



# CCM COVID-19 ALERT

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## COMMERCIAL LEASING ISSUES DURING COVID-19 OUTBREAK

Commercial landlords and tenants are facing a challenging landscape with the COVID-19 outbreak and its impact on the real estate industry of the United States. With the risks stemming from the outbreak, landlords are encouraged to review leases they have with all tenants and their insurance policies. Possible leasing issues include force majeure provisions, notice requirements concerning such provisions, insurance coverage, and casualty clauses.

### Force Majeure

“Force majeure” or “unavoidable delays” provisions provide for the allocation of risk of certain force majeure events. These events may arise and prevent a party from performing under the contract, or in this case, the lease. The clause extends the period of time prescribed in the lease for performance of an obligation. The requirement to perform is not a permanent discharge, but rather, a deferral or excuse for the number of days of the force majeure event. Leases vary as to whether only the landlord or both the tenant and landlord benefit from the deferral of performance of obligations. The clause may have either an unrestricted or finite list of force majeure events which trigger the provision. An event such as “act of God” may be included as a force majeure event, which might include a pandemic such as the current COVID-19 outbreak. Additionally, a force majeure event definition of “causes beyond the control of a party” may

also be triggered by the current outbreak. Other lease provisions may also reference force majeure and should be reviewed by landlords. Leases often include a carveout for the payment of money, meaning the occurrence of a force majeure event does not excuse such actions as the payment of rent or maintenance of insurance. Landlords can point to these carveouts in denying a tenant's request for rent relief.

Another aspect of a force majeure provision to consider is the inclusion or absence of a written notice requirement of the existence of a force majeure event. This written notice may be required before a party can claim an extension or excuse for non-performance. A landlord will want to consider whether such written notice needs to be provided within a certain number of days of the occurrence of the force majeure event, or if the lease calls for an extension that is limited to a specified number of days. If tenants try and claim constructive notice due to the prevalence of COVID-19 in the news and elsewhere, landlords should carefully review the procedural requirements of a party under a force majeure provision. Landlords will also want to review the procedural requirements in case they need to be the party to provide notice.

Outside of the payment of rent, there are multiple circumstances which may be impacted by a force majeure provision concerning a landlord. Circumstances include construction and improvement delays to properties, which could impact the ability of the landlord to deliver possession of property to a tenant. Another situation impacted by a force majeure provision may

include a tenant's request or notice of cessation of business operations. This, which may violate an obligation to continuously operate contained in the lease, may be excused for the duration of the force majeure event.

### **Insurance Coverage**

Leases often call for a tenant to maintain certain insurance policies and coverage. There is also typically a waiver of subrogation included in leases. This clause indicates the landlord and tenant waive claims against the other for loss, damage, or injury which is covered by the insurance carried by such party. The impact of this clause may cause a landlord to direct a tenant to look to its insurer concerning rent relief. These insurance policies may explicitly exclude loss or damage caused by contamination, disease, or virus or the spread or proliferation of such contamination, disease, or virus. Other policies may contain a sublimit for contamination, disease, or virus issues to limit monetary relief. Insured parties should review the definitions, exclusions, endorsement, or extension and other provisions of its insurance policies to understand coverage.

Business interruption insurance may be applicable to policyholders impacted by COVID-19. This type of coverage provides for lost profits and related costs when a company cannot continue normal business operations. Such interruption must result from direct physical loss or damage to the policyholder's property. If a property remains habitable, even if it is closed due to fears of COVID-19, then the policyholder most likely does not meet the direct physical loss requirement. There may be a

direct physical loss if the property is contaminated, such as an infected person has physically been inside. Many business interruption policies contain exclusions for damage arising from virus, communicable disease, or bacteria.

An extension of business interruption insurance may apply, "civil authority". This provides coverage for loss of business income when an order of civil or military authority impairs access to the company's business operations. The civil authority aspect of business interruption insurance requires physical loss or damage to property for coverage. It is likely that a mandatory quarantine order or an order closing a business to prevent the spread of COVID-19 qualifies as an order of civil authority. This coverage is reactive, not proactive. There is no coverage for losses sustained when a business closes due to fear of contagion or for measures taken before actual property damage occurs.

### **Casualty Clauses**

Leases can include casualty clauses. The COVID-19 outbreak might be considered under a casualty clause. However, as the virus is appearing to be temporary and the property damage may be difficult to prove, claims under casualty clauses are not likely to be successful. Landlords should still consider casualty policy coverage and abide by any notice requirements in order to preserve such claims.

## **Searching for Solutions**

Landlords may wish to explore individual workouts with their tenants. This could be a temporary deferral of rent for a short period, with the repayments to occur over future periods. Solutions between landlords and tenants may result in negotiations of lease provisions. Landlords might seek amendments to or elimination of more tenant-favorable provisions or they might seek an extension of lease terms in exchange for rent deferral. Landlords should also consider language with tenants about insurance proceeds that may be recovered later. This would require tenants to reimburse landlords from such proceeds received.

## **Notice to Tenants**

Landlords may find themselves in a situation where there is a confirmed case of COVID-19 at one of their properties. Landlords and property managers need to be mindful of privacy law concerns with the sharing of any information. Keeping such concerns in mind, a landlord or property manager should disclose the presence of a confirmed COVID-19 case to other tenants and occupants of a property. Such proactive steps may limit exposure against claims of negligence or of intentional acts triggered by non-disclosure.

Landlords and property managers should consider consult their real estate attorneys to discuss the implications of COVID-19 on their particular responsibilities and leases.

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