

Select Issues In Terminating Commercial Leases

**Submitted by A. McCampbell Gibson, Samuel R. Rutherford
and Mike H. Shanlever**

- Termination Of Lease By Landlord V. Voluntary Surrender By Tenant
- Abandonment Calamities: The Tenant Has Moved Out – What About The Property Left Behind?
- Self-Help Considerations
- Who's To Clean Up The Toxic Waste Left By The Tenants?
- Bankruptcy Considerations For The Landlord/Tenant Relationship

SELECT ISSUES IN TERMINATING COMMERCIAL LEASES

by

A. McCampbell Gibson,^{*}
Samuel R. Rutherford,^{}**
and
Mike H. Shanlever^{*}**

For a variety of reasons commercial landlords and tenants often seek a premature end to leases. Reasons include financial interests, successor interests, changed circumstances, and simple hindsight.

This section explores issues practitioners should consider when faced with a client who seeks to prematurely end a lease. Potential exposure awaits landlords and tenants in connection with abandoned tenant property, vacant commercial space, waste issues, evictions, and other pitfalls.

I. Termination of Lease by Landlord v. Voluntary Surrender by Tenant

Lease terms are almost always determined by the language of the lease itself. However, leases may provide a lessor with early termination rights upon the happening of certain events. The most common examples are the right to terminate in the event a tenant fails to pay rent, or violating an express prohibition in the lease. In either case, the landlord should take special care to provide the requisite notice to terminate the lease, and to demand possession.

* Mac Gibson is a partner in the Atlanta office of Alston & Bird LLP, where he chairs the firm's Real Estate Litigation Team. He focuses his practice on real estate disputes, including lease enforcement, easement, restrictive covenant, trespass and nuisance claims, brokerage disputes, zoning, premises liability, and eminent domain matters.

** Sam Rutherford is a commercial litigation associate in Alston & Bird LLP's Atlanta office and a member of the firm's Real Estate Litigation Team.

*** Mike Shanlever is a commercial litigation associate in Alston & Bird LLP's Atlanta office and a member of the firm's Real Estate Litigation Team.

Pursuant to O.C.G.A. §§ 44-7-10, when a lease expires by its terms, the lease is automatically terminated without the necessity of notice. However, if the tenant defaults in any way, the landlord must serve timely notice of default, followed by a notice of actual termination, and finally a demand for possession as part of its dispossessory effort. If the landlord fails to follow these steps, a tenant in default may potentially defend its continued possession of the premises. In Wig Fashions, Inc. v. A-T-O Properties, 145 Ga. App. 325, 326 (1978), a landlord sent its tenant four notices of default, stating that a failure to cure within ten days “would result in termination.” The Court of Appeals held that a subsequent dispossessory was unlawful because the letters “did not serve to terminate the lease...but at most could be read to evidence an intent that the lease be terminated at the expiration of ten days,” and therefore the subsequent demand for possession was premature and ineffective. *Id.*; see also Whipper v. Kirk, 156 Ga. App. 218, 221 (1980) (landlord’s notice of default and demand for possession in the same letter failed to initiate a lawful dispossessory because the demand must follow actual termination).

Similarly, tenants should always document in writing any agreement allowing the tenant to surrender leased premises before the lease expires. In Aycock v. Copeland Motor Co., 86 Ga. App. 765 (1952), a landlord agreed to pay its tenant \$500 to surrender premises a year early, so the tenant stopped paying rent and left the premises. The landlord never paid the tenant \$500 as agreed upon, and months later sued the tenant for back-rent. *Id.* The Court of Appeals held that the agreement was merely executory, and by never paying the \$500, the tenant remained obligated under the lease. The long-standing rule of Lamb v. Gorman, 16 Ga. App. 663 (1915) remains best-practice:

[To] complete the evidence of surrender, there must be evidence of something more than an inability on the part of the landlord to compel the tenant to remain in possession. There must be either possession on the part of the tenant, or such circumstances as compel the conclusion that the landlord consented to retake possession of his property.

II. Abandonment Calamities: the Tenant has Moved Out – What About the Property Left Behind?

When a tenant is no longer in possession of leased premises – due to either abandonment, surrender, or the end of the lease term – parties should carefully consider what rights they have relative to property that remains in the lease premises. Ideally, the written lease will address all possible issues; however, leases often fail to contemplate unique factual circumstances.

The clearest case occurs upon expiration of the lease. Pursuant to O.C.G.A. § 44-7-12, “[a]fter the [lease term has] ended, any trade fixtures remaining will be regarded as abandoned for the use of the landlord and will become the landlord's property.” In Chouinard v. Leah Enterprises, Inc., 205 Ga. App. 206, 207 (1992), a tenant refused to vacate upon the expiration of its lease, forcing the landlord to initiate dispossessory proceedings. During the proceedings the tenant continued to pay the landlord rent; however, once the landlord obtained the writ of dispossessory, he locked the tenant out and refused to allow the tenant to remove his trade fixtures. Id. A jury awarded the tenant \$6,140 compensatory damages and \$25,000 punitive damages on its conversion claim. Id. The Court of Appeals reversed, holding that even though the landlord continued to accept rent during the pendency of the dispossessory proceeding, “the tenant had no right to remove its trade fixtures in this case once its rightful possession of the premises ended.” Id. at 208.

When a tenant arguably abandons premises prior to the expiration of a lease, the landlord’s rights are less clear. The safest course is to serve written notice upon the former tenant, expressly stating the landlord’s intention of re-letting the premises to a new tenant, reserving rights relative to back-rent and any difference in future rent, as well stating all intentions regarding abandoned personalty of the former tenant. In Spitzer v. Selig Enterprises, Inc., 140 Ga. App. 156, 157 (1976), a tenant defaulted on rent for several months, and appeared to no longer have any presence at the leased premises. The landlord notified the tenant by letter that it intended to enter upon the premises, re-let the property, and collect back-rent. Id. Upon doing so, the new tenant disposed of the former tenant’s personalty left in the premises, and the former tenant sued the landlord for conversion, alleging that the landlord never formally requested the tenant to vacate.

Id. at 158. The Court of Appeals held that the landlord had a contractual right in the lease to re-enter and re-let the property if the tenant defaulted, provided notice to the tenant that it intended to exercise its right, and the tenant had, in fact, relinquished control of the property, therefore there was no requirement that the landlord follow strict dispossessory requirements. Id. at 159.

One must be concerned with which of these elements are absolutely essential to a lawful re-entry and re-letting of premises without pursuing a dispossessory, in order to avoid potential exposure for converting a tenant's property. In any case, it is evident that a landlord is on its most solid footing when its lease clearly defines rights upon abandonment, clearly documents its intentions through advance written notice to the tenant, then carries those intentions out pursuant to the notice.

III. Self-Help Considerations

When a landlord is confronted with a defaulting tenant, the resulting frustration can naturally lead to consideration of a self-help remedy, such as simply changing the locks. While such an approach seems simple enough on the surface – e.g. “the tenant has failed to pay me rent for months, so I’m not letting him use the space for even another day” – self-help remedies raise a number of legal and practical considerations. Indeed, for some landlords, the formal eviction process is required in order to remove a defaulted tenant. In other circumstances, use of the formal process could help spare the landlord from an even lengthier legal battle.

A. Legal Considerations

The first issue when considering self-help remedies is whether a landlord is legally permitted to evict the defaulted tenant without resort to a dispossessory court action. Fortunately for landlords, the answer under Georgia law is relatively clear: “[A] landlord *may* contract to avoid [the statutory notice and other requirements of a dispossessory proceeding set forth in O.C.G.A. § 44-7-50 et seq.] when renting property which is not used to be as a dwelling place.” Rucker v. Wynn, 212 Ga. App. 69, 70, 441 S.E.2d 417, 419 (1994) (quoting Colonial Self Storage v. Concord Properties, 147 Ga. App. 493, 495, 249 S.E.2d 310 (1978)). Thus, the first prong of the analysis is whether

the lease is one for “a dwelling place,” or put another way a “residential” lease. If it is, then Georgia law does not permit self-help procedures, regardless of the lease terms, for removal of a tenant. The landlord, instead, must utilize the statutory dispossessory proceeding provided by O.C.G.A. § 44-7-50 et seq.

By contrast, a commercial landlord is “entitled to rely upon the default provisions in the commercial lease agreement” and therefore may utilize self-help remedies permitted under the lease. Rucker, 212 Ga. App. at 70, 441 S.E.2d at 419. This raises the second prong of analysis – whether the lease permits the self-help remedy that the landlord seeks to utilize. In Rucker, the lease stated:

Landlord, as Tenant's agent, without terminating this lease may enter upon and rent the premises, in whole or in part, at the best price obtainable by reasonable effort, without advertisement and by private negotiations and for any term landlord deems proper, with Tenant being liable to Landlord for the deficiency, if any, between Tenant's rent hereunder and the price obtained by Landlord on reletting; provided, however, that Landlord shall not be considered to be under any duty by reason of this provision to take any action to mitigate damages by reason of Tenant's default.

Id. Thus, the Court of Appeals held that the landlord acted within his rights under the lease when he “reentered the premises without notice ... after business hours when the tenant was not present, evicted the tenants by changing the locks on the doors, and prepared and re-rented the premises.” Id.

B. Practical Considerations

Given the state of Georgia law, it is the practical issues rather than the legal issues that are the primary consideration for a commercial tenants with the requisite language in its lease agreements. As is often the case, the fact that a clear legal right to do something does not necessarily lead to the conclusion that one **should** do it. In this respect, the Rucker case provides a cautionary tale for a commercial tenant weighing its options with respect to a defaulting tenant.

Although Rucker is a court decision about an eviction, the underlying case was not filed by the landlord seeking an eviction. Indeed, it was far too late to seek that relief given the self-help remedy utilized by the landlord. Instead, the Rucker case was filed by the former tenant **against** the landlord, asserting claims for “wrongful eviction, trespass,

breach of implied covenant of quiet enjoyment of the premises, breach of lease agreement, breach of an alleged oral contract to accept late payment of rent, and conversion of personal property.” 212 Ga. App. at 69, 441 S.E.2d at 418. While the landlord ultimately prevailed in the Court of Appeals, the mere fact that he was subjected to a multi-count lawsuit and protracted litigation (including the appeal) clearly undermined the efficiencies he sought to gain by avoiding the statutory dispossessory proceedings.

Thus, a commercial landlord should weigh the risks of a formal lawsuit by the former tenant claiming conversion or wrongful eviction. Such a lawsuit, even if won on a motion to dismiss, is often likely to be lengthier and costlier than the dispossessory proceedings under O.C.G.A. § 44-7-50 et seq., which include numerous expedited deadlines as discussed in prior articles in these materials.

IV. Who’s to Clean Up the Toxic Waste Left by the Tenants?

A problem commonly associated with industrial and retail leases is allocating the burden associated with disposing of tenants’ hazardous waste. To be sure, these burdens should be expressly addressed in the terms of the lease, especially if either the commercial enterprise associated with the premises is especially susceptible to environmental issues or hazardous waste concerns.

As a general matter, landlord’s are not responsible for the leased premises, including waste, if the tenant has complete possession of the leased premises. Pursuant to O.C.G.A. § 44-7-14, “having fully parted with possession and the right of possession, the landlord is not responsible to third persons for damages resulting from the negligence or illegal use of the premises by the tenant.” Although not specifically in the context of hazardous waste, in Pitts v. Ivester, 171 Ga. App. 312 (1984), the Court of Appeals looked to the terms of the lease, and the facts pertinent to the landlord’s continued involvement with the premises, in order to determine when a landlord assumes a duty to maintain and monitor the activity at its premises. Id. at 314. Because the lease at issue did not place any obligation on the landlord to inspect the premises for dangerous conditions, and because the landlord neither had control over the premises nor induced

third parties onto the premises as a matter of fact, the landlord could not be found responsible for conditions at the premises. Id.

However, in certain circumstances, there could certainly be landlord liability to third parties for waste left by a tenant in the same way a landlord assumes responsibility for other hazards on its premises. This is especially true where the lease is either unclear as to the parties' responsibilities, or the landlord exceeds his common law responsibilities over the course of the lease and creates his own additional duties. Consequently, lawyers should advise their landlord clients to expressly allocate waste-related responsibilities in their leases, and be careful to avoid assumption of any additional exposure through conduct.

V. Bankruptcy Considerations for the Landlord/Tenant Relationship

Any analysis of the rights of landlords and tenants law will appropriately focus on property and contract law, but in the current economic climate a brief discussion, at least, of bankruptcy law is warranted. The purpose of this section is, of course, not to transform the reader into a bankruptcy lawyer or expert, but instead provide guidance regarding some of the fundamental principles that may be relevant when a tenant files for bankruptcy.

As is often the case with landlord/tenant issue, the impact of a bankruptcy filing can vary depending on the terms of the lease and the rights granted thereunder. Nevertheless, there are some general guiding considerations, particularly those provided in Section 365 of the Bankruptcy Code.

11 U.S.C. § 365 permits a tenant that has filed bankruptcy to either assume or reject an unexpired lease (within certain procedural and time limitations for doing so). Thus, a tenant in bankruptcy has the beneficial position being able to assume a below market lease or reject an above market lease. In the event the tenant decides to assume the lease, it remains in effect through and after the bankruptcy proceedings. It should be noted, though, the tenants continued occupancy is not free-of-charge, but rather the tenant is require to cure any outstanding defaults and perform all obligations under the lease.

Importantly, the above provisions of 11 U.S.C. § 365 apply only to **unexpired** leases. Therefore, the most straightforward way for a landlord to avoid the uncertainty

associated with a tenant's bankruptcy is to terminate the lease before the tenant files for bankruptcy. A tenant's bankruptcy can often be preceded by late rent payments, requests from the tenant to make installment payments, or other signs of financial distress. When the tenant's financial distress manifests itself in the form of an event of default under the lease, the landlord should weigh any termination options it may have against the risk of bankruptcy proceedings.

Some commercial leases contain provisions that purport to automatically terminate the lease upon a tenant's filing for bankruptcy. Such clauses, while occasionally held to be enforceable under state law, are deemed unenforceable by the Bankruptcy Code. *See* 11 U.S.C. § 365(e)(1). Moreover, such clauses are disfavored by court, with one Georgia federal court going as far as to say a "basic" policy of bankruptcy law "abhors the operation" of such clauses. *See In re James Cable Partners, L.P.*, 154 B.R. 813, 816 (M.D. Ga. 1993). Thus, in the interest of caution, a landlord desiring to avoid a tenant's bankruptcy proceedings should act promptly on any pre-bankruptcy defaults rather than relying on an automatic termination provision.