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Structuring Landlord Lien Waivers and Collateral Access Agreements: Navigating Competing Interests of Tenant's Lender and Landlord

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August 15, 2017



Landlord Liens



- Three ways that landlords obtain lien or other security interests in tenant's personal property.
 - Consensual security agreement
 - Common law rights of distress or distraint
 - Statutory

Consensual Security Interest

- A landlord may obtain a lien against the tenant's personal property and fixtures through a consensual security interest under Article 9 of the Uniform Commercial Code
 - Written security agreement is required, must include language setting forth the security interest and adequately describing the collateral

Consensual Security Interest

- Landlord must perfect by filing a UCC financing statement in the appropriate state filing office
 - May be filed without the tenant's signature so long as authorized
 - Without financing statement, security interest is unperfected and subordinate to any perfected security interest in same property

Enforcement of Consensual SI

- Landlord may foreclose on the property pursuant to the procedures set forth in the UCC without requirement of filing a court action or exercising other judicial process
 - Significant advantage over common law or statutory rights
 - Caveat: UCC financing statements are only valid for five years

Common Law

- Traditional common law rights of distress and distraint enable a landlord to seize and sell a tenant's personal property located at the premises in order to reimburse the landlord for the amount of unpaid rent and other liability
 - Typically enforced via self-help, without a court order
- Not a lien, per se

Statutory Landlord Liens



- Given to landlords in about half of the states
- There is no uniform or model landlord's lien law and reference must be made to the specific statutes in each applicable jurisdiction
 - Virginia Code Sections 55-227 through 55-238
 - DC Code Sections 42-3213 through 42-3216
 - Maryland Real Property Code Ann. Sec. 8-302 (no automatic statutory lien, landlord action for distress for rent only)

Statutory Landlord Liens



- Rights differ from state to state as to timing, priority and limitations
 - Typically provide the landlord with a lien on all of the tenant's personal property located within the demised premises as security for the tenant's obligations under the lease
- Liens replace or supplement the common law remedies of distress and distraint
 - Often limited to a specific amount or period of time

Extent Of Landlord Liens



- Machinery and Equipment
- Fixtures
- Inventory

- Creditor will typically take priority if UCC financing statement is filed before equipment is placed on the property
- Competing with Purchase Money Security Interests
 - See definition of “security interest”
 - Va. Code Secs. 8.9-324(a), 8.1A-201(b)(35)

Enforcement of Statutory Liens

- Enforcement is often relatively cumbersome, expensive, time consuming
- Limited by statute
- Subject to avoidance in the event of tenant bankruptcy

Enforcement of Statutory Liens

- Virginia, DC and Maryland all require landlord to file a court action and follow very detailed procedures designed to afford the tenant adequate due process prior to losing its property

Enforcement in DC

- Statutory lien terminates three months after the rent owed became due or upon the termination of any action seeking such unpaid rent brought by landlord within that three-month period

Enforcement in Virginia

- Relates back to the commencement of the lease
- Secures:
 - Not more than six months rent if premises are in a city or town, property used for residential purposes
 - Not more than twelve months rent on land used for farming or agriculture

Enforcement in Virginia

- Superior to any other lien upon the tenant's property located at the premises, except for liens attaching prior to the commencement of the lease term and tax liens
- Extends to any goods of the lessee (including lessee's assignee or subtenant) either:
 - Found on the premises or
 - Removed from the premises during the preceding 30 days

Enforcement in Maryland

- No statutory lien rights in favor of a landlord, so a landlord would have to pursue an action for distress with the ability to then lien the personal property if successful in obtaining a judgment

Bankruptcy



- 11 U.S.C. sec. 545(3) and (4)
 - Allows the trustee (or debtor in possession) to avoid any liens for rent or distress for rent (seizure of personalty to enforce a rental obligation)
 - Section specifically uses term “statutory lien” but definition includes all liens for distress for rent whether statutory or not
 - Lease provisions providing for a lien on personalty will generally be ineffective in bankruptcy

Bankruptcy

- Landlord holding perfected UCC security interest will be treated as a secured creditor
 - subject to automatic stay imposed by 11 U.S.C sec. 362

Landlord Waiver Agreements

- The tenant's lenders will want a security interest in the tenant's personal property to secure the repayment of the tenant's loan obligations, creating a conflict between the lien rights of the landlord and the lender
 - As a condition to financing, lenders typically request that the landlord execute waiver
 - SBA loan – landlord waiver an absolute requirement

Landlord Waiver Agreements

- Landlords recognize financing as a critical need without which the tenant would not be able to operate its business and generate the revenues needed to pay the rent
 - May push back at a request to a waiver, but will often to agree to at least subordinate their landlord's lien rights to that of the lender's security interest
 - Subordination (rather than waiver) would at least provide secondary secured position and limited recovery in default situation

Landlord Waiver Agreements

- Lenders Perspective:
 - Landlord waiver agreement is typically bank document prepared by lender's counsel
 - Often grants lender favorable rights and places burdensome obligations on landlord
 - Tenant typically is not a key party to the negotiations, may play a referee position

Landlord Waiver Agreements

- **Tenant's Perspective**

- include lender's required waiver form as exhibit to lease agreement to save time and expense later
- Landlord may try to pass on legal fees incurred in negotiation of waiver onto tenant

Tips for Landlords

- Since most landlord waiver/subordination documents start out as one-sided bank forms, the landlord with leverage should request certain changes to protect their rights.
- **8 Suggested Negotiating Points/Changes**

Tips for Landlords (#1)

- Subordinate landlord's lien rather than provide outright waiver
 - Second lien position may be questionable, but leaves some chance of recovery
 - Limit waiver or subordination only to landlord's statutory or common law rights, not all liens (i.e., judgments)
 - Waiver should not terminate tenant's continued liability under lease

Tips for Landlords (#2)

- Retain control over the process of the lender removing the collateral
 - Removal only after business hours and from designated loading areas
 - Lender must pay for any damage caused by removal, indemnify landlord in case of third party claims resulting from entry
 - Landlord must furnish evidence of insurance
 - Lenders will typically agree to repair damage, push back on blanket indemnification

Tips for Landlords (#3)

- Make clear what equipment constitutes collateral
 - Landlord should agree that personal property remains personalty in exchange for lender agreeing not to pursue its security interest in building systems
 - Ensure leasehold interest does not constitute collateral
 - Exclude cash accounts

Tips for Landlords (#4)

- Limit requirement of notice of tenant's default under lease
 - Landlord will want notice and an opportunity to cure on behalf of tenant, but this places administrative burden on landlord
 - Limit to notice of defaults which may result in termination of lease, or of termination itself
 - Keep cure period short and limited to monetary defaults

Tips for Landlords (#5)

- Limit period after termination for removal of collateral
 - Lender will request a time period (typically sixty to ninety days) to take inventory and remove collateral
 - May not be unreasonable, but prevents landlord from re-leasing property
 - Landlord may insist the lender pay rent during such period, important to define starting and expiration point of such obligation

Tips for Landlords (#6)

- Replacement tenants
 - Lender should agree not to interfere with landlord's efforts to re-lease premises
 - Property should remain available for reasonable inspection by landlord

Tips for Landlords (#7)

- Public liquidation sales
 - Landlord should request lender not to hold such sales without landlord prior consent and subject to landlord's reasonable conditions

Tips for Landlords (#8)

- Termination of Agreement
 - Waiver or subordination document should clearly provide that agreement terminates upon tenant's full repayment or satisfaction of loan, particularly as to landlord's obligations



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