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Workshop 28

Lenders and Landlords and Tenants, Oh My! - Balancing the Competing Interests in Estoppels, SNDAs and Recognition Agreements

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I. TENANT ESTOPPELS

A. What is a Tenant Estoppel?

The legal definition of a tenant estoppel certificate, according to Black's Law Dictionary, is as follows: "[a] signed statement by a party (such as a tenant or mortgagee) certifying for another's benefit that certain facts are correct, as that a lease exists, that there are no defaults, and that rent is paid to a certain date. A party's delivery of this statement estops that party from later claiming a different state of facts.'' Black's Law Dictionary, 572 (7th Ed., 1999).

Most commercial leases will require an estoppel certificate from the tenant upon request. This document is extremely important for due diligence during the acquisition process or underwriting a commercial real estate loan.

A potential purchaser of a shopping plaza has an interest in obtaining estoppel certificates from as many tenants as possible because "[a]n estoppel certificate (also called an estoppel statement or estoppel letter) is a writing given by a lessee setting forth specific facts pertaining to the lessee-lessor relationship, with the intention that a third party (normally, the lender or a purchaser of the fee interest) rely on the statements.'' Alvin L. Arnold & Jeanne O'Neill, Real Estate Leasing Practice Manual, § 35:1 (West Online 2005).

"The purpose of an estoppel statement is twofold: (1) to give a prospective purchaser or lender information about the lease and the leased premises and (2) to give assurance to the purchaser or lender that the lessee at a later date will not make claims that are inconsistent with the statements contained in the estoppel.'' Id. Depending on the size of the shopping center at issue, a 100 percent response rate from tenants may not be feasible, but "a buyer should insist on estoppel certificates from all tenants whose tenancies are a key component of a property's cash flow.'' Stephen A. Cowan, Negotiating the Sophisticated Real Estate Deal 2004: High Stakes Strategies in Uncertain Times: Strategic Analysis of Due Diligence Issues, 39, 58 (PLI Real Estate Law & Practice Course Handbook, Series No. 2948, 2004). As part of its due diligence, a purchaser will rely upon tenant estoppel certificates in determining the offering price for the shopping center, and whether the price ultimately paid is reasonable, given the property's income-generating capacity.

B. Why Should I Have One?

In recent years, commercial tenants have become increasingly assertive in their negotiations and real estate investment trusts ("REITs"), institutional investors, and lending institutions have developed stricter underwriting requirements for the cash flow being generated by a commercial facility about to be acquired or financed.

A tenant estoppel will provide evidence of an establishment's cash flow, which is information a potential investor or lender would need. When parties do not provide for appropriate tenant estoppel requirements, a proposed transaction can be jeopardized.

C. Elements of Tenant Estoppel Certificate

The landlord's typical form of commercial shopping center lease often provides that the tenant must deliver an estoppel certificate within a specified time after the landlord requests it. A typical provision reads as follows: Tenant shall deliver to Landlord upon ten (10) days' request by landlord an estoppel certificate stating:

- The commencement and expiration dates of the lease;
- The amount of rent being paid currently;
- The existence of any amendments, supplements or modifications to the lease;
- Whether or not landlord or tenant is in default of its obligations under the lease;
- The last date through which rent has been paid;
- The amount of any security deposit paid; and
- Such other statements as may be reasonably requested by landlord.

Additional items that should be added to the form of estoppel certificate by a purchaser or lender include:

- Free rent periods and tenant allowances to be paid by Landlord; and
- Negotiated termination rights.

D. Practical Considerations

In determining whether you should ask for tenant estoppel certificate(s), factors such as the prospective purchaser's objective (long-term hold or short-term flip), the size of the building(s), the number of tenants and the lender involved in a purchase may dictate the time devoted to obtaining and reviewing tenant estoppel certificates. With appropriate consideration given to the economics of transactions, counsel for landlords and prospective purchasers will best serve their clients' interests by obtaining as many tenant estoppel certificates as possible and carefully examining them for accuracy during the appropriate due diligence period so that the possibility of later litigation over material lease terms will be minimized.

Recommendations for "Tenant Friendly" Tenant Estoppels in Acquisitions

The more complete and shorter the form of tenant estoppel certificate submitted to a tenant, the more likely that the tenant will sign it. The following methods will facilitate obtaining a mutually satisfactory tenant estoppel certificate:

- When negotiating the form, try hard to keep it short.

- Between the landlord and the prospective purchaser, make the completion of the form of tenant estoppel to be submitted to a particular tenant a cooperative effort, that is, one party should complete the form and ask the other party to review it for completeness and accuracy within a specified time period.

- List all lease documents, including amendments, supplements and material letter agreements, in sufficient detail and make them part of the defined term "Lease" in the estoppel so the statements confirmed by the tenant relate to all of the foregoing documents. All applicable lease documents (i.e., amendments, rent commencement date memorandums, delivery notices, and notices regarding exercising options) should be attached to the estoppel as an exhibit.

- Consider if it would be unfair to require an absolute statement from the tenant, such as: (a) there are no circumstances which, with the giving of notice or passage of time, or both, would give rise to a landlord or a tenant default under the Lease; or (b) tenant has complied with all environmental covenants under the lease. A reasonable middle ground would be to give the tenant a qualifier to such statements - "to the best of tenant's knowledge" in either situation or using a "materiality" standard.

- Do not insist on provisions that make the tenant certify a legal conclusion. For example, a small, unsophisticated tenant in a shopping center or office building may simply not understand a certification that "the lease is non-recourse to the landlord." That conclusion is more appropriately dealt with by counsel for the purchaser in its due diligence and landlords should try to eliminate such a provision from the form of estoppel during negotiation.

See Diana C. Liu, *Counseling the Landlord on Tenant Estoppels and Sndas (with Forms*), Prac. Real Est. Law., July 2000, at 15, 17–18.

Dealing with Tenant Objections and Omissions (Landlord's Counsel)

Below are some practical tips for the landlord and landlord's counsel, in dealing with tenant objections to or omissions from the tenant estoppel:

- Check to see that all estoppels are dated and properly signed before delivering them to the prospective purchaser or the lender. If they are not, send them back to the tenant on an expedited basis to have the omissions addressed.

- If the signatory for the tenant is based at the leased premises as opposed to a corporate headquarters located elsewhere, arrange for the property manager at the premises (assuming a good relationship with the tenant) or an officer of the landlord who is a regular contact person with the tenant to visit the tenant and discuss the possibility of eliminating those objections or substantially limiting them. Often some of the objections can be eliminated or qualified with some explanation by the tenant in the estoppel once the tenant is made to understand the landlord's reasons for having certain certifications included. Be prepared for "Plan B" in case the tenant insists on its objections: have suggested language at hand to

limit the effect of the tenant's objections, such as knowledge qualifiers or prepare limited exceptions to a certification on an attached schedule.

• Keep the prospective purchaser's counsel or the lender's counsel fully apprised of your efforts to eliminate the objections.

• Some major tenants may have crossed out provisions requiring them to certify that there are no purchase options, renewal options, or options to terminate, or may have qualified those provisions with "except as set forth in the Lease," on the ground that the purchaser's or the lender's counsel can review the lease in question and satisfy itself on those items. Since this information from the mouth of the tenant is critical to the purchaser and the lender as a back-up to its own due diligence, counsel for the purchaser or lender is generally not inclined, nor should they be willing to accept such a position from the tenant. So, push hard on this point.

• If the estoppel is returned with certifications that are inconsistent with the lease, such as the assertion of an early termination right based on an alleged oral agreement between the tenant and landlord, what can you do? Although the case law isn't settled on whether inconsistent statements made in a tenant estoppel effectively modify the underlying lease, when you are faced with a "required" estoppel, advise your client of the need to meet with the tenant to come to a mutual agreement on whether this right exists and to promptly advise purchaser's counsel of that agreement. If the landlord believes that the asserted right exists but the lease file is at best scant on the issue, suggest to your client to document this right with certain concessions from the tenant, for example, as to when it can be exercised and the payment of unamortized tenant improvements and leasing commissions, if any, upon exercise of the termination right.

• Tenants have been known to balk at the certification that they are not the subject of any bankruptcy or insolvency proceeding on the ground that they do not know whether an involuntary proceeding has been instituted against them or threatened to be instituted against them. Landlord's counsel and purchaser's counsel should insist on obtaining this certification since it is not always easy for such counsel to obtain this information and the tenant could reasonably be expected to know about its affairs with its creditors.

• When a particular tenant absolutely refuses to deliver an estoppel or will deliver a substantially pared down form, landlord's counsel might suggest delivering a landlord estoppel as to that tenant.

See Diana C. Liu, *Counseling the Landlord on Tenant Estoppels and Sndas (with Forms*), Prac. Real Est. Law., July 2000, at 15, 17–18.

E. Cases Interpreting Tenant Estoppel Certificates

Despite their widespread usage, there are relatively few reported decisions interpreting the effect of tenant estoppel certificates in landlord-tenant lease disputes. Cases interpreting tenant estoppel certificates are largely driven by the facts of each dispute. Common to all of the disputes, however, is a determination that the shopping plaza purchaser (as well as a landlord) is entitled to rely upon the representations made by a tenant in an estoppel certificate.

Ohio

In *Mark-It Place Foods, Inc. v. New Plan Excel Realty Trust, Inc.*, 156 Ohio App.3d 65 (2004), New Plan purchased a shopping center after obtaining an estoppel certificate during its due diligence period. A dispute later arose about an exclusive use violation. All parties moved for summary judgment; on appeal, the Ohio Court of Appeals affirmed in part and reversed in part, and remanded the cause for further proceedings. The court of appeals noted that New Plan, as the purchaser of the shopping center, was entitled to rely upon a January 1993 estoppel letter (obtained during the course of its due diligence prior to purchasing the center). New Plan had introduced evidence of reliance on the representation made in the estoppel certificate. Mark-It Place Foods, 156 Ohio App.3d at 88 - 89, 91 and 94. On remand, the trial court was charged with determining whether New Plan's reliance was reasonable under the facts of the case.

In *Freshman v. Attaboy Manufacturers' Representatives*, Inc., 92 AP-638, 1993 WL 20061 (Ohio App. Feb. 2, 1993), Attaboy entered into a triple net lease with the landlord's predecessor-in-interest in 1984. Attaboy was required to pay minimum rent on a monthly basis, along with real estate taxes and hazard insurance, and periodically execute and deliver estoppel certificates to the landlord. (The tenant acknowledged that the estoppel certificates might be relied upon by a prospective purchaser of the shopping center.) The original landlord agreed

to construct a 12,000 square foot building for the tenant, and the tenant agreed to pre-pay certain rents. Although delivery of the completed building was scheduled for February 1984, it did not occur until April 1984; as a result, the tenant was entitled to rent abatement under the terms of the lease. In December 1986, Freshman purchased the shopping center. As part of the landlord's due diligence, the tenant executed an estoppel certificate which acknowledged that it had not received any rent concessions, and had not made any payments to the landlord as advanced or prepaid rent. When Attaboy subsequently vacated the property, Freshman's attempts to collect unpaid rent, property insurance and property taxes were unsuccessful, and litigation followed. The trial court found for Freshman, but awarded substantially less than what was sought in the complaint. The court of appeals later opined that the trial court erroneously construed the tenant estoppel certificate executed by Attaboy, and reversed and remanded. Addressing the purpose of the estoppel certificate, the court of appeals noted that "this certificate estopped Attaboy from claiming any prepaid rent against plaintiff. There may have been some question of what the overpayments were for in 1986, but this particular estoppel certificate was sought for the protection of plaintiff, as is done in commercial lease transactions.'' *Freshman*, 1993 WL 20061 at *4 (emphasis added). The court of appeals also recognized that "[e]stoppel certificates are useful devices to preserve and enhance the marketability of commercial property.'' Id.

Similarly, in *Katz v. M.M.B. Co.*, No. 50579, 1986 WL 5298 (Ohio App. May 8, 1986), the landlord and the tenant entered into a five-year lease in 1978. In 1979, and again in 1981, the tenant executed estoppel letters in which it affirmatively stated that it had no claims or set-offs with respect to rent paid under the lease. In 1984, the tenant sued the landlord for breach of contract, claiming it had paid annual rent in excess of that required by the lease from 1978 - 1984. The trial court held that the landlord had overcharged the tenant. On appeal, the landlord contended that the trial court erroneously failed to apply the doctrines of waiver or estoppel to bar the tenant's action. The Ohio Court of Appeals noted that the landlord's rent bills were itemized to reflect the amounts paid in rent, operating expenses and electricity, and concluded that the tenant should have known by the time the estoppel letters were executed in 1979 and 1981 that he was being overcharged. The court of appeals went on to hold "that when the tenant signed the letters waiving his claims upon the lease, he was on constructive notice that its terms were being violated.'' *Katz*, 1986 WL 5298 at *3. The court of appeals concluded that the "letters estop the tenant from claiming he has been overcharged.'' Id. The court of appeals affirmed in part, reversed in part, and remanded the case to the trial court to determine the extent of the landlord's liability for overcharges after the 1981 estoppel letter, finding that the tenant had waived only that portion of overcharged rent preceding the 1981 estoppel letter, and was, therefore, entitled to a refund for all overcharged rent thereafter. The court of appeals cited *McAdams v. McAdams (1909), 80 Ohio St. 232* relying on the premise that "… it has long been established that a party who signs his name to an agreement cannot later say that he was ignorant of its contents in order to escape liability."

New York

In *SRM Card Shop, Inc. v. 1740 Broadway Associates, L.P.*, 769 N.Y.S. 2d 483 (2003), the subtenant plaintiff took possession of retail sales space and adjacent storage space under a 1988 sublease with Hallmark. The original landlord then sold the building to the defendant in 1990. In 1996, the subtenant agreed with the landlord's agent to exchange the adjacent storage space for noncontiguous space in the building's basement, and the agent agreed to waive a December 1998 rent increase. Although Hallmark (as the sublessor) was not advised in advance of the proposed storage space exchange, a Hallmark representative was notified of the exchange the day it occurred and did not object. The lease was never modified in writing, and the original storage space was rented to another tenant. In 1997 (after the 1996 space exchange and before the originally scheduled 1998 rent increase), Hallmark and the subtenant plaintiff executed an estoppel certificate for the landlord, which stated (among other things) that there were no offsets, abatements, or defenses against fixed or minimum rent, escalation rent or additional rent payable under the lease. In December 1998, the landlord implemented the scheduled rent increase, and the plaintiff refused to pay, citing the 1996 oral agreement. The subtenant brought a declaratory action against the landlord for reformation of the lease, and the landlord commenced a separate action for nonpayment of rent. After the cases were consolidated, the trial court granted summary judgment in favor of the subtenant. The trial court found that Hallmark had been actually partially evicted, and neither Hallmark nor the subtenant was obligated to pay the increased rent until possession of the original storage space was restored. On appeal, the landlord argued that Hallmark had acquiesced to the storage space substitution, and the estoppel certificate executed by Hallmark and the subtenant barred the partial actual eviction defense. The appellate division of the supreme court agreed, reversed and granted summary judgment for the landlord.

Pennsylvania

In *Liberty Property Trust v. Day-Timers, Inc.*, 815 A.2d 1045 (2003), Day-Timers entered into a 1988 lease with Liberty's predecessor-in-interest. The lease was amended in 1991 by way of an addendum, and provided for a flat rental charge through June 1, 1996, with annual increases thereafter based upon percentage

increases in the Consumer Price Index (CPI). Prior to the June 1996 increase, Day-Timers was notified by the original landlord that the rent would increase by only 8% as opposed to 15%. The following month, the original landlord circulated a second addendum to the lease, which proposed a further modification to the annual CPI adjustment to Day-Timers' rent. The second addendum was never executed, but rent was apparently calculated by the original landlord and paid by Day-Timers as if it were in effect. Liberty acquired the property from the original landlord in 1997. As part of the sale, Day-Timers executed a tenant estoppel certificate that identified the 1988 lease and the 1991 addendum as the operative lease documents, but made no reference to the proposed and unexecuted second addendum. After Liberty acquired the property, it charged Day-Timers rent calculated without regard to the unexecuted second addendum. Day-Timers refused to pay, and Liberty sued for breach of the lease and declaratory relief. The trial court, finding that the unexecuted second addendum was an enforceable oral modification of the lease, entered judgment in favor of Day-Timers, and Liberty appealed. On appeal, the Pennsylvania Superior Court vacated the trial court's judgment and remanded the case, noting that "no reference was made to the modification of the lease which is at the heart of this dispute.'' Liberty Property, 815 A.2d at 1051. Focusing on the central issue of the case, the superior court found that "Day-Timers made an affirmation [sic] representation in the certificate that there were no oral modifications of the lease, precisely the opposite of what it now claims to be the case.'' Id. (emphasis in original). Determining that the trial court abused its discretion, the superior court opined that "the whole purpose of tenant estoppel certificates is to avoid the very situation that resulted in this lawsuit.'' *Liberty Property*, 815 A.2d at 1052. Shopping Center Legal Update Vol. 26 Issue 3 Fall/Winter 2006.

California

California courts have afforded estoppel certificates even greater weight than courts in other jurisdictions. In *Plaza Freeway Limited Partnership v. First Mountain Bank*, 81 Cal.App.4th 616 (2000), the landlord plaintiff and the defendant tenant were successors-in-interest to the original landlord and tenant under a 25-year commercial real estate lease. Prior to the time the plaintiff purchased the real property, the defendant signed and delivered an estoppel certificate, which affirmatively represented the lease expiration date to be October 31, 1998. When the defendant did not timely exercise an option to renew the lease and did not vacate the premises, the landlord commenced an unlawful detainer/eviction action against the tenant. Notwithstanding the tenant's estoppel certificate, the trial court concluded that the actual expiration date of the initial lease term was some eight months later. The court of appeal reversed, finding that the estoppel certificate was a "written instrument'' for evidentiary purposes under California law, and the tenant was estopped from contradicting the October 31, 1998, date in the estoppel certificate. The Plaza Freeway Court concluded that "estoppel certificates are almost always used in commercial real estate transactions. They inform lenders and buyers of commercial property of the tenant's understanding of the lease agreement. Lenders and buyers rely upon the certificates in finalizing loans and purchases. Thus, application of [California Evidence Code] Section 6221 to estoppel certificates would promote certainty and reliability in commercial transactions. A contrary conclusion would defeat the purpose behind the widespread practice of using estoppel certificates.'' *Plaza Freeway*, 81 Cal.App.4th at 628 B 629. The court of appeals in California further emphasized the breadth of issues affected by a tenant's estoppel certificate in Miner v. Tustin Avenue Investors LLC, 116 Cal.App.4th 264, 273 (2004) when it opined: Estoppel certificates are equally critical to landlords because they affect their ability to sell commercial real property and to secure financing. Estoppel certificates inform prospective buyers and lenders of the lessees' understanding of the lease agreement.

II. SUBORDINATION, NON-DISTURBANCE AND ATTORNMENT AGREEMENTS

A. Overview

A subordination, non-disturbance and attornment agreement ("SNDA") is an agreement between a mortgage lender and a tenant, which sets forth the relative rights and obligations of the parties in the event that the lender forecloses on the landlord's interest in the subject property. There are three main elements to an SNDA. First, a lender ensures that its mortgage will have priority over the lease (i.e., achieving subordination of the leasehold interest). Second, the tenant makes sure that its right to occupy the property pursuant to the lease will continue post-foreclosure (i.e., obtaining the lender's assurance of non-disturbance). Third, the lender gets a commitment from the tenant that, following a foreclosure, the tenant will recognize the lender as its landlord under the lease (i.e., getting the tenant's agreement of attornment). In connection with the parties' agreements respecting non-disturbance and attornment, the tenant will seek to preserve its rights under the lease to the greatest extent possible, and the lender will aim to limit its obligations and liabilities when it steps into the landlord's shoes.

The landlord/borrower may or may not be a party to the SNDA. The lender or tenant might want to include the landlord as a party to the agreement for the purpose of acknowledging certain terms thereof (e.g.,

acknowledging that the tenant will not be in default under the lease if it abides by a rent direction letter that the lender delivers). However, the SNDA, by its nature governs the relationship of the parties when the landlord has been foreclosed out of its interest. Therefore, the landlord is often not viewed as a necessary party to the document. The landlord's main objective in the negotiation of an SNDA is to facilitate an agreement between its lender and its tenant so that the landlord can complete its loan or lease transaction.

B. Subordination

Generally speaking, a mortgage will be subject to any prior leases of the mortgaged property. 54A Am. Jur. 2d Mortgages §164. However, landlords often include subordination clauses in their leases, whereby the tenant agrees that its lease shall be subject and subordinate to all current and future mortgages encumbering the property. For example, the lease might state:

> "Tenant agrees that: (i) this Lease is, and all of Tenant's rights hereunder are and shall always be, subject and subordinate to any mortgages, deeds of trust or ground leases pursuant to which Landlord has or shall retain the right of possession of the Premises or security instruments (collectively called "Mortgage") that now exist, or may hereafter be placed upon the Premises or the Shopping Center or any part thereof and to all advances made or to be made thereunder and to the interest thereon, and all renewals, replacements, modifications, consolidations, or extensions thereof; and (ii) if the holder of any such Mortgage ("Mortgagee") or if the purchaser at any foreclosure sale or at any sale under a power of sale contained in any Mortgage shall at its sole option so request, Tenant will attorn to and recognize such Mortgagee or purchaser as Landlord under this Lease for the remaining portion of the Term, subject to all terms of this Lease; and (iii) the aforesaid provisions shall be self-operative and no further instrument or document shall be necessary unless required by such Mortgagee or purchaser."

In cases where the tenant has strong bargaining power (and therefore the ability to either heavily negotiate the landlord's lease form or utilize its own form of lease), this clause may be eliminated, or the subordination of the lease may be conditioned on tenant's receipt of a non-disturbance agreement from the mortgagee. Such a negotiated clause might state that:

> "Notwithstanding the provisions of Section ___, the subordination of this Lease to future Mortgages shall be conditioned on Landlord's delivery to Tenant of a Subordination, Non-Disturbance and Attornment Agreement ("SNDA") from the holder of such Mortgage, in the form annexed hereto as Exhibit __ with such commercially reasonable changes as shall be requested by the Mortgagee provided such changes do not increase Tenant's obligations or decrease Tenant's rights from those set forth in the form of SNDA annexed hereto as Exhibit __, and Landlord will use commercially reasonable efforts to obtain same on behalf of Tenant."

If a lease is not automatically and unconditionally self-subordinating, a lender will likely require an SNDA from the applicable tenant. The tenant, in agreeing to subordinate its interest, should seek to clarify that it is subordinating only to the particular mortgage in question. The following is a typical SNDA subordination provision:

> "The Lease shall be subject and subordinate in all respects to the lien and terms of the Mortgage, to any and all advances to be made thereunder and to all renewals, modifications, consolidations, replacements and extensions thereof. This Agreement is not intended and shall not be construed to subordinate the Lease to any mortgage, deed of trust or other security instrument other than those expressly referenced in Paragraph __ of the preliminary statements of this Agreement."

Tenants with leases that include significant incentives such as extensive landlord improvements, free rent periods, rights to setoff, self help provisions, and tenant improvement allowances provided by the landlord must ensure that their leases are only subordinate to any mortgage upon receipt of a commercially reasonable SNDA that protects the tenant's right to receive the full value of the incentive negotiated in their lease.

C. Non-Disturbance

When a lease is subordinate to a mortgage, the tenant is in peril of losing its leasehold estate upon a foreclosure. Therefore, if a prior lease is being subordinated to a new mortgage, in return for agreeing to the subordination, a tenant will expect a promise of non-disturbance from the lender. If a lease with a substantial tenant is executed subject to an existing mortgage, the tenant might be able to condition the effectiveness of the lease on its receipt of an SNDA from the landlord's mortgagee. A lender does not want to be forced into keeping a problematic tenant at the property and therefore will require that, as a condition to non-disturbance, the tenant

must not be in default under the lease. Also, a lender might seek to preserve the procedural right to name the tenant in a foreclosure action, provided that it is not for the purpose of terminating the leasehold estate. Below is an example of a negotiated non-disturbance provision in an SNDA:

> "So long as Tenant is not in default (beyond any period given Tenant to cure such default) in the payment of rent or in the performance of any of the material terms, covenants or conditions of the Lease on Tenant's part to be performed (a) Tenant's possession and occupancy of the Demised Premises shall not be interfered with or disturbed by Lender during the term of the Lease or any extension thereof duly exercised by Tenant; (b) Lender will not name Tenant as a party to any judicial or non-judicial foreclosure or other proceeding to enforce the Mortgage unless joinder is required under applicable law but in such case Lender will not seek affirmative relief against Tenant, the Lease will not be terminated and Tenant's possession of the Demised Premises will not be disturbed; and (c) if Lender or any other entity acquires the Property through foreclosure, by other proceeding to enforce the Mortgage or by deed-in lieu of foreclosure or otherwise, Tenant's possession of the Demised Premises will not be disturbed and the Lease will continue in full force and effect between Lender (or such other entity) and Tenant."

D. Attornment

The final, basic element of an SNDA is the tenant's agreement to attorn to and recognize the lender (or another party acquiring the property in connection with a foreclosure or deed in lieu thereof) as its landlord under the lease. As discussed in more detail below, the tenant will seek to preserve as much of the benefit of its bargain with the original landlord as possible, while the lender will seek to limit certain of landlord's obligations and liabilities under the lease. A balanced attornment provision might read like this:

> "If the interests of Landlord under the Lease shall be transferred by reason of the exercise of any foreclosure or other proceeding for enforcement of the Mortgage, or by deed in lieu of foreclosure or such other proceeding, or if Lender takes possession of the Property pursuant to any provisions of the Mortgage or otherwise, Tenant thereafter shall be bound to Purchaser (hereinafter defined) or Lender, as the case may be, under all of the terms, covenants and conditions of the Lease for the balance of the term thereof and any extensions or renewals thereof which may be effected in accordance with any option therefor in the Lease, with the same force and effect as if Purchaser or Lender were landlord under the Lease, and Tenant does hereby attorn to Purchaser or Lender, as the case may be (if it takes title to or possession of the Property), as landlord under the Lease. Such attornment shall be effective and self-operative without the execution of any further instruments upon the succession by Purchaser to the interest of Landlord under the Lease or the taking of title to or possession of the Property by Lender. Nevertheless, Tenant shall, from time to time at no cost to Tenant, execute and deliver such instruments evidencing such attornment as Purchaser or Lender may reasonably require. The respective rights and obligations of the Purchaser, Lender and Tenant upon such attornment, to the extent of the then remaining balance of the term of the Lease and any extensions and renewals, shall be and are the same as now set forth in the Lease except as otherwise expressly provided in Section __ hereof. As used herein, the term "Purchaser" means any person acquiring the interest of Landlord under the Lease as a result of any foreclosure or other action or proceeding in the nature of foreclosure or by way of any deed in lieu of any such action or proceeding."

E. Limitations on Lender's Obligations and Liabilities

Although the lender agrees to be bound by the terms of the lease, the lender will seek to limit its exposure to various obligations and liabilities, including those that may have accrued under the watch of the original landlord (i.e., its defaulting borrower). From the lender's perspective, it agreed to make a loan and is only stepping into the landlord's shoes because of a default under that loan. The lender will be wary of incurring additional costs and expenses by virtue of succeeding to the landlord's position under the lease. The tenant, on the other hand, will take the view that it struck a bargain with the landlord and expects the benefit of that bargain. Therefore, the tenant will want to resist SNDA provisions that serve to modify the lease to the tenant's detriment, and the tenant will want to preserve its rights with respect to any breaches that continue after the lender has taken over the property.

In addition, the lender is agreeing to be bound by the provisions of the lease, as they exist when the SNDA is executed. The lender will seek protection against incurring obligations under any subsequent lease

amendments made by the tenant and landlord without lender's consent. However, it is in the tenant's interest to retain flexibility to address future situations that may warrant an amendment, with some assurance that the lender will be reasonable in approving and agreeing to be bound by same.

Below is a sample provision that reflects a compromise between the competing interest of lender and tenant when it comes to the limitations on lender's liability:

> "Neither the Purchaser nor Lender, however, shall be:
>
> (a) liable for any act or omission of Landlord, which was to have been performed under the Lease except that Tenant shall have the rights and remedies afforded to Tenant under the Lease with respect to any default relating to the construction, maintenance and repair obligations which are required to be performed by Landlord under the terms of the Lease;
>
> (b) liable for the return of any security deposit which Tenant under the Lease has paid to Landlord under the Lease, except to the extent that the amount thereof is turned over to Purchaser or Lender, as the case may be;
>
> (c) subject to any offsets or defenses which Tenant under the Lease might have against Landlord under the Lease;
>
> (d) bound by the payment of any basic rent, additional rent or any other payments (any and all of which are herein referred to as "Rent") which Tenant might have paid under the Lease for more than one month in advance to Landlord under the Lease, except with respect to estimated payments on account of Taxes and Operating Expenses to the extent actually paid to Landlord and to the extent provided in the Lease;
>
> (e) bound by any amendment or modification of the Lease made without Lender's prior written consent, which consent shall not be unreasonably withheld or delayed;
>
> (f) bound by any consent by Landlord under the Lease to any assignment of Tenant's interest in the Lease or any sublease of all or any portion of the Leased Premises made without Lender's prior written consent, which consent shall not be unreasonably withheld or delayed;
>
> (g) personally liable for any default under the Lease or the violation of any covenant or breach of any obligation on its part to be performed thereunder as successor to Landlord which first occurs prior to Lender's or Purchaser's taking of possession or ownership of the Property, it being acknowledged that Tenant's sole remedy in the event of such default shall be to proceed against Landlord to recover any monetary damages; provided, however that the foregoing shall not limit either (i) Tenant's right to exercise against Lender or Purchaser any offset right set forth under the Lease that relate to events occurring after Lender or Purchaser takes title to the Property or (ii) subject to the other provisions of this Agreement, Lender's or Purchaser's obligation to correct any conditions that existed as of the date Lender or Purchaser takes title to the Property that constitute a violation of the holder of the landlord's interest under the Lease;
>
> (h) liable for or deemed to incur any obligation with respect to any breach of warranties or representations of any nature of Landlord under the Lease or otherwise, including, without limitation, any warranties or representations of Landlord respecting use, compliance with zoning, Landlord's authority, habitability or fitness for any purpose or presence or absence of hazardous materials or substances, including petroleum products;
>
> (i) liable for any consequential or other damages which may have been incurred by Tenant by reason of any breach of obligations to be performed by Landlord;
>
> (j) liable for any leasing commissions, the triggering event for which arose prior to the date Lender or Purchaser succeeded to Landlord's interest; or
>
> (k) liable to Tenant hereunder or under the terms of the Lease beyond its interest in the Property and all rents attributable thereto."

F. Other SNDA Provisions

In addition to the foregoing provisions, an SNDA will frequently address one or more of the following issues:

- Purchase Rights and Options: If a tenant has any right or option to purchase the property, the lender will need to ensure that such right does not interfere with its ability to acquire the property following a default under the loan.

- Disposition of Casualty and Condemnation Proceeds: A provision relating to the disposition of casualty and condemnation proceeds can be one of the most contentious points in the negotiation of an SNDA. A lender typically has the right under its mortgage (subject to conditions specified therein) to apply such proceeds to the repayment of its loan. A tenant may have negotiated casualty and condemnation provisions in its lease that provide for the proceeds to be otherwise applied (e.g., to the restoration of the property). Resolution of this issue will come down to a variety of factors, including the relative bargaining strength of each party and the specifics of the operative provisions of the lease and mortgage. For example, a lender might take comfort if the lease provides that the landlord's obligation to restore is subject to the rights any mortgagee has or may have to the insurance proceeds.

- Notice and Opportunity to Cure Defaults: In large part, a mortgagee is lending against an underwritten income stream generated by the property. Any disruptions in the payment of rents could hamper its borrower's ability to repay the loan, causing problems for the lender. Therefore, a lender will request that the tenant provide it with copies of any notices sent to the landlord and an opportunity to cure landlord defaults before the tenant has a right to exercise remedies, including termination. The lender's preference will be to attempt to force its borrower to cure the breach, rather than expending the time, money and effort to cure, itself. Therefore, the lender will generally want an extended period of time (beyond the landlord's cure period) within which to cure the default, including any time required to gain possession of the property, if necessary. A tenant can be expected to resist any erosion of the rights and remedies that it negotiated under its lease and will often propose that, while it will accept cure of a default by lender, the lender will have the same period of time to effect the cure as the landlord has under the lease. A frequent compromise in this situation is for the lender to get an extended cure period, subject to an outside limit agreed upon by the parties. However, tenants should preserve any self-help rights to cure a landlord default as expressly negotiated in the lease and ensure that defaults resulting in an emergency situation are not subject to the same extended cure period as non-emergency defaults.

- Continuing Defaults: The landlord must remain responsible for continuing obligations under the lease. A typical definition of continuing obligations is, a default by landlord under the lease that began prior to the lender taking title, is ongoing and continuing following the change in title, is susceptible to being cured, and for which tenant provided lender with notice prior to change in title. In the case of a monetary continuing default, tenant's remedy is often limited to offsetting its rent next due and payable until such monetary continuing default is completely offset. Tenants must ensure that they preserve their self-help rights and carve out the lender's ability to veto permitted assignments of the lease that do not require landlord consent.

III. SUBLEASE RECOGNITION AGREEMENTS

A recognition agreement is an agreement between a prime landlord and a subtenant, which provides that if the prime lease between the prime landlord (as landlord) and the sublandlord (as tenant) terminates, the prime landlord will recognize the subtenant as its direct tenant, and the subtenant will be permitted to continue in occupancy of the premises. Since a subtenant's rights are derivative of its sublandlord's rights under the prime lease for the premises, a subtenant is in danger of losing its premises if the prime lease terminates for any reason. To address this risk, as a condition to entering into a sublease, particularly a sublease of a substantial amount of space at the property (e.g., a subtenant taking over all or a large portion of a former shopping center anchor's space), a subtenant may insist on the delivery of a recognition agreement by the prime landlord.

A prime landlord will likely be reluctant to agree in the prime lease that it will grant a recognition agreement to a hypothetical subtenant. The prime landlord's preference would be to weigh any such request on a case-by-case basis at the time when there is an actual sublease, with an actual subtenant to evaluate. In cases where a tenant is able to obtain the prime landlord's prior agreement to execute a recognition agreement with a subtenant, the prime landlord will want to ensure, among other things, that if the sublease is for less than all of the premises demised under the prime lease, the remaining space will be rentable. So, there will often be conditions imposed. For example, a prime landlord might not agree in advance to execute a recognition agreement unless the subleased premises contain a minimum square footage; any remaining (non-subleased) space shall be configured so as to satisfy criteria to ensure it is leasable; and each resulting space is separately demised with its own separate utilities and entrance.

In cases where a prime landlord is not required by the prime lease to grant a recognition agreement to a subtenant, upon request the prime landlord may still decide that it is in the prime landlord's interest to execute a recognition agreement and establish privity with a subtenant. The prime landlord may arrive at this conclusion, considering a variety of factors, including market conditions, the terms of the proposed sublease, the prime landlord's relationship with the prime tenant (i.e., the sublandlord) and the financial standing of the prime tenant and subtenant.

In cases where a prime landlord ultimately agrees to execute a recognition agreement, the parties will likely request a number of provisions in addition to the basic agreement that a termination of the prime lease will result in a direct lease relationship between the subtenant and the prime landlord. For instance, the subtenant will want the prime landlord to confirm items such as the list of all prime lease documents, that no defaults exist under the prime lease, what the use restrictions applicable to the shopping center are and that the subtenant will have rights to the common areas. A prime landlord will seek to address concerns similar to those of a lender executing an SNDA. For example, the prime landlord will not want to be subject to any offsets or defenses that the subtenant may have against the sublandlord, liable for the return of any security deposit not actually received by the prime landlord or bound by any sublease amendments executed without prime landlord's consent.

Attached hereto as Schedule 1 is a basic form of recognition agreement that addresses core issues that will be important to a prime landlord and a subtenant. However, all prime leases and subleases are different, and will have their own unique terms and circumstances to be addressed. Therefore, any form of recognition agreement will need to be tailored to address property-specific and transaction-specific issues.

SCHEDULE 1

(SPACE ABOVE RESERVED FOR RECORDER'S USE)

Record and Return To: This Instrument Prepared By:

RECOGNITION AGREEMENT

THIS RECOGNITION AGREEMENT, made as of the ___ day of _____, 20___, between _____, _____, a _____, having an address at _____, _____ ("Fee Owner"), and _____, a _____, having an address at _____ ("Subtenant").

RECITALS

A. Fee Owner is lessor under a certain lease dated _____ (the "Prime Lease") with _____, as lessee ("Sublandlord") which demises certain premises consisting of approximately _____ square feet located within _____ Shopping Center (the "Shopping Center") which Shopping Center is further described in Exhibit B attached hereto, with an address of _____ (the "Premises") more particularly described in the Prime Lease. The documents comprising the Prime Lease are set forth on Exhibit A annexed hereto and made a part hereof.

B. Pursuant to a Sublease dated _____ (the "Sublease"), Sublandlord subleased a portion of the Premises consisting of approximately _____ square feet (the "Subleased Premises") to Subtenant.

NOW THEREFORE, in consideration of the mutual promises and undertakings hereinafter set forth and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged the parties hereto hereby agree as follows:

1. Fee Owner warrants and represents, to the best of Fee Owner's knowledge, as follows:

(a) that Fee Owner is the fee simple owner of the Premises and has the full authority to execute this Recognition Agreement;

(b) that the Prime Lease is unmodified and in full force and effect, and that the documents comprising the Prime Lease consist of only those documents set forth on Exhibit A;

(c) that neither Fee Owner nor Sublandlord are in default under the Prime Lease, nor has any event occurred which would, after notice to Sublandlord and the passage of any applicable cure period, become a default of Sublandlord under the Prime Lease; and

(d) [the restrictions contained in Exhibits __ (Prohibited Uses) and __ (Exclusive Uses) attached to the Sublease constitute all of the use restrictions applicable to the Shopping Center as of the date hereof].

2. For so long as the Sublease remains in full force and effect, and provided Subtenant is not in default in the performance of the obligations on Subtenant's part to be performed under the Sublease, after the receipt of notice thereof and the expiration of any applicable cure period, Fee Owner shall not, in the exercise of any of the rights arising or which may arise out of the Prime Lease or of any instrument modifying or amending the same or entered into in substitution or replacement thereof, disturb or deprive Subtenant in, or of, its possession or its right to possession of the Subleased Premises or of any interest, right or privilege granted to or inuring to the benefit of Subtenant under the Sublease.

3. Fee Owner hereby acknowledges receipt of a copy of, and consents to, the Sublease. The Sublease is expressly made subject and subordinate to all of the terms, covenants, conditions and provisions contained in the Prime Lease and to any and all amendments, modifications, revisions now or hereafter made thereto.

4. In the event of the termination of the Prime Lease by reentry, notice, conditional limitation, surrender, summary proceeding or other action or proceeding, because Sublandlord or Fee Owner has exercised an option to terminate or reject the Prime Lease, by operation of law, by mutual agreement between Fee Owner and Sublandlord, or otherwise, or if the Prime Lease shall expire for any reason before any of the dates provided in the Sublease for the termination or expiration of the initial or renewal terms of the Sublease, and if immediately prior to such surrender, termination or expiration of the Sublease shall be in full force and effect and Subtenant is not in default in the performance of the obligations on Subtenant's part to be performed after the receipt of notice thereof and the expiration of any applicable cure period:

(a) Subtenant shall not be made a party in any removal or eviction action or proceeding nor shall Subtenant be evicted or removed of its possession or its right of possession be disturbed or in any way interfered with, and

(b) the Sublease shall continue as a direct lease between Fee Owner and Subtenant for the remainder of the term of the Sublease without the necessity of executing a new Sublease, or the same terms and conditions as are in effect under the Sublease immediately preceding the termination of the Prime Lease.

5. Notwithstanding any provision hereof to the contrary, in no event shall Fee Owner be:

(a) liable for any default, act or omission of any sublandlord under the Sublease;

(b) subject to any offset or defense which Subtenant may have against any sublandlord under the Sublease;

(c) bound by any payment of rent or additional rent made by Subtenant more than 30 days in advance;

(d) bound by any modification or supplement to the Sublease, or waiver of Sublease terms, made without Fee Owner's written consent thereto;

(e) liable for the return of any security deposit or other prepaid charge paid by Subtenant under the Sublease, except to the extent such amounts were actually received by Fee Owner;

(f) liable for any payment to be made to Subtenant under the Sublease; or

(g) liable for construction or completion of any improvements to the Subleased Premises.

6. As a condition of and in consideration for Subtenant's execution of the Sublease and this Recognition Agreement, Fee Owner agrees with Subtenant, and as a direct contractual agreement with Subtenant, that:

(a) Fee Owner grants to Subtenant all rights, privileges, easements and licenses to the common areas of the Shopping Center.

(b) Fee Owner shall maintain the common areas of the Shopping Center as specified in the Prime Lease.

7. [Fee Owner expressly approves Subtenant's plans and specifications for Subtenant's initial alterations as described in Subtenant's plans designated as: _____, dated _____, and prepared by _____. Further, Fee Owner approves Subtenant's signage attached as Exhibit ___ to the Sublease.]

8. [With respect to Section ___ of the Prime Lease or any other express or implied provision regarding continuous operation or a right of recapture to Fee Owner based upon a cessation or lack of operations at the Subleased Premises, the violation of any continuous operation requirement or the exercise of any recapture right will not be based upon any lack or cessation of operations at the Subleased Premises which occurs prior to the date of this Recognition Agreement or which subsequently results from the demolition, design or remodeling of the Subleased Premises in preparation for Subtenant's opening for operation in the Subleased Premises.]

9. Fee Owner agrees that whenever it has an obligation with respect to the Subleased Premises, or its consent or approval is required for any action on behalf of Sublandlord under the Prime Lease, then, to the extent such obligation, consent or approval relates to the Subleased Premises or Subtenant's use and occupation

thereof, it will perform such obligation and will not unreasonably withhold or unduly delay such consent or approval.

10. Fee Owner hereby subordinates to any lender of Subtenant any and all rights or remedies against Subtenant, pursuant to any lien, statutory or otherwise, that it may have against the personal property, goods or chattels of Subtenant in or on the Subleased Premises.

11. This Recognition Agreement contains the entire agreement between the parties and cannot be changed, modified, waived or canceled except by an agreement in writing executed by the party against whom enforcement of such modification, change, waiver or cancellation is sought.

12. Invalidation of any of the provisions contained in this Recognition Agreement, or of the application thereof to any person judgment or court order shall in no way affect any of the other provisions hereof or the application thereof to any other person and the same shall remain in full force and effect.

13. This Recognition Agreement and the covenants herein contained are intended to run with and bind all lands affected thereby.

14. This Recognition Agreement may be executed in several counterparts, each of which shall be deemed an original. The signatures to this Recognition Agreement may be executed and notarized on separate pages, and when attached to this Recognition Agreement shall constitute one complete document.

15. This Recognition Agreement shall be interpreted in accordance with the laws of the State of _____.

16. This Recognition Agreement shall be binding on and shall inure to the benefit of the parties hereto and their respective heirs, legal representatives, successors and assigns.

17. Any notice or demand in connection with this Recognition Agreement shall be in writing and shall be forwarded by registered or certified mail, return receipt requested, or by nationally recognized courier service providing written confirmation of delivery, to the addresses of the parties specified above. Notice shall be deemed to have been given or served on the delivery date indicated by the United States Postal Service or courier service on the return receipt or on the date such delivery is refused or marked “undeliverable.” Either party may change its address by providing written notice as specified herein; provided, however, all addresses provided must be the actual street address of a residence or business establishment. The foregoing method of service shall be exclusive, and Subtenant and Sublandlord waive, to the fullest extent permitted under law, the right to any other method of service required by any statute or law now or hereafter in force. Whenever multiple notices are sent or multiple methods of transmitting any notice are utilized, any time period that commences upon the giving or deemed giving of such notice shall commence upon the earliest date such delivery is effectuated, and such time shall not be extended by operation of law or otherwise because of any later delivery of the same notice.

18. If either party brings an action or proceeding to enforce the terms hereof or declare rights hereunder, the prevailing party in any such action or proceeding shall be entitled to recover its reasonable attorneys’ fees.

[NO FURTHER TEXT ON THIS PAGE]

IN WITNESS WHEREOF, the parties have caused this instrument to be executed on the date first above written.

FEE OWNER:

By: _____
Name: _____
Its: _____

SUBTENANT:

By: _____
Name: _____
Its: _____

[INSERT APPROPRIATE NOTARY BLOCKS]

[ATTACH EXHIBITS A AND B]