

BE PREPARED: BAD TENANTS HAPPEN TO GOOD LANDLORDS

By: Jack Garson, Esq.

If you own property, you've heard the nightmares. You've prayed they don't happen to you. But they happen all the time.

For instance, a dry cleaner owed his landlord more than \$100,000 in rent. The business then abandoned the premises and left behind a mess of obsolete dry cleaning equipment. Worse yet, the dry cleaner had regularly spilled perc on the premises, a hazardous solvent that is expensive to remediate. The landlord's losses from unpaid rent and remediation exceeded: more than \$350,000.

Whether he owns a shopping center in Bethesda, a warehouse in Manassas, lab space in Rockville or an office building in the District, a landlord must guard against tenant defaults at several critical times: when qualifying a tenant, when preparing the lease and when pursuing his own rights.

Beware of phantom financials.

Obviously, the best way to avoid tenant defaults is to avoid problem tenants in the first place. Prudent landlords qualify tenants by requesting financial and experience information. Be prepared with a list of required information and forms to assist the prospective tenant in providing both a balance sheet (summarizing assets and liabilities) and an income statement (describing revenue and expenses over a particular time period).

One client recently sued a tenant who had failed to pay rent, only to discover the tenant had pulled off a bait and switch. The tenant had provided the landlord with financial statements for an entity that was solvent and had adequate assets. When the lease was executed, however, a related entity with a similar name, but no assets, signed the lease. As a result, the landlord had no effective recourse for the unpaid rent.

Prevent problems early.

Additional measures to qualify a tenant include obtaining references, personal guarantees, and collateral for the tenant's obligations, such as a security deposit or letter of credit.

Typically, the lease provides the business terms: a well-prepared lease also protects the landlord if the tenant defaults. Include provisions that identify and clarify the tenant's obligations, that describe when the tenant shall be in default and that provide enforceable remedies in the event of the tenant's default.

Wear and tear by forklift.

Leases often fail to clearly describe a tenant's obligations. For example, when a tenant vacates the premises, what must the tenant do to restore the premises to its original condition? One landlord was shocked to learn that holes gouged in the cinder block walls of a

warehouse by the tenant's forklift constituted ordinary wear and tear in the view of the judge. The landlord would have benefited from greater clarity in the lease, such as limiting the ordinary wear and tear provision to floor and wall coverings instead of the entire premises.

Also, describe when the tenant shall be in default. Failure to pay rent is an obvious default. Less obvious defaults might include unauthorized alterations, excessive use of parking, utilities or other facilities, failure to cooperate with a refinancing or sale of the property and interfering with other tenants.

Significantly, the lease must contain not just a list of landlord remedies, but remedies that a court will enforce.

Late charges may apply.

Many jurisdictions limit other landlord remedies. Often, a landlord is prohibited from accelerating the rent, even when the tenant has repeatedly failed to pay the rent. Accordingly, it may be appropriate to provide for a significant late charge if



the tenant fails to pay rent in a timely manner. Landlords also are vulnerable because of other unusual laws. For example, if a tenant signs the lease, but refuses to accept the premises, the landlord may not be able to recover all of the rent that the tenant should have paid under the lease. The only meaningful remedy may be a liquidated damages clause requiring the tenant to pay the landlord a predetermined estimate of the landlord's damages.

Once the tenant breaches, a savvy landlord should review the lease to confirm all rights and obligations, provide required notices and reserve your rights, obtain experienced counsel to file suit and preserve any settlement in a carefully drawn agreement.

The greatest regret of most landlords is signing a lease with a bad tenant in the first place. Most landlords also regret failing to act swiftly when a bad tenant breaches the lease. As a rule of thumb, if a tenant fails to pay the rent, a landlord should

send a notice of default no later than the date that the next rent payment is due. Prepare well, act aggressively.

Be aware that the courts and procedures applicable to lease disputes are highly specialized, often arcane and usually counterintuitive. Your lawsuit to evict the tenant might be dismissed because you provided the tenant with 30 days notice, instead of one month's notice. The tenant might then request a trial by jury, resulting in a further delay of the trial by as much as one year. Notably, by requesting a jury trial, the tenant also may be able to prevent you from receiving the rent for that one-year period. Finally, on the eve of trial, your lawsuit might be dismissed because the tenant vacates the premises.

To avoid such an outcome, landlords should engage knowledgeable assistance, prepare leases very carefully, and take aggressive action when necessary.

ABOUT JACK GARSON



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Jack Garson's practice focuses on Real Estate, Construction and Business law. He serves as a legal advisor for numerous local, regional and national companies. In his role as legal counsel, Jack also serves as a strategic advisor and lead negotiator. Further, Jack provides guidance on the structure of complex transactions, the resolution of business disputes, the growth and sale of companies, and the management of issues such as liability and risk reduction, employment practices, and enhancing profitability.

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In the past two years, we've grown by 50% through expansions in New York City and, most recently, Charlotte, North Carolina. This growth has provided immense value to our clients and attorneys.

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