lease to obtain a new lease with more favorable terms to themselves." 130 The landlords had made the mistakes of: (1) not inquiring into the proposed assignee's creditworthiness, (2) expressing an interest only in improving their position, and (3) failing to show that any of their legitimate interests were threatened. 131 Incidentally, the court reiterated California's rule that a sale of corporate stock does not breach the tenant's mere promise not to assign its lease. 132

A Colorado appellate court also upheld an award of damages for breach of contract when a landlord took too long to consider a proposed assignment, and the tenant lost its proposed sale. The tenant had provided all the required information about the assignee, whose credit was admittedly acceptable, but never gotten a response. The appellate court, however, reversed the trial court's judgment for the tenant on its claim of tortious interference with prospective advantage because the tenant's claims arose under a contract. 133

Some courts have ruled for tenants when malicious interference alone is shown, 134 while

129 See Toys "R" Us v. NBD Trust Co. of Ill., Dec. 23, 1996 (U.S. Dist LEXIS 19177), for a case apparently not involving a sale, but merely a profitable sublease.
130 Richardson v. La Rancherita, 98 Cal. App. 3d 73, 159 Cal. Rptr. 285, 290 (Cal. App. 4th Dist. 1979). A similar case recurred in California with a lease that required the landlord's consent to any assignment. Sade Shoe Co. v. Oschin & Snyder, 162 Cal. App. 3d 1174, 209 Cal. Rptr. 124 (Cal. App. 2d Dist. 1984). In considering whether the complaint was legally sufficient to establish claims of interference with prospective advantage and contractual relationship, the court said that the fact that the lease may have allowed the landlord to withhold its consent arbitrarily did not furnish justification or privilege to interfere with the transaction of which the assignment was a part.
other courts have demanded that the tenant prove that the assignment or sublease failed only because of the landlord's conduct. A New York court, considering a claim of "illegal interference with precontractual negotiations" denied it because there was no allegation of illegality, and no showing that the negotiations would have succeeded but for the alleged interference.\footnote{Suskind v. Ipco Hosp. Supply Corp., 49 A.D.2d 915, 373 N.Y.S.2d 627 (N.Y. App. Div. 2d Dep't 1975).}

A frustrated prospective assignee may also have a claim against a landlord whose consent has been unreasonably withheld.\footnote{Optivision, Inc. v. Syracuse Shopping Ctr. Assocs., 472 F. Supp. 665 (N.D.N.Y. 1979) (follows Suskind).} On the other hand, a California court held that a disappointed assignee did not have standing to sue if a landlord declined its consent because the proposed assignee was not the real party in interest. In a semantic distinction, the court said that the proposed assignee might have standing if it had an assignment that was conditioned upon the landlord's consent.\footnote{Pinellas County v. Brown, 450 So.2d 240 (Fla. Dist. Ct. App. 2d Dist. 1984).} A broker may likewise have a claim.\footnote{Courthouse Plaza Co. v. Goodenough, 106 Cal. App. 4th 832, 131 Cal. Rptr. 2d 193 (Cal. App. 6th Dist. 2003).} In an Iowa case,\footnote{Donald G. Culp Co. v. Reliable Stores Corp., 14 Ohio App. 3d 161, 14 Ohio B. 178, 470 N.E.2d 193 (Ohio Ct. App., Franklin County 1983) (the broker did not recover under a theory of tortious interference with contract; the court felt that the landlord had been reasonable in requiring a restoration bond as a condition to the assignment).} an assignor recovered compensatory and punitive damages from both its landlord and its proposed subtenant; the unusual facts reveal that the landlord (who was upset with its tenant's profit on a sublease) and the subtenant (who had other acrimonious business relations with the tenant) tried to "squeeze" the tenant by a rent escrow and later direct dealings to the tenant's detriment. The New Mexico Supreme Court held that the landlord is reasonable to refuse an assignment or sublease when it would devalue the reversion, but is unreasonable to demand a share of sublease rents "not bargained for in the original lease," thus suggesting that a profit-sharing provision may be lawful.\footnote{J.M. Grimstad, Inc. v. ScanGraphics, Inc., 539 N.W.2d 732 (Iowa Ct. App. 1995).}

In view of these cases, a landlord should insist upon the following provision that exonerates it from monetary liability if it is found to have been unreasonable:

**FORM 13-6**

**ASSIGNMENT—EXONERATION FROM DAMAGES FOR UNREASONABLE REFUSAL TO CONSENT**

If Tenant believes that Landlord has unreasonably withheld its consent, Tenant's sole remedy will be to seek a declaratory judgment that Landlord has unreasonably withheld its consent, an order of specific performance, or mandatory injunction of Landlord's agreement to give its consent. Tenant will not have any right to recover damages or to terminate this Lease. Tenant will indemnify, defend, protect and hold harmless Landlord from any and all losses, liabilities, and expenses (including without limitation attorneys' fees) involving or asserted by any third party or parties (including without limitation, Tenant's proposed Transferee and any broker representing Tenant or such Transferee) claiming they were damaged by Landlord's wrongful withholding or delaying of Landlord's consent to such proposed Transfer, or other breach of this agreement.
Section {{fill character="baseline-rule" width="7" }}.  

Such a provision does not assure absolute insulation from liability. For example, a New York court held that it did not bar a tenant's claim that the landlord “acted maliciously or in bad faith.”¹⁴² Also, the provision will only bind the tenant, and not a litigious assignee or broker.

Although there are procedural devices by which an adjudication may be accelerated,¹⁴³ few assignees or subtenants will agree to await the outcome of litigation; without the assurance of a assignee or subtenant in the event of victory, no tenant will want to undertake litigation. An option may be an expedited arbitration. From a tenant's view, this sort of provision may be less appropriate in an office or single-tenant lease than in a shopping center lease where the criteria (of which tenant mix is one) are somewhat subjective, and the landlord may have an honest but unreasonable objection. On behalf of a tenant, a prudent real estate professional will limit this provision's exculpatory effect to those situations in which the landlord is found unreasonable in the application of objective criteria. To the earlier provision, a tenant would add:

Tenant may recover damages if Landlord is found either to have acted in bad faith, or to have acted unreasonably in determining the proposed assignee's or subtenant's creditworthiness, identity, business character, use, and the lawfulness of the use.

Although the landlord may be willing to accept some responsibility for culpable conduct, it may not want an open-ended risk. It may agree that the tenant can terminate its lease if the landlord is culpable.

The tenant will also want assurances that the landlord will respond promptly to its proposals of an assignee or subtenant. Like justice, consent delayed is consent denied. So the tenant will want to add:

Landlord's consent to a proposed assignment or sublease will be conclusively presumed from its failure to respond within fifteen (15) days after its receipt of Tenant's proposal.

Although the time period will be a source of friction, the landlord and tenant can come to some agreement along these lines.

To avoid claims from tenants, in any event, a landlord should:
1. State in its lease as clearly and extensively as possible the standards that will be employed in considering an assignment or sublease.
2. Insist that all of the information necessary for it to make a decision about a proposed assignment or sublease is delivered to it before a decision is made.
3. Respond as promptly as possible to proposed assignments or subleases.
4. Not insist upon changes to the lease or economic incentives as a condition to approval.
5. Not meet with the proposed assignee or subtenant except in the tenant's presence, and then only to gather the information necessary to make an informed decision.
6. Respond in writing, stating specific reasons for refusing a proposed assignment or sublease, or preferably, stating the ways in which the assignment or sublease may be made acceptable.

¹⁴³Goldstein, Provisions for Subletting or Assigning a Commercial Lease (with Form), 28 Prac. Law. at 31 (1982).
§13.08 REDEFINING THE ASSIGNMENT AND SUBLEASE

Because public policy not only favors the free alienability of property but also abhors the forfeiture of valuable rights, prohibitions of assignments and subleases are strictly construed against the restriction. A prohibition of assignments does not forbid subleases, and vice versa; a prohibition of assignments does not forbid assignments by operation of law, nor encumbrances of the leasehold (even though the effect may be an assignment if the security interest is foreclosed). A prohibition of a sublease of the premises usually does not prevent a sublease of a part of the premises. A prohibition of a sublease of the premises usually does not prevent a sublease of a part of the premises. Easements, concessions, vending machine arrangements, and licenses are not subleases. In order to avoid the many traps that the law has laid, the cautious landlord will define assignment and subletting very broadly.

FORM 13-7
ASSIGNMENT—OTHER TRANSACTIONS REQUIRING LANDLORD'S CONSENT

These transactions will also require Landlord's prior written consent:

(a) an assignment by operation of law;

(b) an imposition (whether or not consensual) of a lien, mortgage, or encumbrance upon Tenant's interest in this Lease;

(c) an arrangement (including without limitation management agreements, concessions, and licensees) that allows the use and occupancy of all or part of the Premises by any one other than Tenant;

(d) a transfer of voting control of Tenant, creation of a voting trust for any of the shares of Tenant, recapitalization of Tenant, public sale of any shares of Tenant, or redemptions of any shares of Tenant (if Tenant is a corporation);

(e) a transfer of more than 50% of the interest in the capital or beneficial ownership of Tenant (if Tenant is a partnership or limited liability company or trust); and

(f) conversion of Tenant from a general partnership to a limited liability partnership.

The provisions of clause (a) are necessary to avoid the transfer of the tenant's interest in the lease to its receiver, trustee in bankruptcy, executor, legatee, or to a purchaser of the lease or the tenant's voting stock at a judicial sale. A transfer to an individual tenant's heirs, for example, is a transfer by operation of law. In contrast to the usual methods of effecting an assignment or sublease, transfers by operation of law are not voluntary. As a rule, assignments by operation

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144 Annot., 56 A.L.R.2d 1002, Subletting or renting part of premises as violation of lease provision as to subletting (1957).

145 For a Florida case distinguishing a sublease and a license, see Hilton Head Air Serv. v. Beaufort County, 308 S.C. 450, 418 S.E.2d 849 (S.C. Ct. App. 1992), involving an unusual situation with a governmental lease to an air service operator and its license to car rental companies.

146 A very helpful discussion is Neil E. Botwinoff, Handling Assignment Clauses in an Age of Chameleon Entities (Parts I and II), Prac. Real Est. Law at p. 45 (Sept. 1999 & Nov. 1999). See also Bauer & Mantini, Change of Control in 2 Shopping Centre Leases, (H.M. Haber ed. 1982).

147 Dodier Realty & Inv. Co. v. St. Louis Nat'l Baseball Club, 361 Mo. 981, 238 S.W.2d 321 (1951).
of law do not breach a prohibition of assignments. For example, a transfer of a lease to the tenant’s legatee did not breach the tenant’s covenant not to assign the lease. However, Form 13-7 may be too broad because it may prevent a corporate merger in which the assignment may be said to be by operation of law; an exception for corporate mergers is discussed with regard to clause (d). However, in a Maryland case, a transfer of a lease by operation of law to the successor corporation violated the prohibition of assignments.

Clause (b) prevents a transfer that might occur when the lender forecloses on the leasehold. This provision is also too broad. A tenant may sell the leasehold as part of a sale of its business; assuming that the sale of the business was not a default (perhaps because it was a permissible sale of stock), the tenant may accept purchase money financing secured by the leasehold. As written, clause (b) would prevent a sale. Therefore, a prudent tenant might insist upon an exclusion from clause (b) of “liens, mortgages, or encumbrances incidental to a transaction for which landlord's consent is not required by the provisions of this paragraph.” Although only the most perspicacious tenant would divine the need to ask for the landlord's consent in advance, when a tenant assigns its lease in connection with a sale of its business, and takes a security interest in the lease to assure payment of the price for the business, the tenant must determine whether the “reassignment” necessitates the landlord's consent.

On the other hand, a federal court applying Colorado law concluded that a hair salon tenant's assignment of its license agreements with stylists to a bank did not violate the anti-assignment provision.

Although the landlord's intentions are honorable when clause (c) is proposed, once again the draftsmanship is too sweeping. The landlord wants to be certain that the tenant does not effectively sublease the premises by giving a stranger the right to use and occupy them. Often an office building tenant anticipates growth and leases more space than it needs; it may wish to share some portion of the premises until its growth occurs. This clause causes considerable consternation to a shopping center tenant that may wish to have a department run by a concessionaire, or to provide leased vending machines for customer convenience. The simple solution is to limit the area of the premises that may be occupied by others. A provision of that sort may be:

Tenant may allow individuals or entities other than Tenant (the “Other Occupants”) to occupy up to 7% of the area of the Premises, as they may be expanded from time to time, for the Term and any extension of it, so long as:

(i) no demising wall separates the office spaces occupied by such Other Occupants from the office spaces occupied by Tenant;
(ii) the number of Other Occupants (expressly as individuals as opposed to entities) occupying such office space does not exceed 7% at any one time; and
(iii) the Other Occupants have a business relationship with Tenant.

150 As to the Louisiana law and practice, see Rubin & Sperry, Lease Financing in Louisiana, 59 La. L. Rev. 845 (Spring 1999).
Landlord agrees that such occupancy by Tenant will not constitute an assignment or sublease of Tenant's interest under this Lease. In addition, at Tenant's request and cost, Landlord agrees to list the names of the Other Occupants on the Building directory located in the Building lobby for the term of their occupancy of the Premises.

The tenant must be careful not to breach its lease with an innocent office sharing arrangement if the lease only allows subleases to controlled entities. A sublease to a prospective merger partner is a default. 151.2

Because a lease is an asset of the corporate tenant, transfer of corporate stock effects a transfer of the lease. 152. This device has been used with great success in avoiding the prohibitions against assignment, 153 however, it is not infallible. 154 Even without a transfer of stock, a loosely worded restriction against transfers can be avoided by a transaction in which the tenant (a) assigns its lease to a specially created subsidiary, (b) merges the subsidiary into a specially created subsidiary of the “true” assignee, and (c) sells its shares in the subsidiary to the “true” assignee for the value of the leasehold. A more complicated structure to recover the bonus value of a lease—the amount by which market rent exceeds the lease rent—involves the (a) creation of a subsidiary to which the lease is assigned, (b) the issuance of common voting stock to the parent-tenant, (c) the issuance of non-voting preferred stock to the lender, (d) the sublease by the subsidiary to the parent-tenant at market rent, and (e) the subsidiary's payment to the lender on account of its preferred stock the difference between the market rent and the lease rent. To prevent this circumvention, the landlord may limit the definition of “affiliates” to which transfers are allowed without restriction to those affiliates all of whose shares or debt are owned by the tenant, and the landlord may allow the transfer only so long as the subsidiary remains wholly owned by the tenant.

This clause (d), then, has several objectionable aspects. First, it cannot apply either to a tenant whose stock is publicly traded or to a tenant that makes a public offering of its stock. Second, in closely held companies, it will prevent, for example, three of five equal owners from selling their interests in unrelated transactions over a 10-year period. Third, corporate flexibility is impaired

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152 Annot., 12 A.L.R.2d 179, Conditions accompanying or following dissolution of lessee corporation, as breach of covenant against assignment or sublease (1950); Rubinstein Bros. v. Ole of 34th Street, Inc., 101 Misc. 2d 563, 421 N.Y.S.2d 534 (N.Y. Civ. Ct. 1979). See also Annot., 39 A.L.R.4th 879, Merger or consolidation of corporate lessee as breach of clause in lease prohibiting, conditioning, or restricting assignment or sublease (1985) (suggesting that sales of corporate assets, as opposed to transfer of corporate stock, are more likely to breach such a clause).
154 Christacos v. Blackie's House of Beef, Inc., 583 A.2d 191 (D.C. 1990), holding that a sale of 100 percent of the corporate stock was a sale of the corporation's assets or business for purposes of a contract for the sale of a business that required an additional payment if the corporate business or assets were transferred. Similarly, an Oregon court found that a merger of a parent and its subsidiary was an assignment requiring the landlord's consent, and a breach of the lease without that consent. Pacific First Bank by Wash. Mut. v. New Morgan Park Corp., 319 Or. 342, 876 P.2d 761 (Or. 1994).
because subsidiaries and affiliated companies cannot be created to act as separate entities. Fourth, the corporation cannot sell additional shares in order to raise capital. Fifth, one shareholder cannot transfer its shares to another shareholder. Sixth, a transfer by bequest is prohibited, although a California court held that a transfer of a deceased shareholder's shares to his heirs was not a change in control.\footnote{Lindgren v. Guys, Inc., 2005 Cal. App. Unpub. LEXIS 11339.} Any restriction on transfer of stock ownership should be considered by a tenant in light of its employee stock ownership plans. In professional corporations, which are required by statute to redeem the shares of a retired, deceased, or inactive professional, such a prohibition is intolerable. By its terms, such a provision is violated by the enlargement of the tenant's board of directors and the adoption of cumulative voting; in these common occurrences, no shares have changed hands.

The strictures of such a clause may be relieved by a provision such as:

**FORM 13-8**

**ASSIGNMENT—MODIFICATION OF CORPORATE ON-ASSIGNMENT PROVISION**

Tenant may assign all or part of this Lease, or sublease all or a part of the Premises, to:

- (a) any corporation that has the power to direct Tenant's management and operation, or any corporation whose management and operation is controlled by Tenant; or,
- (b) any corporation a majority of whose voting stock is owned by Tenant; or
- (c) any corporation in which or with which Tenant, its corporate successors or assigns, is merged or consolidated, in accordance with applicable statutory provisions for merger or consolidation of corporations, so long as the liabilities of the corporations participating in such merger or consolidation are assumed by the corporation surviving such merger or created by such consolidation; or
- (d) any corporation acquiring this Lease and a substantial portion of Tenant's assets; or
- (e) any corporate successor to a successor corporation becoming such by either of the methods described in (c) or (d), so long as on the completion of such merger, consolidation, acquisition, or assumption, the successor has a net worth no less than Tenant's net worth immediately prior to such merger, consolidation, acquisition, or assumption.

Some provisions (such as the one in **FORM 13-8**) allow mergers if the surviving corporation's net worth—or credit worthiness—is at least equal to that of the tenant. This is a useless restriction for many reasons, not the least of which is that corporations do not have “net worths” (which is deliberately overlooked in the ensuing discussion). Unless the acquiring corporation has a negative net worth, the surviving corporation's net worth will always be equal to or greater than the tenant's. Some leases appear to go further by requiring the acquiring corporation to have a greater net worth than the tenant. This is not helpful. If the tenant's net worth is low (perhaps as the result of unsuccessful operations), an equally weak corporation could acquire it. Net worth tests are usually expressed in such a way that the net worth need not be maintained after the assignment; it need only exist at the time of the assignment. As a result, assets may be transferred out of the surviving corporation after the assignment and it may be left a worthless shell. An apparent solution is to require the surviving corporation to maintain its net worth as a continuing condition to the effectiveness of the assignment. This is not a fair solution since it requires more from the surviving corporation than it required from the tenant itself. Needless to say, if the real
Tenants can manipulate these sorts of modifications to the strict prohibitions on assignments or subleases. For example, a corporate tenant could assign its lease to a subsidiary and sell its stock in the subsidiary, thus transferring the lease. Real estate professionals may wish to enlarge Form 13-8 by adding prohibitions of any transactions used in order to transfer the lease, and by adding provisions that allow transfers to subsidiaries for so long as the subsidiaries remain subsidiaries of the tenant. This will avoid a transfer of the lease to a subsidiary formed solely to own it, and a subsequent merger of that subsidiary with a stranger to the lease; the effect is an otherwise impermissible assignment. Some landlords condition these permitted transfers on their use not being a subterfuge to avoid the prohibition on assignment.

As a matter of corporate law, a corporation may be liable for the debts of another corporation under a theory of successor liability if it assumed the debts existing when it merged with the debtor, or is a “mere continuation” of the debtor. A Colorado court used the “mere continuation” basis to hold a successor management company liable for the debts of a tenant of which it owned one percent of the stock. The successor had the same officers, directors, and management.\footnote{CMCB Enters., Inc. v. Ferguson, 114 P.3d 90 (Colo. Ct. App. 2005).}

A partnership tenant has understandable reservations about clause (e). Incorporation is impossible. The retirement of senior partners over a long period is precluded, as is the admission of new partners by expansion of the capital and interests in profits and losses. Although, on the theory that a partnership is an entity and not an aggregate, admission of a new partner is not a default.\footnote{Rubinstein Bros. v. Ole of 34th Street, Inc., 101 Misc.2d 563, 421 N.Y.S.2d 534 (N.Y. Civ. Ct. 1979); Friedman §7.303b.} Clause (e) speaks specifically to the magnitude of the change and not to the admission of the partner. A two-person partnership must be particularly careful of “dissolution” in broad prohibitions against assignment, because when one partner dies, the surviving partner no longer has a partnership. Unlike a partnership with more than two partners, two-person partnerships cannot be reformed after a partner dies. Most courts are sympathetic to the survivor; however, a Texas court held that a withdrawing partner's assignment of its partnership interest to its partner was a prohibited assignment.\footnote{Heflin v. Stiles, 663 S.W.2d 131 (Tex. App. Fort Worth 1983).} In a case involving a due-on-sale clause in a mortgage, a Connecticut court held that a change in the general partners of a limited partnership was not a sale.\footnote{Fidelity Trust Co. v. BVD Assocs., 196 Conn. 270, 492 A.2d 180 (1985).} In preparing a lease with this case in mind, the real estate professional may state that any change in the membership of the tenant-partnership is an assignment.

Clause (f) is necessary because of the many state laws that allow a general partnership to convert to a limited liability partnership. The liability of partners for partnership debts before the conversion is not affected, but their liability after conversion is limited. For example, what liability do the partners have in a renewal term exercised after conversion? As a condition to its consent to a conversion, the landlord may require personal guarantees in order to preserve its recourse after the conversion.

In special circumstances, the tenant may want to exclude certain transfers from the ambit of the landlord's prohibition. Those include:

1. Office sharing arrangements as previously noted. These are usually seen in leases to professionals, and are limited to a stated percentage of the area of the premises, and to people in the same line of work as the tenant, such as lawyers and accountants.
2. Transfers to a franchisee. The franchisor usually remains liable.
3. Transfers to the tenant's employees' stock ownership plan.

4. Transfers of fewer than all of tenant's locations. This is common in a national retail tenant's lease when the stores in a region may be sold.

Although it is by no means common apart from ground leases, a tenant may want to borrow money on the value of its lease. A leasehold mortgage is similar to a “garden variety” mortgage of a fee interest, except that the foreclosing lender gets a lease instead of a fee and the landlord gets a new tenant that is unlikely to know how to run the defaulting tenant's business. In order to be able to finance its leasehold, a tenant will ask for the right to do it (since the landlord's form of lease probably restricts collateral assignments) and request lender-protective provisions such as:

1.1 Protection of Leasehold Mortgagees. If Tenant mortgages this Lease in compliance with the provisions of this Article, then so long as any such Leasehold Mortgage remains unsatisfied of record, these provisions will apply:

1.1.1 Consent. No cancellation, surrender or modification of this Lease will be effective as to any Leasehold Mortgagee unless consented to in writing by the Leasehold Mortgagee, except that consent will not be required with respect to a termination in accordance with this Article or with Articles (damage and destruction and condemnation provisions)

Condemnation.

1.1.2 Notice of Default. Landlord, upon providing Tenant any notice of: (a) default under this Lease, or (b) a termination of this Lease, or (c) a matter on which Landlord may predicate or claim a default, will at the same time provide a copy of such notice to every Leasehold Mortgagee of which Landlord has been provided notice in accordance with Section [{fill character="baseline-rule" width="7" }]. Landlord will have no liability for the failure to give any notice, except that no notice by Landlord to Tenant will be deemed to have been duly given unless and until a copy has been so provided to every Leasehold Mortgagee of which Landlord has been provided notice in accordance with Section [{fill character="baseline-rule" width="7" }]. After notice has been given to a Leasehold Mortgagee, the Leasehold Mortgagee will have the same period, after the giving of such notice upon it, for remedying any default or acts or omissions which are the subject matter of such notice, or causing the same to be remedied, as is given Tenant after the giving of such notice to Tenant, plus in each instance, the additional periods of time specified in Section [{fill character="baseline-rule" width="7" } to remedy, commence remedying or cause to be remedied the defaults or acts or omissions specified in such notice. Landlord will accept such performance by or at the instigation of such Leasehold Mortgagee as if the same had been done by Tenant. Tenant authorizes each Leasehold Mortgagee to take any such action at
such Leasehold Mortgagee’s option and does authorize entry upon the Premises by the Leasehold Mortgagee for such purpose.

1.1.3 Notice to Mortgagee. If any default occurs which entitles Landlord to terminate this Lease, Landlord will have no right to terminate this Lease unless, following the expiration of the period of time given Tenant to cure such default or the act or omission which gave rise to such default, Landlord notifies every Leasehold Mortgagee of Landlord’s intent to so terminate at least thirty (30) days in advance of the proposed effective date of such termination if the nature of such default is the failure to pay a sum of money to Landlord, and at least ninety (90) days in advance of the proposed effective date of such termination in the event of any other default. The provisions of Section [fill character="baseline-rule" width="7"] will apply only if, during such 30- or 90-day termination notice period, any Leasehold Mortgagee will:

(a) Notify Landlord of the Leasehold Mortgagee’s desire to nullify such notice; and
(b) Pay or cause to be paid all Rent and other payments (i) then due and in arrears as specified in the termination notice to such Leasehold Mortgagee and (ii) any of the same which become due during such 30- or 90-day period as and when they become due; and
(c) Comply or in good faith, with reasonable diligence, commence to comply with all non-monetary requirements of this Lease then in default and reasonably susceptible of being complied with by the Leasehold Mortgagee; however, that the Leasehold Mortgagee will not be required during such 30-day or 90-day period to cure or commence to cure any default consisting of Tenant’s failure to satisfy and discharge any lien, charge or encumbrance against Tenant’s interest in this Lease or the Premises junior in priority to the lien of the Leasehold Mortgage held by the Leasehold Mortgagee.

Any notice to be given by Landlord to a Leasehold Mortgagee pursuant to any provision of this Section will be deemed properly addressed if sent to the Leasehold Mortgagee who served the notice referred to in Section [fill character="baseline-rule" width="7"] unless notice of a change of Leasehold Mortgage ownership has been given to Landlord in writing.

1.1.4 Procedure on Default.

(a) If Landlord elects to terminate this Lease by reason of any default of Tenant, and a Leasehold Mortgagee has proceeded in the
manner provided for by Section {{fill character="baseline-rule" width="7" }}, this Lease will not be deemed terminated so long as the Leasehold Mortgagee will:

(i) Pays or causes to be paid the Rent and other monetary obligations of Tenant under this Lease as they become due, and continue its good faith efforts to perform all of Tenant's other obligations under this Lease excepting (A) obligations of Tenant to satisfy or otherwise discharge any lien, charge or encumbrance against Tenant's interest in this Lease or the Leasehold Estate junior in priority to the lien of the Leasehold Mortgage held by the Leasehold Mortgagee, and (B) past non-monetary obligations then in default and not reasonably susceptible of being cured by the Leasehold Mortgagee; and

(ii) If not enjoined or stayed, take steps to acquire or sell Tenant's interest in this Lease by foreclosure of the Leasehold Mortgage or other appropriate means and prosecute the same with due diligence.

Nothing in this Section, however, will be construed to extend this Lease beyond the original Term, nor to require a Leasehold Mortgagee to continue such foreclosure proceedings after the default has been cured. If the default will be cured and the Leasehold Mortgagee discontinues such foreclosure proceedings, this Lease will continue in full force and effect as if Tenant had not defaulted under this Lease.

(b) If a Leasehold Mortgagee is complying with subsection (a) of this Section, upon the acquisition of the Leasehold Estate by such Leasehold Mortgagee or its designee or any other purchaser at a foreclosure sale or otherwise and the discharge of any lien, charge or encumbrance against Tenant's interest in this Lease or the Premises which is junior in priority to the lien of the Leasehold Mortgage held by the Leasehold Mortgagee and which Tenant is obligated to satisfy and discharge by reason of the terms of this Lease, this Lease will continue in full force and effect as if Tenant had not defaulted under this Lease.

(c) The making of a Leasehold Mortgage will not be deemed to constitute an assignment or transfer of this Lease or the Leasehold Estate, nor will any Leasehold Mortgagee, as such, be deemed to be an assignee or transferee of this Lease or of the Leasehold Estate so as to require such Leasehold Mortgagee, as such, to assume the performance of any of the terms, covenants or conditions on the part of Tenant to be performed, but the purchaser at any sale of this Lease and of the Leasehold Estate in any proceedings for the foreclosure of any Leasehold Mortgage, or the assignee or transferee of this Lease and of the Leasehold Estate under any instrument of assignment or transfer in lieu of the foreclosure of any Leasehold Mortgage, will be deemed to be an assignee or transferee within the meaning of this Section and will be deemed to have agreed to perform all of the terms, covenants and conditions on the part of Tenant to be performed from and after the date of such
purchase and assignment only for as long as such purchaser or assignee is the holder of this Leasehold Estate. If the Leasehold Mortgagee or its designee becomes holder of the Leasehold Estate and if the Premises will have been or become materially damaged on, before or after the date of such purchase and assignment, the Leasehold Mortgagee or such designee will be obligated to repair, replace or reconstruct the Improvements only to the extent Tenant is required to do so by the terms of Section [fill character="baseline-rule" width="7"] of this Lease (the damage and destruction provisions) and then only to the extent of the insurance proceeds received by the Leasehold Mortgagee or such designee by reason of such damage. If such net insurance proceeds are insufficient to repair, replace or reconstruct the Improvements and if the Leasehold Mortgagee or such designee chooses not to reconstruct the Improvements, such failure will be a default by Tenant under this Lease, and the net insurance proceeds will be distributed to the parties as provided in Section [fill character="baseline-rule" width="7"] (damage and destruction provisions); provided that the Leasehold Mortgagee will not be entitled to receive insurance proceeds in excess of the then outstanding balance of the debt secured by the Leasehold Mortgage.

(d) Any Leasehold Mortgagee or other acquirer of the Leasehold Estate pursuant to foreclosure, assignment in lieu of foreclosure or other proceedings, and any tenant under a New Lease (as defined in Section [fill character="baseline-rule" width="7"]), may, upon acquiring the Leasehold Estate, without further consent of Landlord sell and assign the Leasehold Estate on such terms and to such persons and organizations ("Subsequent Assignee") as are acceptable to such Leasehold Mortgagee or acquirer and be relieved of all obligations under this Lease so long as such Subsequent Assignee has delivered to Landlord its written agreement to be bound by all of the provisions of this Lease.

(e) Any sale of this Lease and of the Leasehold Estate in any proceedings for the Foreclosure of any Leasehold Mortgage, or the assignment or transfer of this Lease and of the Leasehold Estate in lieu of the Foreclosure of any Leasehold Mortgage, will be deemed to be a permitted sale, transfer or assignment of this Lease and of the Leasehold Estate.

The landlord's concerns are that it will get paid rent by the successor lender-tenant and that the
entity to whom the lender-tenant assigns the lease (since the lender will not conduct business in the premises) meets the assignment standards in the lease. In the retail context, the landlord will also be concerned about co-tenancy requirements and whether the lender will satisfy them.

§13.09 IMPOSING FURTHER CONDITIONS TO CONSENT

Once it has agreed to give its consent, the landlord will usually add further conditions to its consent:

**FORM 13-9**

**ASSIGNMENT—PROHIBITION OF FURTHER ASSIGNMENT**

Landlord’s consent to one assignment or sublease will not waive the requirement of its consent to any subsequent assignment or sublease.

This provision is meant to avoid the result in *Dumpor’s Case*. The giving of one consent required by a lease ends the requirement for future consents. To be precise, the rule in *Dumpor’s Case* is not applied to consents to subleases, only to consents to assignments. The rule has been mercilessly criticized but rarely disavowed. As recently as 1971, a New York court wrote, “The written consent to the first assignment obviated the necessity for consent to further assignments,” and at least one other New York court has followed the rule. The simple provision in **Form 13-9** avoids such results.

In order to give an informed consent to a proposed assignment or sublease, the landlord needs some information, and may want to insert the following:

**FORM 13-10**

**ASSIGNMENT—SUBMISSION OF INFORMATION**

If Tenant requests Landlord’s consent to a specific assignment or sublease, Tenant will give Landlord at the time of its request: (i) the name and address of the proposed assignee or subtenant, (ii) a copy of the proposed assignment or sublease, (iii) reasonably satisfactory information about the nature, business, and business history of the proposed assignee or subtenant, and its proposed use of the Premises, and (iv) banking, financial, or other credit information, and references about the proposed assignee or subtenant sufficient to enable Landlord to determine the financial responsibility and character of the proposed assignee or subtenant.

A tenant does not owe its landlord a duty of care in selecting an assignee, and if the lease releases the tenant upon an assignment, the tenant is not liable to its landlord for negligence if the premises are damaged after the insolvent assignee vacates the premises.

The landlord will also insist that:

**FORM 13-11**

**ASSIGNMENT—FURTHER DOCUMENTS TO BE PROVIDED BY TENANT**

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Landlord's consent to an assignment or sublease will not be effective until: a fully executed copy of the instrument of assignment or sublease has been delivered to Landlord; in the case of an assignment, Landlord has received a written instrument in which the assignee has assumed and agreed to perform all of Tenant's obligations in the Lease; and Landlord has been reimbursed for its attorneys' fees and costs incurred in connection with both determining whether to give its consent and giving its consent.

This provision requires the assignee's assumption of all the tenant's responsibilities in the lease, not just those that accrue after the date of assignment. This avoids any question of whether the tenant's obligations run with the land, because it creates privity of contract as well as privity of estate between the landlord and assignee. The tenant and assignee must arrange between themselves for the payment and performance of obligations that have accrued but are not yet due.

The landlord will usually add:

**FORM 13-12**

ASSIGNMENT—NO RELEASE OF TENANT

Landlord's consent to an assignment or sublease will not release Tenant from the payment and performance of its obligations in the Lease, but rather Tenant and its assignee will be jointly and severally primarily liable for such payment and performance. An assignment or sublease without Landlord's prior written consent will be void at Landlord's option.

A tenant-assignor should realize that, after an assignment, it remains liable by privity of contract for payment of rent and performance of its other promises in the lease. This rule continues the tenant-assignor's liability through extensions and renewals of the lease; however, an assignor is not obligated for its assignee's unpaid rent accrued during a holdover period to which the landlord consents. Courts are divided on the question of whether the original tenant remains liable primarily or merely as a surety, in much the same way as courts divide on the question of whether a mortgagor remains primarily liable or liable only as a surety when it sells its encumbered property. The form of the tenant's assignment and the landlord's consent to it should address this issue. In order to preserve its rights against the tenant-assignor, the landlord must be certain to give it any notices and cure rights that the lease provides. In a shopping center lease, the landlord may also insist that the minimum rent be increased to the greater of (1) market minimum rent or (2) the average minimum rent and percentage rent paid by the assignee during its occupancy of the premises. The landlord could also insist upon a recapture or profit-sharing provision such as those discussed in §13.10.

Leases should provide that assignments made in contravention of the prohibition are void at the landlord's option. Otherwise, the assignment may be effective and the landlord may have only a claim for damages from the breach (if any could be shown). A purchase contract that fell prey to judicial scrutiny provided:

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165 Caneva v. Miners & Merchants Bank, 335 N.W.2d 339 (S.D. 1983).
166 Green (ed.), Keeping Current—Property, Prob. & Prop. at 25 (Nov./Dec. 2012) (holding that an assignment made in violation of the lease was voidable at the landlord's option and effective until termination of the lease by the landlord); Anderson v. Lissandri, 19 Mass. App. Ct. 191, 472 N.E.2d 1365 (1985) (in which the landlord was found to have consented to the assignment when it cashed the assignee's checks with knowledge of the assignment).
Purchaser shall have the right to assign this agreement to any partnership which [sic]is a general partner; provided however, that purchaser shall have such right of assignment only if such assignee or transferee shall in writing expressly assume and agree to perform and discharge each and every obligation and liability of purchaser set forth in this agreement.

The court held that this paragraph amounted to a restriction on delegation of duties, and not a restriction on the assignment of rights. The court was influenced by the fact that the purchaser's name was followed by “and/or assigns,” and that the binding effect provision included “assigns.”

Finally, when a lease is guaranteed, the landlord should condition its consent on the guarantor's ratification of the assignment. This may avoid the guarantor's defense that its risk was enlarged without its consent, as discussed in §31.06. When the lease and guarantee are negotiated, the guarantor may want to be released upon an assignment. The landlord might agree if the guarantor or the assignee produces a substitute guarantee of equivalent creditworthiness (or sufficient credit to support the remaining lease obligations). The problem with the guarantor insisting upon a release is that an otherwise acceptable and creditworthy assignee may be unable to produce a guarantor and the assignment may fail, perhaps with the unintended consequence that the guarantor is liable when the tenant fails, even though the assignee would not have failed.

§13.10 RECAPTURE AND PROFIT SHARING

[A] Recapture

The recapture provision is another weapon in the landlord's arsenal of anti-assignment weaponry. The recapture right enables the landlord to take back the premises if the tenant has a proposed assignment or sublease. In one way or another, it enables the landlord to take the increased rental value for itself if the tenant intends to assign the lease or to sublease the premises. To the real estate professional, the recapture provision may seem like the due on sale provision of a mortgage. The landlord may exercise this right to make money, to make a longer lease with the proposed subtenant or assignee, or to offer the space to a larger tenant. In some cases (of which Form 13-13 is an example), a recapture provision gives the landlord a right to take an assignment or sublease from the tenant at the lower of the lease rate or proposed transfer rate (and, thus, not release the tenant), and then to do the assignment or sublease that the tenant proposed. Variations include: the landlord's right to terminate the lease as to the part of the

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168 See §33.23.


170 See Saltz, Landlord Impediments to Subleasing and Assignment, Prob. & Prop. at 42 (May/June 2007) for a history of the development of recapture and profit sharing.
premises proposed to be transferred, with the result that (in the case of a sublease) the tenant never has the use or value of the space again; and a suspension of the tenant's rights in the premises for the duration of the sublease or assignment, with the result that the tenant is not completely rid of the space. The lease could grant the landlord the ability to exercise its recapture rights merely because the tenant proposes a transfer, even though it does not have a commitment from a transferee. In any case, the result is that the landlord takes, and the tenant loses part or all of the value of the lease.

This provision not only precludes the tenant's profit, but also impedes an assignment or sublease because prospective transferees are loath to negotiate their best deal only to find that the landlord has taken it. Coupled with short-term leases and periodic adjustments of rent, this provision virtually eliminates any bonus value in the lease. Recapture and profit-sharing provisions are more common in office building leases than in shopping center leases, where shorter terms, percentage rents, and much more stringent restrictions on assignments or subleases inhibit such transfers by the tenant.

A common variation on recapture is to give the landlord a right to recapture if the tenant advises the landlord that it proposes to go to market for an assignment or sublease. If the landlord recaptures the premises, the tenant is spared the rent expense while it finds a transferee. If the landlord does not recapture, then the tenant can make a transfer without fear that the landlord will then exercise its recapture rights. Of course, the transfer is subject to the requirements and standards in the lease. If the landlord passes up its recapture right and the tenant does not present a proposal in a stated period, the landlord's rights revive; in other words, the tenant cannot ask once and have a perpetual right to avoid recapture. A refinement of this approach allows the landlord to recapture the space when the proposed transferee is presented (even though the landlord previously passed up its recapture right) if the landlord reimburses the tenant's costs incurred in effecting the proposed transfer.

Tenants should have concerns about recapture provisions. Many of these provisions are written in such a way that: the tenant is not released because the landlord takes an assignment or sublease; the landlord can recapture the entire premises even though the proposed transfer affects only part of them; the tenant cannot make transfers to permitted transferees (such as parent, sister, or subsidiary corporations) without triggering the recapture rights; the landlord has a long or unstated period within which to exercise its recapture right, and the tenant cannot withdraw its proposed transfer if the landlord has indicated that it will exercise its recapture rights. 171 The tenant may also wonder if it is liable to its broker for a commission if the landlord recaptures the premises after the broker finds an assignee; in what condition the premises will be returned if the landlord accepts a sublease from the tenant, and who pays for the improvements for the subleased space, the separation of the subleased space from the rest of the premises, and the reunion of the subleased space to the rest of the premises at the end of the sublease. The tenant should also be concerned about its recovery of the cost of improvements it has made to the premises. The proposed assignment or sublease may have enabled it to recover some or all of those costs, but a recapture will eliminate that prospect. Thus, some tenants ask for the unamortized cost of their improvements if the landlord recaptures the premises.

A recapture provision in one or more leases in a retail chain may make acquisition of the chain impossible and, thus, depress its value; chains often resist recapture especially in the event of a sale of all or substantially all its stores in the chain or region. This difficulty is avoided if transfers of a stated number of stores or all the stores in a region are excluded by definition from the transfer restrictions.

171 Miller, Counseling the Client on Assignments and Subleases, 14 Prac. Real Est. Law at 31 (Jan. 1998).
In most cases, the tenant wants to assign its lease if it has outgrown its premises or if it has come into financial difficulty. If the reason is financial difficulties, then the landlord should bear in mind the possibility of a default, and consider the discussion in §13.11. If the tenant has outgrown the premises, the tenant must satisfy its needs; the tenant probably wants the difference between its rent and the proposed assignment or sublease rent to defray the expenses of its new premises.

The California Supreme Court held that a recapture provision is not an unreasonable restraint on alienation, 172 and that the landlord's exercise of its recapture rights is not a breach of the implied covenant of good faith and fair dealing. The court was influenced by the landlord's express right to enter into a lease with the proposed assignee or subtenant, and by the provision that the tenant's improvements become the landlord's property (thus precluding any unjust enrichment of the landlord by exercising its recapture rights). Given this imprimatur, the following provision will be seen frequently by the real estate professional:

**FORM 13-13**

**ASSIGNMENT—LANDLORD'S RIGHT TO RECAPTURE**

If Tenant intends to assign all or part of this Lease or to sublease all or any portion of the Premises, it will first submit to Landlord the documents described in [Form 13-10], and will offer in writing:

(a) with respect to a prospective assignment, to assign this Lease to Landlord without cost; or,

(b) with respect to a prospective sublease, to sublease to Landlord the portion of the Premises involved (the "Leaseback Area")

(i) for the term specified by Tenant in its offer,

(ii) at the lower of (A) Tenant's proposed subrent or (B) the rate of base monthly rent and additional rent then in effect according to this Lease, and

(iii) on the same terms, covenants and conditions contained in this Lease and applicable to the Leaseback Area. The offer will specify the date on which the Leaseback Area will be made available to Landlord; however, that date will not be earlier than thirty (30) days nor later than one hundred eighty (180) days after Landlord's acceptance of the offer. Tenant may withdraw the offer at any time before it is accepted. If the prospective sublease results in all or substantially all of the Premises being subleased, then, if Landlord accepts the offer, Landlord will have the option to extend the term of its sublease for the balance of the Term of this Lease less one day.

Landlord will accept or reject the offer within thirty (30) days after it receives the offer. If Landlord accepts the offer, Tenant will then execute and deliver to Landlord, or to anyone designated by Landlord, an assignment or sublease, as the case may be, in either case in a form reasonably satisfactory to Landlord's counsel. If Landlord accepts the offer, this Lease will terminate on the date set forth in the offer for the delivery of the Leaseback Area and Landlord and Tenant will be relieved of their obligations to each other as of that date. If Landlord rejects the offer, or fails to accept the offer within such

172 Carma Developers (Cal.), Inc. v. Marathon Dev. California, Inc., 2 Cal. 4th 342, 6 Cal. Rptr. 2d 467, 826 P.2d 710 (1992), in which the landlord's recapture right arose if the tenant merely gave notice of its intention to assign or sublease.
period, Tenant may assign the Lease or sublease the Leaseback Area; however, any sublease will be subject to the provisions of this paragraph as though the subtenant were the Tenant under this Lease.

Any sublease made to Landlord or its designee will:

(a) permit Landlord to make further subleases of all or any part of the Leaseback Area and (at no cost to Tenant) to make, at Landlord's expense, all changes, alterations, installations, and improvements in the Leaseback Area as Landlord may deem necessary for such subletting;

(b) provide that Tenant will at all times permit reasonably appropriate access to the common facilities in the Leaseback Area and to and from the Leaseback Area and Common Areas of the Building;

(c) negate any intention that the estate created under such sublease be merged with any other estate held by Landlord or Tenant;

(d) provide that Landlord will accept the Leaseback Area “as is” except that Landlord, at Tenant's expense, will perform all work and make all alterations required to separate the Leaseback Area from the remainder of the Premises and to permit lawful occupancy, so that Tenant will have no other cost or expense in connection with the subletting of the Leaseback Area; and

(e) provide that at the expiration of the term of the sublease Tenant will accept the Leaseback Area in its then-existing condition, subject to the obligations of Landlord to make such repairs to the Leaseback Area as may be necessary to preserve the Leaseback Area in good order and condition, ordinary wear and tear excepted.

Performance by Landlord, or its designee, under a sublease of the Leaseback Area will be deemed performance by Tenant of any similar obligation under this Lease, and any default by Landlord, or its designee, under any sublease will not be a default under a similar obligation contained in this Lease. Tenant will not be liable for any default under this Lease or deemed to be in default under this Lease if the default is occasioned by or arises from any act or omission of subtenant under the sublease or if it is occasioned by an act or omission of any occupant holding under the sublease.

The objections raised to rights of first refusal to lease in §4.18[C] and rights of first refusal to purchase in §4.18[H] are applicable to recapture provisions, and should be considered when reviewing them. Tenants should be certain that recapture rights are triggered by an actual offer that the tenants intend to accept, and not merely by a proposal subject to negotiation.

A tenant ought to require its landlord to repay the unamortized cost of the tenant's own improvements if the landlord exercises a recapture right; presumably the tenant would have been made whole in these costs if it had assigned the lease or sublet the premises without hindrance by the recapture provision. Without a right to such repayment, the tenant will have unwittingly improved the premises for its landlord's benefit.

[B] Profit Sharing

As an alternative to a recapture provision (and perhaps, in addition to it) a landlord may provide that the tenant must pay part or all of the profit on a transfer; some real estate professionals prefer to use the term “transfer premium,” especially when the tax status of the landlord prohibits its sharing of profits. A profit-sharing provision may be:
FORM 13-14
ASSIGNMENT—PROFIT SHARING ON ASSIGNMENT OR SUBLEASE

Without affecting any of its other obligations under this Lease, Tenant will pay Landlord as Additional Rent one-half of any sums or other economic consideration that (a) are received by Tenant as a result of an assignment or subletting (other than the rental or other payments that are attributable to the amortization over the term of this Lease of the cost of nonbuilding standard leasehold improvements that are part of the assigned or sublet portion of the Premises and have been paid for by Tenant), whether or not denominated rentals under the assignment or sublease, and (b) exceed in total the sums which Tenant is obligated to pay Landlord under this Lease (prorated to reflect obligations allocable to that portion of the Premises subject to such assignment or sublease). The failure or inability of the assignee or subtenant to pay Tenant pursuant to the assignment or sublease will not relieve Tenant from its obligations to Landlord under this Section. Tenant will not amend the assignment or sublease in such a way as to reduce or delay payment of amounts that are provided in the assignment or sublease approved by Landlord.

The profit sharing is usually 50/50. A landlord that insists upon all the profit gives the tenant no reason to make a profit. A Massachusetts court found that a landlord who was entitled to share profits was unreasonable to refuse to consent to a sublease at a subrent equal to what the tenant was paying, thus having no profit for the landlord. 173

The tenant will resist this provision by saying that it (and not the landlord) bears the risk that the premises are less valuable, and that the tenant should be entitled to the increase in value; moreover, the tenant will say the landlord is not making any less than it expected as a result of the assignment or sublease. The tenant's argument is stronger if it has made substantial improvements to the premises and has, in a sense, created their value, because the tenant has run the real risk that it might not recover its investment. The tenant's argument is stronger still if the lease forbids subleases or assignments at rates below those being offered by the landlord, because in that case, the tenant is locked into payments regardless of value.

The tenant must make sure to recover certain costs before the “profit” is calculated. These include: the cost of original leasehold improvements in the subleased premises made at the tenant's expense; the cost of improvements made for the transferee or an allowance given to it; the tenant's incidental costs of the transfer, such as attorneys' fees and advertising costs; the cost of takeover leases, moving allowance, free rent, and other tenant concessions; brokerage commissions and other marketing costs; advertising costs, and depreciation on furniture, fixtures, and equipment for which the tenant paid, and which the subtenant is allowed to use. Some tenants also insist upon including any rent paid between the date on which they vacated the premises (if they did) and the date on which the transferee took occupancy. They view this as a cost to preserve the premises from which the profit arose. Landlords view it as an obligation the tenant had in any event, and do not know why their share of the profits should be reduced by the time the tenant takes to effect a transfer. For itself, the landlord will want all revenue or other value received by the tenant in connection with the assignment or sublease to be considered in determining the landlord's share of the profits. This includes, without limitation, base rent, bonus payments, and additional rent (such as a share of operating expenses). The landlord may consider the price paid in excess of book value for fixed assets to be “profit.” If the lease had a rentabatement, the landlord and tenant must determine whether profit is measured against the face rate or the effective rate.

An important—and often overlooked—question is whether the tenant's costs are spread over the term of the sublease or the balance of the term of the lease, or recovered from first dollars paid to the tenant. If they are spread, the tenant is at risk for the transferee's performance, and the landlord gets money sooner.

The tenant should insist that it is released from liability if any part of the premises is recaptured or made subject to the profit-sharing provision; the landlord will not want to release the tenant if the recapture or profit sharing occurs in connection with a sublease.

If a profit-sharing provision is used in a retail lease, the landlord and tenant should consider how it affects a sale of all of the tenant's assets, including the lease. If the tenant cannot convince the landlord to exclude such transactions from the ambit of the profit-sharing provision, the tenant may try to avoid its effect by its allocation of the purchase price to fixtures, inventory, or goodwill. The landlord may want to provide that the lease must be appraised in connection with any of those transactions, and that the profit sharing be based upon the appraised value.

Despite its approval of recapture provisions, the California judiciary has not blithely accepted profit-sharing provisions. When a dry cleaner sold its business, it allocated the price to the business and the noncompete covenant. It gave no value to the lease that was believed to be above the market value. When the landlord demanded a portion of the amount allocated to the covenant not to compete, the sale failed and the tenant sued the landlord. The appellate court affirmed the trial court's award of compensatory damages for the tenant, although it reversed the punitive damages award because punitive damages are available only in tort claims not contract claims.

The profit-sharing provision should be carefully considered when tax exempt entities (such as pension plans) are landlords because, as a general rule, income based on the tenant's profit will be taxable. The sparse and inconclusive authority on the matter suggests that amounts received from a tenant in a sharing of proceeds from a transfer will not be excluded from the term “rents from real property” within the meaning of §856(d)(1)(A) of the Internal Revenue Code of 1986, as amended, insofar as real estate investment trusts are concerned.

§13.11 RELATIONSHIP OF PROHIBITIONS OF ASSIGNMENT AND SUBLEASE TO DEFAULT PROVISIONS

When a landlord balks at the suggestion that its consent to an assignment or subleasing should not be unreasonably withheld, the tenant ought to point out the interrelationship of the default provisions and the provisions regarding transfers. As a practical matter, the tenant that cannot assign its lease is often a tenant that soon cannot perform its lease.

Some of the cases in which courts have held that the landlord's consent to a proposed assignment or sublease cannot be unreasonably withheld, even in the absence of an express requirement, have considered the landlord's claim for rent from a defaulting tenant. The courts held that the landlords could not recover rent because they failed to mitigate their damages by their refusal to allow a proposed transfer. This is a familiar doctrine in contract law discussed

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174 E. Halper, *Shopping Center and Store Leases* §10.01 (n) (Supp. 1984).
177 Friedman §7.304a.
178 *Danpar Assocs. v. Somersville Mills Sales Room, Inc.*, 182 Conn. 444, 438 A.2d 708 (1980). However, the Connecticut Supreme Court held that a landlord may arbitrarily withhold its
in §31.04. Its application to leases recognizes the convergence of contract law and real property
law. On the strength of this argument, the tenant may demand a reasonableness standard as a
condition to the landlord's recovery of rent accruing after default.

By the same token, states that have adopted the contract law rule that a landlord must mitigate
its damages have opened the door for the tenant's argument that a landlord cannot unreasonably withhold its consent to a proposed assignment or sublease if the effect will be a
default by its tenant. Put differently, it is illogical to require mitigation on default but not to
require conduct that would avoid a default. Needless to say, this argument is of no benefit to a
tenant that wants to profit from its sublease or assignment.

The real estate professional may have noted the irony of a strong anti-assignment provision,
and its defeat in the face of a weak tenant's default. If the landlord has declined a preferred
transfer that would have avoided the tenant's default, it cannot successfully pursue the tenant after
the default if the landlord has relet the premises on the terms proposed by the tenant. “If the
landlord has no practical reason for wanting to terminate the lease and find a new tenant for
essentially the same rent, any landlord with reasonable business judgment will not attempt to
enforce the prohibitions on assignment, regardless of how tightly they may be drafted,” one
commentator has observed. 180

§13.12 PREPARING A FORM OF ASSIGNMENT

A form of assignment is:

FORM 13-15
ASSIGNMENT OF LEASE

For valuable consideration, the receipt and adequacy of which are expressly
acknowledged, Assignor and Assignee agree that:

1. Definitions. In this Assignment, the following terms have the meanings given to them:

(a) Assignor: 
(b) Assignee: 
(c) Lease: 
(d) Premises: Unit

179 See §31.04.
180 Cavitt, Defiant Assignment: When Boilerplate Meets Reality, Prob. & Prop. at 27
(Sept./Oct. 1997).
2. **Assignment and Delivery of the Premises.** Assignor assigns to Assignee, effective as of the Date, all of Assignor’s right, title, and interest in (a) the Lease, (b) the Security Deposit made pursuant to the Lease, and (c) the Minimum Rent (the "Rent") prepaid under the Lease. Assignor reserves the right, however, to receive any refunds of overpayments from Landlord relating to the period prior to the Date. Assignor will deliver possession of the Premises to Assignee on the Date or on such other date as may be set forth above for Delivery of Possession.

3. **Assumption and Acceptance of the Premises.** Assignee assumes and agrees to perform each and every obligation of Assignor under the Lease, effective as of the Date. Assignee will accept the Premises in their condition as of the Date.

4. **Assignor’s Warranties.** Assignor warrants to Assignee that (a) the Lease is in full force and effect and unmodified; (b) Assignor's interest in the Lease is free and clear of any liens, encumbrances, or adverse interests of third parties; (c) Assignor has full and lawful authority to assign its interest in the Lease; and (d) there is no default under the Lease or any circumstances which by lapse of time or after notice would be a default under the Lease. The warranties contained in this paragraph will be true as of the date of Assignor's execution of this Assignment and will be true as of the Date. The warranties will survive the Date.

5. **Mutual Indemnification.** Assignor will indemnify Assignee against and hold Assignee harmless from any and all loss, liability, and expense (including reasonable attorneys' fees and court costs) arising out of any breach by Assignor of its warranties contained in this Assignment, and Assignee will indemnify Assignor against and will hold Assignor harmless from any loss, liability, and expense (including reasonable attorneys' fees and court costs) arising out of any breach by Assignee of its agreements contained in this Assignment after the Date.

6. **Rent.** Commencing on the Date, the Minimum Rent will be the New Minimum Rent and the Percentage Rent will be the New Percentage Rent.
7. **CAM Reconciliation.** Assignor will be liable to Landlord for all of the outstanding consolidated CAM charge for the Calendar Year. If Assignor fails to pay the outstanding charge in full within thirty (30) calendar days after its receipt of the bill from Landlord, Assignee will pay the charge to Landlord in addition to its Minimum Rent. If Assignor has paid any monies in excess of the total consolidated CAM charge for the Calendar Year, Landlord will refund the excess to Assignor.

8. **Submission Fee.** Assignor will pay Landlord, contemporaneously with its submission of this Assignment, a non-refundable administrative fee in the amount of the Fee. Landlord's acceptance of the Fee will not impose a duty upon Landlord to consent to this Assignment. If the Fee is not submitted with this Assignment, the Fee will become due as Additional Rent under the Lease, payable upon demand. Assignor will also pay all reasonable legal fees incurred by Landlord with respect to the submission of this Assignment (the “Legal Fees”). If Landlord consents to this Assignment, the Fee and the Legal Fees will be the joint and several obligation of Assignor and Assignee.

9. **Consent and Joinder.** The effectiveness of this Assignment is conditioned upon the endorsement of the Consent by Landlord and the Joinder by Guarantor.

10. **Amendment of Lease.** Assignor authorizes Assignee to amend the Lease after the Date, at Assignee’s sole discretion and without notice to or consent of Assignor, and Assignor agrees that no such amendment will limit or alter Assignor’s liability under the Lease, as it may be amended from time to time; however, no such amendment will increase the amount of Rent for which Assignor is obligated under the Lease.

11. **Joint and Several Liability.** The liability of Assignor and Assignee under the Lease will be joint and several. If the term “Assignee” refers to more than one corporation, partnership, trust, association, individual, or other entity, their liability under this Assignment will be joint and several.

12. **Entire Agreement.** This Assignment embodies the entire agreement of Assignor and Assignee with respect to the subject matter of this Assignment, and it supersedes any prior agreements, whether written or oral, with respect to the subject matter of this Assignment. There are no agreements or understandings that are not set forth in this Assignment. This Assignment may be modified only by a written instrument duly executed by Assignor, Assignee, Guarantor and Landlord.

13. **Binding Effect.** The terms and provisions of this Assignment will inure to the benefit of, and will be binding upon, the successors, assigns, personal representatives, heirs, devisees, and legatees of Assignor and Assignee.

Assignor and Assignee have executed this Assignment on the respective dates set forth beneath their signatures below.

**ASSIGNOR:** [Signature]

**ASSIGNEE:** [Signature]

**CONSENT**

Landlord consents to the foregoing Assignment on the express conditions that

1. Assignor will remain liable for the performance of each and every one of its obligations under the Lease;

2. this Consent will not be deemed a consent to any subsequent assignment, but rather any subsequent assignment will be subject to the terms of the Lease and require
the consent of Landlord pursuant to the Lease;

(3) the Assignment will be subject to the Lease. Any provision of the Assignment that conflicts with, or purports to vary, any provision of the Lease will be of no effect despite Landlord's consent to the Assignment;

(4) Assignor agrees that the Lease may be modified and extended in any manner by Landlord and Assignee without the consent of Assignor, and that no such modification or extension will release Assignor from liability for the full performance and discharge of all of its obligations under the Lease (as so modified or extended);

(5) the consent will not be deemed to be a consent to alterations, to the installation of signs, to any change in the present manner of the operation of business conducted at the Premises, or to any other matter that may be referred to or contemplated by the Assignment; and

(6) the consent will not be deemed to be:

(a) an acknowledgement of the validity or accuracy of any recital, statement, representation or warranty contained in the Assignment, or

(b) a waiver of any uncollected or unbilled Rent that may be due or payable under the Lease.

**LANDLORD:**

By:
Name:
Title:
Date:

**GUARANTOR'S CONSENT**

Guarantor consents to the preceding Assignment and confirms that its Guaranty of Lease dated {{fill character="baseline-rule" width="7" }}, {{fill character="baseline-rule" width="7" }}, is in full force and effect as unmodified, and confirms and ratifies its Guaranty after Assignment of the Lease.

**GUARANTOR**

By:
Name:
Title:
Date:

This form simply transfers the lease to the assignee, and probably satisfies the landlord by adding the assignee's credit to the assignor's. The assignee's assumption will avoid any possibility that the assignee is bound only by those covenants that run with the land (and extinguished upon a subsequent assignment), because the assignee will have privity of contract with the landlord. This form does not provide for the release of the tenant/assignor from its liability under the lease.
Many tenants request such a release and landlords usually refuse to give it. As a compromise, the landlord may agree that the assignor/tenant will have no further liability under the lease if the assignee does not default for two years after the assignment; by then the landlord will know it has a “real” new tenant. To the contrary, this form makes it clear that the tenant/assignor will be bound by the lease even if it is amended. As a general rule, the tenant/assignor remains liable during any renewal or extension of the lease. 181 Although this form deals with the security deposit, many do not; when an assignment of two leases made no mention of security deposits, the Virginia Supreme Court ruled that the tenant was entitled to them because it remained liable under the lease. 182 However, a landlord may inadvertently release its tenant/assignor if (without the tenant/assignor’s consent) the landlord makes an agreement with the assignee that changes the terms of the lease in such a way as to increase the tenant/assignor's liability under the lease. 183

An assignor that is not released has lent its credit to the assignee; if the assignee defaults, the assignor must still pay rent. That “loan” is almost always unsecured. With a security interest in the lease, the assignor can take it back and reduce its losses following the assignee’s default. Of course, it will need notice of default from the landlord and a right to cure if it is to have any meaningful recourse. An assignor may require a collateral assignment (or re-assignment) of the lease as security for the assignee's indemnity in the assignment. A leasehold mortgage would have the same effect, and may be more appropriate under local law. Any security interest is itself probably subject to the assignment provisions, and requires the landlord's consent. 184 The assignor must be very careful that its self-protective measures, such as a reserved right of re-entry, do not create a risk of recharacterization of the assignment as a sublease, with resultant loss of privity between the landlord and the prospective assignee. A form of collateral assignment that might be included in an assignment (but that includes personal property) is:

FORM 13-16

ASSIGNMENT—COLLATERAL ASSIGNMENT

(a) If (i) Assignee fails to observe any of the covenants contained in this Assignment for a period of ten (10) days with respect to monetary obligations, and thirty (30) days with respect to non-monetary obligations, after written notice from Assignor; or (ii) an Event of Default under the terms of the Lease occurs, (either (i) or (ii), a “Default”), then Assignor may, but without any obligation, perform Assignee's obligations and covenants under the Lease. Assignor will have the right but not the obligation to repossess the Premises, together with the personal property, equipment, and fixtures located at the Premises (the “Leasehold Personal Property”) without further notice to Assignee, and to dispossess Assignee and any other assignees or subtenants, licensee, or party in possession from the Premises, and to exercise all other remedies available to Assignor at law or in equity. Assignee will be liable for any actual damages, costs, expenses and fees suffered by Assignor attributable to an Event of Default including without limitation, reasonable attorneys' fees and court costs.

(b) Assignee, as security for the payment, performance and observance of its obligations under this Assignment and the Lease (collectively, the “Obligations”), assigns to Assignor, and creates a security interest in all of Assignee's right, title and

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184 The Italian Fisherman, Inc. v. Middlemas, 545 A.2d (Md. 1988).
interest under the Lease. This Assignment is present, direct and continuing, and is made for the purpose of providing security to Assignor for the performance by Assignee of the Obligations. This Assignment will not in any way impair or diminish the obligations of Assignee under the provisions of this Assignment or the Lease, nor will any of the obligations of Assignee contained in this Assignment or the Lease be imposed upon Assignor. Upon the earlier to occur of Assignor's being released from liability under the Lease by Landlord or termination of the Lease and liabilities under it, this Assignment and all rights assigned to Assignor will automatically terminate and all the right, title and interest of Assignor in and to the Lease will revert to the Assignee.

(c) Assignee represents to Assignor that Assignee has not executed any other assignment of the Lease or sublease of the Premises. Assignee agrees that this Assignment is irrevocable and that Assignee will not take any action under the Lease or otherwise that is inconsistent with the Lease or this Assignment, and that any action inconsistent with this Assignment will be void. Assignee will, from time to time upon the request of Assignor, execute all instruments of further assurance and all such supplemental instruments with respect to this Assignment as the Assignor may reasonably request. The term “instruments” as used in this Assignment means all documents, certificates, waivers, consents, or other written agreements, understandings, or statements.

(d) To secure further Assignee's performance under the Lease and this Assignment, Assignee grants to Assignor a security interest in the property described in Exhibit {[fill character="baseline-rule" width="7"]} (the “Leasehold Personal Property”) and all other property affixed to or located upon the Premises, which will be deemed fixtures and a part of the Premises, and all articles of personal property and all materials delivered to the Premises for incorporation or use in any construction being conducted on the Premises and owned by Assignee. To the extent any property covered by this Assignment consists of rights in action or personal property covered by the Uniform Commercial Code, this Assignment constitutes a security agreement and financing statement, and is intended when recorded to create a perfected security interest in such property in favor of Assignor. This Assignment will be self-operative with respect to such property, but Assignee agrees to execute and deliver on demand such security agreements, financing statements, and other instruments as Assignor may request in order to impose the lien more specifically upon any of such property, and to pay all related recording and filing fees. For the purposes of treating this Assignment as a security agreement and financing statement, Assignor will be deemed to be the secured party and Assignee will be deemed to be the debtor. Assignee agrees that the security interest granted by Assignee pursuant to this Assignment will be a first and prior security interest in Assignee's interest in the Premises and the Leasehold Personal Property.

This form does not fully address the assignee's concerns. They include: assurance from the landlord in the nature of an estoppel certificate that the lease is in effect without default; comfort that its proposed use is allowed; and certainty that desirable options (such as renewal or expansions) are available to it. The assignee must always be sure that the obligations it is assuming are only those accruing after the assignment; otherwise, it may be burdened by the assignor's past duties. 185

185 But see Quebe v. Davis, 586 N.E.2d 914 (Ind. Ct. App. 1992), holding that an assignee is not liable for defaults before the assignment in the absence of a special undertaking.
The assignor's primary concern should be its liability if the assignee defaults. The assignor's nightmare is the assignee's bankruptcy and rejection of the lease as a result of which the assignor cannot regain control of the premises in order to mitigate its losses, and remains fully liable under the lease. However, unlike its posture in a sublease, the assignor has nothing but the assignee's indemnity (if that). The assignor may not even get a notice of default, and may first hear about the default when it is sued. At that point, of course, the assignor cannot cure the default or do anything other than defend itself in an indefensible position. Assignors should try to get notice and cure rights that extend beyond the assignee's notice and cure periods (if any). If the tenant is unable to negotiate its release at the time of the assignment, it may still be able to convince the landlord to release it if the assignee exercises a renewal or an expansion. If the assignee defaults, the tenant should consider whether it has surety defenses or the defenses that are discussed with regard to guarantees in §31.06, such as novation or other conduct that would release the assignor. 187 Statutory protection may come to the assignor's rescue. As a result of a New York law that requires the landlord to give a tenant notice that an automatic renewal is about to occur, an assignor that did not get the notice is not liable to the landlord after the assignee's default in the renewal term. 188

In reality, a landlord is interested in rent and not litigation. After an assignee's default, it should be inclined to work with the assignor in order to reduce both of their losses without litigation in which the landlord's conduct will be scrutinized by a judge sympathetic to the hapless tenant's inevitable claim that the landlord has not mitigated its damages.

§13.13 PREPARING A FORM OF SUBLEASE

A sublease is a lease created by the tenant within the boundaries of its lease with its landlord (the “prime lease,” “master lease,” or “head lease”). The tenant cannot sublease more space than it has, nor can it sublease the space that it does have for longer than its term (and any renewal terms). The sublease is an agreement between the tenant and the subtenant, and not between the landlord and the subtenant. Accordingly, the landlord and subtenant have no obligations to each other because, technically speaking, they are not in privity of contract, but only in privity of estate as discussed in §13.03[A] and [B]. Subleases are deceptively complicated documents. A lease represents the agreement of two people, while a sublease represents the agreement of three. Despite its complexity, the sublease is often believed to be an inexpensive, fast, and easy agreement. 189

When considering a sublease, the real estate professional's first task is to understand the prime lease, because it sets the limits on the sublease (and, perhaps, limits the tenant's right to create the sublease in the first place). A sublease of all of the premises for a day less than the balance of the term is much different from a sublease of a part of the premises for part of the

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186 Applying Virginia law in a case of first impression, a federal district court ruled that an assignor becomes a surety with the benefit of the surety's defenses that release the assignor-surety, such as an amendment to the lease made after the assignment. Corner Assocs. v. W. R. Grace & Co., 1997 WL 797582 (E.D. Va. 1997).
187 For a very useful discussion of contracts to purchase leaseholds, as opposed to the assignment itself, see Klein, How to Purchase a Leasehold (with Form), 8 Prac. Real Est. Law. at 75 (Mar. 1992).
189 For an invaluable analysis and checklist, see Herz & Wohl, Subleases: The Same Thing as Leases, Only Different, Real Prop., Prob. and Tr. J., Fall 2000, at 667. For a very helpful form, see Hollyfield, A Model Commercial Sublease Assignment, Prac. Real Est. Law. at 7 (July 2005).
term. The former is an assignment for all practical purposes, and the real estate professional should expect the subtenant to have greater rights and responsibilities than in the latter case of an “assignment” for part of the premises for part of the term. As an illustration, the real estate professional should consider the subtenant’s right to cure defaults by the tenant; obviously, in a sublease of a part of the premises for a part of the term, the subtenant’s ability and inclination to cure a default relating to all of the premises will be considerably less than it would be if the subtenant subleased all of the premises for the balance of the term less a day. Similarly, the subtenant cannot realistically expect the tenant to agree to renew the prime lease in order to extend the term of the sublease if the subtenant occupies only a part of the premises. In any discussion of subleases, the goals of the prime landlord, tenant, and subtenant are affected by the size of the subleased premises and the term of the sublease.

For its due diligence, the subtenant will review the prime lease to determine the obstacles to its sublease, and meet the landlord to determine its amenability to the transaction. The subtenant must look at each provision of the prime lease as though it were primarily bound by it because the subtenant, although not technically bound, cannot cause a default under the prime lease. The subtenant will want to assure itself of suitability of the premises for its use, determine the changes necessary to make them suitable, and get the landlord’s consent to the changes. Of course, it will want to assure itself that the lease is in effect, the tenant has not defaulted, and all necessary consents (including the landlord’s lender’s consent) are in place. Finally, the subtenant will want to assure itself that third party contracts on which it will depend are secure.

The landlord wants: an agreement with the subtenant that they will be bound to each other if the tenant defaults (and if the landlord believes the sublease is worth saving); the right to collect rent from the subtenant if the tenant fails to pay it; the confirmation of the continued liability of any guarantors of the lease; the right to enforce (and on demand get an assignment of) the tenant’s rights against the subtenant in the event of a default under the prime lease caused by the tenant; and indemnity from the subtenant and insurance to support it. The landlord does not want further subleases or assignments of the sublease to which it has consented, and it does not want the subtenant to have the benefit of personal concessions to the tenant such as a “cap” on expenses or renewal rates.

The tenant wants: a release (but is unlikely to get it); the subtenant’s compliance with the prime lease; indemnification against loss arising from default under the prime lease that is caused by the subtenant; exoneration from performance of duties under the prime lease that the tenant is not in a position to perform, such as the landlord’s violation of an exclusive right; the subtenant’s agreement to join amendments to the prime lease; copies of notices that the subtenant receives from the landlord so that the tenant can cure or prevent defaults under the prime lease; a right of re-entry or eviction so it can get a nonpaying subtenant out of the premises quickly without paying rent while it litigates with the tenant on a contract claim; a security deposit, and indemnity supported by insurance.

The subtenant wants: a recognition agreement from the landlord (in the nature of a subordination, nondisturbance and attornment agreement (SNDA), discussed in further detail in §13.14 and Chapter 25) providing notice and an opportunity for the subtenant to cure the tenant’s default under the prime lease, and recognition of the subtenant as the “tenant” on the terms of the prime lease if the tenant defaults; an agreement not to amend the prime lease without the subtenant’s consent; an SNDA from the landlord’s lender (which may be very difficult to obtain) in the event of the landlord’s default or bankruptcy; a promise by the tenant to comply with the prime lease; an indemnification by the tenant for its breach of the prime lease causing loss to the

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190 The ensuing discussion of due diligence is based upon Shaffer, Sublease Due Diligence, 17 Prob. & Prop., September/October 2003, p. 44, whose discussion and checklist are invaluable.
subtenant; the same rights against the tenant that the tenant has against the landlord, such as
setoff; the tenant's promise to exercise its option or extension rights if necessary to assure the
subtenant's rights under the sublease; the tenant's promise not to amend the prime lease; a
provision in which the subtenant agrees not to cause any breach of the prime lease in lieu of a
provision in which the subtenant assumes the obligations of the tenant under the prime lease and,
thus, becomes bound to the landlord by privity of contract.

Whom does the subtenant call if its lights do not go on or if it wants additional services, such
as an elevator on a weekend? This is a simple illustration of all the subtenant's concerns in a
sublease after it has assured itself of the sufficiency of the premises and the term. If the landlord
has an obligation to supply services to the tenant, and the subtenant has (at best) a right to those
services from the tenant who may not be in a position to provide them, and if the tenant has a cure
(and deduct) right for the landlord's default, the subtenant may have a similar right against the
tenant. Otherwise, the subtenant's best hope is an assignment of the tenant's rights against the
landlord on account of the landlord's breach, and a right to pursue those rights at the subtenant's
expense. If the subleased premises are a part of the larger premises that are affected by the
landlord's default, then the tenant and the subtenant will probably be pursuing the landlord
together, and the tenant may even agree to include the subtenant's claim as its own by an
assignment of its rights. The tenant and subtenant will allocate the cost of the action in proportion
to their share of the total premises. On the other hand, if the entire premises are covered by the
sublease, the subtenant may have negotiated an agreement from the landlord to provide services
to the subtenant. Since it is unlikely that the tenant can provide services, there is nothing that it
can do other than act as a conduit for what is provided to it from the landlord and as a claimant on
behalf of the subtenant for what is not provided. The complexities of subleases are further
suggested by these common issues:

1. Although the sublease rent would seem intuitively to be based on a percentage of the total
   premises, this is not necessarily true if the premises and the subleased premises have different
   views, amenities, or access.

2. Similarly, although parking would seem to be a simple proration, a telemarketing tenant that
   subleases part of its space for storage may not want to give up a proportionate share of its
   parking.

3. If the prime lease is long and the sublease is short, the subtenant's maintenance
   responsibilities should be less burdensome than the tenant's. Similarly, its insurance limits
   might be lower if it is just taking a portion of the premises. A mere incorporation of the
   requirements of the prime lease will not be fair to the subtenant.

4. A waiver of subrogation in the prime lease will not extend to the benefit of the subtenant so
   that the landlord's insurer could pursue subrogated rights against the subtenant unless a
   waiver of subrogation is obtained in the landlord's policy, and similarly the subtenant's
   insurer could pursue claims against the landlord without a waiver. These matters must be
   addressed in an agreement between the landlord and the subtenant.

5. If a portion of the premises is damaged but the subleased premises are not affected, the tenant
   may have a right to terminate the lease even though the subtenant has not been affected. Since
   the subtenant uses only a portion of the premises, it is not in a position to override the tenant's
   termination by an agreement to use the entire premises.

6. If the subtenant is required to remove its improvements in connection with the surrender of
   the premises, and the surrender occurs two days before the end of the term, what can the
   tenant do if the subtenant fails to remove them in the one day of the term remaining?

7. If the tenant has expansion or extension options, will the subtenant get the benefit of them,
and what can the subtenant do if the tenant refuses to exercise them?

8. If the subtenant is taking just a part of the premises and paying a share of operating expenses or CAM charges, should the tenant (sublandlord) charge an administrative fee in addition to its rent and pass through of those charges in order to compensate it for its time and trouble processing the subtenant's payment? If the landlord charges a management or administrative fee—why not the tenant?

9. The storage space (if any) should be adequate and accessible.

10. The subleased premises must have access for customers, but also for deliveries.

Despite the daunting obstacles (or, perhaps, because of them), real estate professionals produce poorly reasoned subleases with speed and ease. 191

A form of sublease is:

**FORM 13-17**

**ASSIGNMENT—SUBLEASE FORM**

THIS SUBLEASE is made on [[fill character="baseline-rule" width="7" ]], [[fill character="baseline-rule" width="7" ]], by [[fill character="baseline-rule" width="7" ]], ("Sublandlord"), whose address is [[fill character="baseline-rule" width="7" ]], and [[fill character="baseline-rule" width="7" ]] ("Subtenant"), whose address is [[fill character="baseline-rule" width="7" ]].

**RECITALS**

[[fill character="baseline-rule" width="7" ]]}, as landlord ("Landlord"), and Sublandlord, as Tenant, entered into a Lease dated [[fill character="baseline-rule" width="7" ]], [[fill character="baseline-rule" width="7" ]] (the "Prime Lease"), with regard to Suite [[fill character="baseline-rule" width="7" ]], [[fill character="baseline-rule" width="7" ]] Street, [[fill character="baseline-rule" width="7" ]], [[fill character="baseline-rule" width="7" ]] (the "Premises"). A copy of the Prime Lease is attached to this Sublease as Exhibit A. Sublandlord wishes to sublease to Subtenant, and Subtenant wishes to sublease from Sublandlord, a portion of the premises known as Suite [[fill character="baseline-rule" width="7" ]], [[fill character="baseline-rule" width="7" ]] Street, [[fill character="baseline-rule" width="7" ]], [[fill character="baseline-rule" width="7" ]] (the "SUBLEASED PREMISES").

The SUBLEASED PREMISES are depicted on Exhibit B to this Sublease. Accordingly, Sublandlord and Subtenant agree:

1. **Agreement.** Sublandlord subleases the SUBLEASED PREMISES to Subtenant, and Subtenant subleases the SUBLEASED PREMISES from Sublandlord, according to this Sublease. The provisions of the Prime Lease (except paragraphs [[fill character="baseline-rule" width="7" ]], [[fill character="baseline-rule" width="7" ]], and [[fill character="baseline-rule" width="7" ]]) are incorporated into this Sublease as the agreement of Sublandlord and Subtenant as though Sublandlord was landlord under the Prime Lease and Subtenant was tenant under the Prime Lease.

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191 See Neufeld, *Leasing or Subleasing?*, Real Est. Fin. J. at 73 (Summer 2003), for some of the benefits (such as below market rent) and problems (such as the subtenant's alterations) in subleases.
2. **Term.** The Term of this Sublease will begin on {{fill character="baseline-rule" width="7" }}, {{fill character="baseline-rule" width="7" }}, and will end on {{fill character="baseline-rule" width="7" }}, {{fill character="baseline-rule" width="7" }}, inclusive. If Sublandlord is unable to deliver possession of the Subleased Premises to Subtenant because the present occupant of the Subleased Premises fails to vacate them on or before {{fill character="baseline-rule" width="7" }}, {{fill character="baseline-rule" width="7" }}, then Subtenant's right to occupy, and obligation to pay for, the Subleased Premises will be delayed until Sublandlord delivers possession of the Subleased Premises. The deferral of Subtenant's obligation to pay such rent will be full satisfaction of all claims that Subtenant may have as a result of such delayed delivery of possession.

3. **Rent.** Subtenant will pay Sublandlord as Rent for the Subleased Premises $[amount] per month, in advance, without notice, demand, offset, or counterclaim, on the first day of each month. Rent will be paid at Sublandlord's address. If the Term of this Sublease begins on other than the first day of a month or ends on other than the last day of a month, Rent will be prorated on a per diem basis.

4. **Acceptance of the Premises.** Subtenant accepts the Subleased Premises in their present condition. Sublandlord will not be obligated to make any alterations or improvements to the Subleased Premises on account of this Sublease.

5. **Security Deposit.** Subtenant has deposited with Sublandlord the sum of {{fill character="baseline-rule" width="7" }$[fill character="baseline-rule" width="7" ]} Dollars ($[fill character="baseline-rule" width="7" ]}) that Sublandlord will hold in accordance with paragraph {{fill character="baseline-rule" width="7" }} of the Prime Lease.

6. **Other Charges.** During the Term of this Sublease, Subtenant will pay to Sublandlord {{fill character="baseline-rule" width="7" }%} any increase in Sublandlord's rent pursuant to paragraphs {{fill character="baseline-rule" width="7" }} and {{fill character="baseline-rule" width="7" }} of the Prime Lease. Such payments will be made as and when due under the Prime Lease.

7. **Parking.** Sublandlord agrees that, during the Term of this Sublease, Subtenant will be entitled to use {{fill character="baseline-rule" width="7" }} ({{fill character="baseline-rule" width="7" }}) of the parking spaces in the parking garage allocated by Landlord to Sublandlord pursuant to the Prime Lease. Subtenant will pay the monthly rate for such space as the same is adjusted from time to time.

8. **Services.** Sublandlord will not be obligated to provide any services to Subtenant. Subtenant's sole source of such services is Landlord, pursuant to the Prime Lease. Sublandlord makes no representation about the availability or adequacy of such services.

9. **The Master Lease.** This Sublease is subject to the Prime Lease. The provisions of the Prime Lease are applicable to this Sublease as though Landlord under the Prime Lease were the Sublandlord under this Sublease and Tenant under the Prime Lease were Subtenant under this Sublease. Subtenant has received a copy of the Prime Lease. Subtenant will indemnify Sublandlord against any loss, liability, and expenses (including reasonable attorneys' fees and costs) arising out of any default under the Prime Lease caused by Subtenant, and Sublandlord will indemnify Subtenant against any loss, liability, and expenses (including reasonable attorneys' fees and costs) arising out of any default under the Prime Lease caused by Sublandlord.
Sublandlord and Subtenant have executed this Sublease on the date first written above.

SUBLANDLORD:
By:
Name:
Title:
Date:

SUBTENANT:
By:
Name:
Title:
Date:

CONSENT TO SUBLEASE

Landlord consents to the subletting by Sublandlord to Subtenant, pursuant to a Sublease dated as of [fill character="baseline-rule" width="7" ]}, {[fill character="baseline-rule" width="7" ]} (the “Sublease”), a copy of which is attached as Exhibit A, of all or a portion of the Premises as shown and marked on the floor plan attached to the Sublease (the “Sublet Space”):

1. Nothing contained in this Consent will:
   (a) operate as a representation or warranty by Landlord, and Landlord will not be bound or estopped in any way by the provisions of the Sublease, or
   (b) be construed to modify, waive or affect (i) any of the provisions, covenants or conditions in the Prime Lease, (ii) any of Sublandlord’s obligations under the Prime Lease, or (iii) any rights or remedies of Landlord under the Prime Lease, or otherwise or to enlarge or increase Landlord’s obligations or Sublandlord’s rights under the Prime Lease, or
   (c) be construed to waive any present or future breach or default on the part of Sublandlord’s under the Prime Lease. In case of any conflict between the provisions of this Consent and the provisions of the Sublease, the provisions of this Consent will control.

2. This Consent is not assignable and is personal to Subtenant.

3. The Sublease will be subject to subordinate at all times to the Prime Lease and all of its provisions, covenants and conditions.

4. Neither the Sublease nor this Consent will release or discharge Sublandlord from any liability under the Prime Lease and Sublandlord will remain liable and responsible for the full performance and observance of all of the provisions, covenants and conditions set forth in the Prime Lease on the part of the Sublandlord to be performed and observed. Any breach or violation of any provisions of the Prime Lease by Subtenant will be a default by Sublandlord.

5. This Consent will not be construed as a consent to any further subletting or assignment of any interest in the Lease or Sublease either by Sublandlord or
Subtenant. The Sublease may not be assigned, renewed or extended nor will the Premises or Sublet Space, or any part of it, be further sublet without prior written consent of Landlord in each instance.

6. Upon the expiration or any earlier termination of the Prime Lease, or in case of the surrender of the Prime Lease by Sublandlord to Landlord, the Sublease will end as of the effective date of such expiration, termination, or surrender and Subtenant will vacate the Sublet Space on or before that date. If the Prime Lease expires or terminates during the term of the Sublease for any reason other than condemnation or destruction by fire or other cause, or if Sublandlord surrenders the Prime Lease to Landlord during the term of the Sublease, Landlord, in its sole discretion (upon written notice given to Sublandlord and Subtenant within thirty [30] days after the effective date of such expiration, termination or surrender and without any additional further agreement of any kind on the part of the Subtenant), may elect to continue the Sublease with the same force and effect as if Landlord and Subtenant had entered into a lease as of such effective date for a term equal to the then unexpired term of the Sublease and containing the same terms and conditions as those in the Sublease. In that event, Subtenant will attorn to Landlord and Landlord and Subtenant will have the same rights, obligations and remedies as were had by Sublandlord and Subtenant prior to such effective date, respectively, except that in no event will Landlord be (a) liable for any act or omission by Sublandlord, (b) subject to any offsets or defenses which Subtenant had or might have against Sublandlord, (c) bound by any rent or additional rent or other payment paid by Subtenant to Sublandlord in advance, or (d) bound by any amendment to the Sublease not consented to by Landlord. If Subtenant does not vacate the Sublet Space upon expiration of the Sublease pursuant to the provisions of the first sentence of this Section, Landlord will be entitled to all the rights and remedies available to a landlord against a Sublandlord holding over after the expiration of a term.

7. Tenant's obligation to indemnify and hold Landlord harmless as set forth in the Lease includes indemnification from any claims arising from the use of the Premises (as defined in the Lease), or any portion thereof, by Subtenant, its agents, employees or contractors.

8. Both Sublandlord and Subtenant will be and continue to be liable for all bills rendered by Landlord for charges incurred by or imposed upon Subtenant for services rendered and materials supplied to the Sublet Space. If a separate submeter is installed to measure electric current furnished to the Sublet Space, then payment for the current so furnished will be made by Subtenant directly to Landlord as and when billed and the furnishing of such current will be in accordance with and subject to all of the applicable terms, covenants and conditions of the Prime Lease.

9. Sublandlord authorizes Landlord to furnish services requested by Subtenant and to charge Subtenant directly for such services without notice to Sublandlord.

10. Landlord and Subtenant waive on behalf of any insurer providing insurance to it, any right of subrogation which such insurer might otherwise acquire against the other or its shareholders, officers, directors, partners, members, managers or employees by virtue of losses to Landlord or Subtenant. Landlord and Subtenant waive any and every claim that arises or may arise in its favor against the other and the other's shareholders, partners, officers, and employees during the Term for any and all loss of or damage to any property, located within or upon or constituting a part of, the
Premises or the Building, which loss or damage is caused by a peril required by this Lease to be covered by the insurance of the party incurring the loss or, if greater, to the extent of the actual recovery under any insurance policy covering the party incurring the loss.

11. As further security for Tenant's performance of its obligations under the Lease, Tenant assigns to Landlord Tenant's interest in all rent from the Sublease;

(a) until an Event of Default occurs in the performance of Tenant's obligations under the Lease, Tenant may receive the rent from the Sublease. However, if an Event of Default occurs, then Landlord may, at its option, collect directly from Subtenant all rent owing and to be owed under the Sublease. Landlord will not, by reason of this assignment of the rent from the Sublease nor by reason of the collection of the rent under the Sublease, be deemed liable to Subtenant for any failure of Tenant to perform its obligations under the Sublease;

(b) Tenant irrevocably authorizes and directs Subtenant, upon receipt of any written notice from the Landlord stating that an Event of Default has occurred under the Lease, to pay to Landlord the rent due and to become due under the Sublease. Tenant agrees that Subtenant will have the right to rely upon any such statement and request from Landlord, and that Subtenant will pay such rent to Landlord without any obligation or rights to inquire as to whether such Event of Default exists. Tenant will have no right or claim against Subtenant for any such rent so paid by Subtenant.

12. Any notice or communication with respect to this Consent will be given by prepaid certified mail, return receipt requested, addressed to such other party, in the case of Landlord at its address in the Prime Lease, and in the case of Sublandlord or Subtenant at the Premises, or in any case at such other address as such other party may designate by notice given in accordance with provisions of this Section. Any such notice or communication will be deemed to have been given at the time it is mailed.

13. This Consent will be construed in accordance with the laws of the State of [fill character="baseline-rule" width="7"]], contains the entire agreement of the parties with respect to its subject matter, and may not be changed or terminated orally or by course of conduct.

LANDLORD:

By:
Name:
Title:
Date:

TENANT:

By:
Name:
Title:
Although no particular form is necessary for the sublease, the tenant cannot create greater
erights for its subtenant than it has under the prime lease; for example, the tenant cannot grant a
renewal option that would extend the term of the sublease beyond the term of the prime lease. In
order to avoid any inconsistencies, many tenants use the prime lease as the form of the sublease.
In this approach the prime lease is carefully reviewed and the rights and obligations are allocated
appropriately to the tenant-sublandlord and subtenant. However, a long document can result.
Other tenants incorporate the terms of the prime lease by reference, saying in effect that
“Landlord means Sublandlord [that is, the tenant] and Tenant means Subtenant.” The
incorporation of the master lease will result in several awkward or inappropriate provisions in the
sublease. The landlord’s rights to terminate the lease after damage or condemnation should not
be available to the tenant-sublandlord, and the landlord’s duties in those events cannot practically
be performed by the tenant-sublandlord. The limitation of tenant’s recourse to the landlord’s
interest in the building must be reconsidered; perhaps the subtenant’s claims are limited to the
tenant’s leasehold, but this gives the subtenant no practical recourse since the lease—if lost—is
worthless. The tenant-sublandlord cannot give a broad covenant of quiet enjoyment and cannot be
liable for a failure of landlord’s title. If the tenant needs the subtenant’s rent to pay its own rent
(and other charges such as pass-throughs or parking charges), then it will want the subrent paid
several days before the rent is due. The tenant may not be able to do the repair and maintenance
for the subtenant that the landlord is obligated to do for the tenant (because the tenant has no
access to the necessary areas of the building). The waiver of subrogation should be examined to
be certain that the subtenant has its benefit. Finally, so long as care is taken not to go outside the
bounds of the prime lease, an entirely new lease can be used with little or no reference to the
prime lease; this is true of subleases on ground leased land.

In a New York case, the sublease made reference to the master lease, incorporated it, and
subjected the sublease to it. The subtenant objected to the payment of its share of “pass-through”
costs that the tenant/sublandlord paid pursuant to the master lease. The tenant prevailed with the
assistance of some judicial prestidigitation. The landlord’s problem could have been avoided
by a specific statement of the tenant’s responsibility for those costs.

Many subleases state that the termination of the prime lease will terminate the sublease.
Certainly, this is true; however, such a provision may excuse the sublandlord that caused the
termination of the prime lease (by defaulting in its rent payment to the landlord, for example).

No. 1, 1 (Spring 1999) and their follow-up article “Subleases: A New Approach Revisited,” Real
Prop., Prob. & Tr. J., Spring 2006, at 1, updating their early sublease form. Goldberg, Preparing
the Sublease, N.Y. St. B.J. at 25 (Dec. 1986). This article is required reading for real estate
professionals involved in subleases.

193 NPS Engineers & Constructors, Inc. v. Underweiser & Underweiser, 73 N.Y.2d 996, 541
The subtenant should not accept any such exculpation for liability caused by the sublandlord's own default. A tenant is liable to its subtenant if the tenant's duties under the sublease are breached by the landlord's exercise of its rights under the master lease, because the subtenant has no reason to know what the master lease provides. A defaulting subtenant whose sublandlord surrenders the prime lease in order to mitigate its damages from the subtenant's breach is liable for rent accruing after the surrender in excess of amounts saved on the prime lease. The surrender of the lease by the tenant can have one of two results. If the surrender is voluntary, the subtenant becomes a direct tenant of the landlord just as though the sublease had been assigned to the landlord. However, if the surrender is involuntary, then the sublease is terminated just as though the tenant had been evicted. A surrender is considered "voluntary" when there is no clear legal basis for termination by the landlord.

Once the sublandlord has created a sublease that gives the subtenant no greater rights than the prime lease gives the tenant/sublandlord, the sublandlord is legally protected. Practically, however, one obstacle must be overcome. What happens if the landlord breaches one of its obligations to the tenant/sublandlord, thus preventing the tenant/sublandlord's performance? This is a dilemma about which sublandlords and subtenants can argue endlessly. The sublandlord explains that it is giving the subtenant what it has, but that it cannot be responsible for its landlord's breaches. The subtenant contends that it has no relationship with the landlord, that it is paying the tenant/sublandlord, and that it expects performance from the tenant/sublandlord. In fact, however, the tenant has no ability to cure many of its landlord's defaults, such as failure to provide utilities or elevator service. In those circumstances, the tenant and subtenant may agree that the subtenant will have the tenant's rights against the landlord and that, if the tenant's rent is abated, the subtenant's rent will be proportionately abated.

Because a subtenant has no relationship with the landlord, it may ask for a sublandlord's efforts to act on its behalf in matters that the landlord controls:

**FORM 13-18**

**ASSIGNMENT—TENANT TO ACT AS SUBLANDLORD IN MATTERS WITH SUBTENANT**

Sublandlord will use reasonable efforts to cooperate with Subtenant in (a) obtaining on Subtenant's behalf (i) additional services requested by Subtenant pursuant to the Lease and this Sublease, (ii) any benefit to Sublandlord relating to the Subleased Premises under the Lease that would directly benefit Sublandlord relating to the Subleased Premises under the Lease that would directly benefit Subtenant, including, without limitation, any dispute rights regarding Operating Expenses in the Lease, and (iii) Landlord's consent for any action under the Lease for which Subtenant must obtain Landlord's consent, and (b) delivering any notice to Landlord as required by any provision of the Lease, including, without limitation, promptly forwarding any request made by Subtenant to Landlord for services, its consent, or approval, and providing Landlord with all information required with respect to such request or that Landlord may

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reasonably request. Sublandlord agrees that if Landlord consents to any matter that requires Landlord's consent under the Lease, such consent will be deemed given by Sublandlord under this Sublease, except for approvals and consents relating to alterations (other than items for which neither Landlord's nor Sublandlord's consent is required), as to which, if granted by Landlord, Sublandlord agrees that it will not unreasonably withhold or delay its consent or approval.

The tenant/sublandlord and subtenant must still resolve all the questions attendant upon their sharing the premises, the common areas serving the premises, the means of access, and the services to the premises.

Finally, when notice provisions are repeated verbatim or incorporated by reference, there is a risk that the tenant who receives a notice on the last day of a notice period will be unable to pass on the notice in a timely fashion. For example, consider a damage provision that enables the landlord to keep the lease in effect by giving notice within 60 days after the occurrence of its election to repair the damage. If no notice is given, the provision continues, the tenant may cancel the lease. If the landlord gives its tenant a notice on the 60th day, the tenant may be unable to give its subtenant the same notice on the same day; as a result, the subtenant may cancel the sublease while the tenant remains bound by the lease. Consequently, notice periods under the sublease should be extended to enable the tenant to receive notice from the landlord and give notice to the subtenant. Subtenants will, however, insist upon sufficient advance notice to cure their sublandlord's defaults.

The Consent to Sublease that is appended to Form 13-17 can be augmented in several ways:

1. If the master lease calls for profit sharing, the sublandlord and subtenant may be asked to represent that there is no consideration being paid that is subject to the profit sharing provision.

2. The sublandlord may give its advance consent to the landlord's provision of services (such as after hours HVAC) to the subtenant that sublandlord gets under the master lease. Of course, the sublandlord will be liable for payment if the subtenant fails to pay for them.

3. The rights of the master landlord to the subtenant's rents in the event of default by the tenant can be set forth at great length as they would be in a lender's assignment of rents. The need for such a provision will depend upon the importance of the subtenant to the landlord's rent stream.

§13.14 RECOGNITION AGREEMENT (FOR A SUBLEASE)

The real estate professional will recognize a structural similarity between the relationship of first lender, landlord, and tenant (which is more fully discussed in Chapter 25), and the relationship of prime landlord, tenant, and subtenant. A foreclosure by the first lender or lease termination by the prime landlord affects the tenant or subtenant, as the case may be. In both of these situations, a three-party agreement is appropriate because it creates a direct relationship between the first lender or prime landlord and the tenant or subtenant, and assures the tenant or subtenant that its occupancy may continue even though the rights of its landlord or sublandlord

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197 See Croudace, Negotiated Form of Landlord's Consent To Sublease (With Annotations), Prac. Real Est. Law. at 45 (Jan. 2010).
198 Friedman §7.704b, contains a lengthy discussion of the need for these agreements.
have ended.

A knowledgeable commentator has aptly observed that a tenant with the bargaining power to do so is well advised to negotiate in the lease the terms on which a landlord will make such an agreement with a future subtenant. 199 These discussions are difficult because the landlord is being asked to accept an unknown subtenant as its own tenant in the event the original tenant and its credit no longer support the lease. A form for an “advance” agreement (which binds the landlord to the sublease rents even though they may be less than the lease rate) may be:

If Tenant subleases part or all of the Premises (the “Sublet Premises”) pursuant to its rights under this Lease, and thereafter, the Lease or Tenant's right to possession terminates for any reason prior to expiration of the sublease, Landlord will accept attornment at the election of either Landlord or the subtenant (“Subtenant”), upon the terms and conditions of the Sublease for the remainder of the term of the Sublease. In the event of any such election by Landlord or Subtenant, Landlord will not be (a) liable for any rent paid by Subtenant to Tenant more than one month in advance, or any security deposit paid by Subtenant to Tenant, unless it has been transferred to Landlord by Tenant; (b) liable for any act or omission of Tenant under the Lease, Sublease, or any other agreement between Tenant and Subtenant, or for any default of Tenant under any of those documents that occurred prior to the effective date of the attornment; (c) subject to any defenses or offsets that Subtenant may have against Tenant that arose prior to the effective date of the attornment, or (d) bound by any changes or modifications made to the Sublease without the written consent of Landlord. If neither Landlord nor Subtenant so elects to have Subtenant attorn to Landlord, the Sublease and all rights of Subtenant in the Sublet Premises will terminate upon the date of termination of the Lease or Sublandlord's right to possession. The terms of this Section will only apply if the Sublet Premises is all of the Premises or a separately demised portion of the Premises, and will supersede any contrary provisions in the Sublease.

An appropriate three-party agreement for the sublease may be:

FORM 13-19

RECOGNITION AGREEMENT

THIS AGREEMENT is made as of [fill character="baseline-rule" width="7" ], 19[fill character="baseline-rule" width="7" ], between [fill character="baseline-rule" width="7" ], a [fill character="baseline-rule" width="7" ] limited partnership, whose address is [fill character="baseline-rule" width="7" ] (“Prime Landlord”), and [fill character="baseline-rule" width="7" ] corporation, having its principal office at [fill character="baseline-rule" width="7" ] (“Subtenant”).

RECITALS

Prime Landlord is the owner of premises in the City of [fill character="baseline-rule" width="7" ], County of [fill character="baseline-rule" width="7" ], and State of [fill character="baseline-rule" width="7" ] in the shopping center known as [fill character="baseline-rule" width="7" ] Shopping Center (the “Center”). Prime Landlord has leased the premises to [fill character="baseline-rule" width="7" ] corporation, as tenant (“Sublandlord”) pursuant to a Lease Agreement dated [fill character="baseline-rule" width="7" ], 19[fill character="baseline-rule" width="7" ], as amended by First Amendment to Lease Agreement dated [fill character="baseline-rule" width="7" ], 19[fill character="baseline-rule" width="7" ] and Second Amendment to Lease Agreement dated [fill character="baseline-rule" width="7" ]

Sublandlord has subleased the premises subject to the Underlying Lease to a corporation ("Subtenant"), pursuant to a Sublease dated [fill character="baseline-rule" width="7" ] (the “Sublease”). Subtenant and Prime Landlord wish to provide for certain events affecting the Underlying Lease.

Accordingly, they agree:

1. Consent. Prime Landlord consents to the execution and delivery of the Sublease in the form annexed as Exhibit A.

2. Nondisturbance.
   
   (a) If the current term of the Underlying Lease, or any extension or renewal of it, ends before the expiration of the term of the Sublease, or any extension or renewal of it, for any reason other than condemnation, fire, or other casualty, the Sublease, if then in existence, will continue as a lease between Prime Landlord, as landlord, and Subtenant, as tenant, with the same force and effect as if Prime Landlord, as landlord, and Subtenant, as tenant, had entered into a lease as of the end of the Underlying Lease, containing the same terms, covenants, and conditions as those contained in the Sublease for a term equal to the unexpired term of the Sublease.

   (b) The provisions of this paragraph 2 will inure to the benefit of only Subtenant and will not pass to any successor or assignee of Subtenant or any other party unless the liability of Subtenant survives the assignment.

3. Attornment. From and after the end of the Underlying Lease:
   
   (a) Subtenant will attorn to Prime Landlord, and Prime Landlord will accept the attornment.

   (b) Prime Landlord will have the same remedies against Subtenant for the nonperformance of any agreement contained in the Sublease for the recovery of rent, for the commission of any waste, or for any other default which Sublandlord had or would have had if the Underlying Lease had not ended.

   (c) From and after the time of such attornment, Subtenant will have the same remedies against Prime Landlord for the breach of any agreement contained in the Sublease that Subtenant might have had against Sublandlord if the Underlying Lease had not ended.

   (d) Prime Landlord will adopt the Sublease between Sublandlord and Subtenant as and for its lease; and will be deemed the landlord and Subtenant its tenant under the lease; and will assume each and every covenant, condition, and agreement in the lease and required to be kept, observed, and performed by Sublandlord, with the same force and effect as if Prime Landlord had originally been named as the landlord of Subtenant, so that Prime Landlord will be substituted as the landlord in the Sublease.

   (e) Upon any adoption by Prime Landlord of the Sublease, Subtenant will pay the rent required to be paid by it under the Sublease directly to Prime Landlord, and Prime Landlord will accept the rent. Subtenant will comply with every other term, covenant, condition, and agreement of the Sublease.
4. **No Modifications.** Neither Subtenant nor its successors or assigns will enter into any agreement which modifies, surrenders, or merges the Sublease without the prior consent of Prime Landlord, and an agreement made in contravention of the provisions of this paragraph will not affect the Prime Landlord.

5. **Sale of the Premises.** The term “Prime Landlord” as used in this Agreement means only the owner of the premises for so long as it owns them, so that in the event of any sale or other transfer of an interest in the premises, Prime Landlord will be relieved of all covenants and obligations of Prime Landlord in this Agreement. The provisions of this Agreement, however, will bind any subsequent owner of the premises.

6. **Notices.** Any notice or demand pursuant to this Agreement must be in writing and be given or made by registered or certified mail, return receipt requested, and will be deemed to have been given when sent; notices by Subtenant to Prime Landlord will be addressed to Prime Landlord at the address first set forth; and notices given by Prime Landlord to Subtenant will be addressed to:

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   {[fill character="baseline-rule" width="7"]}
   {[fill character="baseline-rule" width="7"]}
   {[fill character="baseline-rule" width="7"]}
   with copy to: {[fill character="baseline-rule" width="7"]}
   {[fill character="baseline-rule" width="7"]}
   {[fill character="baseline-rule" width="7"]}
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Prime Landlord or Subtenant may change its address for the service of notices by giving to the other prior written notice of such change of address.

7. **Binding Effect.** This Agreement will be binding upon, and will inure to the benefit of, Prime Landlord and Subtenant, and (subject to paragraph 2(b) as to Subtenant) their respective successors and, and any purchaser, assignee, or transferee of the Sublease, and any subtenant under it.

Prime Landlord and Subtenant have duly executed this Agreement as of the day and year first above written.

PRIME LANDLORD:

By: {[fill character="baseline-rule" width="7"]}
A simple agreement like a recognition agreement can have unexpected results. In a Georgia case, the landlord and subtenant had an agreement that continued the subtenant's rights under the terms of the master lease if the tenant defaulted. After the tenant defaulted and the landlord and erstwhile subtenant performed pursuant to the lease, the subtenant exercised a renewal option in the lease, and the landlord objected that the renewal option was not incorporated into their direct agreement. The court disagreed because the tenant had the right to occupy under the terms set forth in the sublease that included the renewal right.  

The largest issue in the recognition agreement is the reality that subleases almost always provide for lower rent from the subtenant than the tenant/sublandlord pays under the prime lease, because the tenant/sublandlord is ridding itself of space it does not need and hoping to cut its costs—and, of course, competing with more desirable direct leases. Landlords do not like the prospect of less rent if they recognize the subtenant. Accordingly, some recognition agreements provide that the landlord can elect to recognize the subtenant on the terms of the sublease or on the terms of the prime lease, but the subtenant can elect to terminate if the landlord elects the prime lease. This compels the landlord and subtenant to discuss the matter because the landlord faces the re-rental cost and delay, and the subtenant risks the market rate rent plus inconvenience of moving.

When a landlord agrees to recognize a tenant after a foreclosure at the tenant's request, the tenant should make the request before the lease is terminated by the foreclosure.  

§13.15 LENDERS' CONCERNS ABOUT ASSIGNMENTS AND SUBLEASES

The lenders' concerns about assignments and subleases are that:

201Bain v. Pioneer Plaza Shopping Ctr. Ltd. Liab. Corp., 894 P.2d 47 (Colo. Ct. App. 1995). There, the master landlord (whose position is analogous to a lender's) agreed to recognize a subtenant at the subtenant's request. However, the subtenant did not make the request until the master lease had been terminated, and the court held that the request was too late.
1. The original creditworthiness of the lease remains so that the original tenant should not be released when an assignment occurs.

2. The new tenant's creditworthiness should be proven.

3. The new tenant should assume the tenant's obligation under the lease.

4. The assignment should not result in a default under existing exclusive use provisions.

5. No major tenant should have a right to assign during any period in which the shopping center is initially leasing up with smaller tenants.

§13.16 RELATED PROVISIONS

The assignment provisions touch upon almost all of the other provisions of the lease, including expansion and extension rights (§4.18[D] and §5.11); relocation (§4.19); use (Chapter 11); operating covenants (§11.05[A] through §11.05[D]); signage (Chapter 14), and alterations (§20.03).
PROFESSIONAL EDUCATION BROADCAST NETWORK

Speaker Contact Information

DRAFTING SUBLEASES & ASSIGNMENTS IN COMMERCIAL REAL ESTATE, PART 1 & PART 2

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