# Commercial Lease Defaults: when the money's gone

Robert Nix
Lawrence Shoffner

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**Robert R. Nix II** is a member with the Detroit law firm of Kerr, Russell and Weber, PLC and specializes in the practice of real estate law, commercial law and commercial litigation. He is a regular speaker for seminars for the Institute of Continuing Legal Education and the Homeward Bound series for the Real Property Law Section of the State Bar. These presentations have included a variety of real estate subjects, including commercial purchase agreements, mixed used developments, reciprocal easement agreements, mortgages and land contracts, lender liability and usury. He is a past chairperson of the Real Property Law Section and is a member of the Michigan Land Title Standards Committee, American College of Real Estate Lawyers, American College of Mortgage Attorneys, a Fellow of the Michigan State Bar Foundation and a variety of other real estate related organizations.

Contact:

Kerr, Russell & Weber PLC

One Detroit Center

500 Woodward Avenue, Suite 2500

Detroit, MI 48226

313.961.0200

rrn@krwlaw.com

**Lawrence Shoffner** practices in the areas of commercial leasing and real estate related litigation. He is a past Chairman of the Real Property Law Section of the State Bar of Michigan; a member of the Section's Council since 2000; a past Chairman of the Section's Special Committee on Commercial Leasing; and a current member of the SBM Publications and Website Advisory Committee. Mr. Shoffner is co-author of ICLE's *Michigan Lease Drafting and Landlord-Tenant Law* and the author of numerous articles on commercial leasing and real estate related litigation for the *Michigan Real Property Review* and *Michigan Bar Journal.* He is a frequent speaker for ICLE and other organizations, including the American Bar Association, the Building Owners and Managers Association, and the International Council of Shopping Centers; a member of ICLE's Executive Committee; a member of ICLE's Real Estate Advisory Board; and a long time contributor to ICLE's online FormBank.

Contact:

Lawrence Shoffner, Esq

353 Griswold Street, Suite 1550

Detroit, MI 48226

313.806.0076

Law@LawrenceShoffner.com

# Commercial Lease Defaults

Value of Possession (when the money's gone)

- Landlord's perspective: Sometimes any tenant is better than no tenant
- Tenant's perspective: Customers, equipment & disruption
- Lender's perspective: all money is good

Commercial Lease Defaults

Landlord Defaults (when the money's gone)

- Maintenance & Repair
- Mortgage Defaults - Foreclosure
- Real Estate Taxes - Forfeiture
- Bankruptcy

**Maintenance & Repair**

- The nature and scope of the landlord's maintenance and repair obligations are dependent upon whether the lease is a triple net lease, modified net lease or a gross lease.
- Does the landlord's failure to perform maintenance or repairs (1) constitute a material breach of the lease, (2) result in a violation of building and use codes, environmental laws or other laws, or (3) result in personal injuries or property damage which may be covered by liability insurance carried by either the landlord or tenant?
- Does the lease provide landlord with notice and cure opportunities before the maintenance and repair failure constitutes a default under the lease?
- A breach by landlord of its covenant to repair the premises may give the tenant the right to either abandon the premises and terminate the lease if the tenant is unable to beneficially use and enjoy the premises or make the required repairs and set off the cost of repairs against rent. *Lynder v SS Kresge Co,* 329 Mich 359 (1951); *Anchor Inn of Michigan, Inc v Knopman*, 71 Mich App 64 (1976).

**Mortgage Defaults – Foreclosure**

- Under the common law, a covenant of quiet enjoyment was implied in every lease. *Grinnell Bros v Asiuliewicz*, 241 Mich 186 (1927). The covenant of quiet enjoyment is an agreement that the tenant will not be dispossessed by the landlord or any party claiming through the landlord, such as a mortgagee. If there is no redemption by landlord or a subordination, non-disturbance and attornment agreement between the lender and the tenant, the foreclosure of a prior mortgage terminates all junior interests, including leases. *Dolese v Bellows-Claude Neon Co*, 261 Mich 57 (1933).

**Real Estate Taxes – Forfeiture**

- Unless otherwise provided in the lease, the tenant has no obligation to pay real estate taxes, which are the obligation of the landlord. *Wycoff v Gavriloff Motors, Inc*, 362 Mich 582 (1961).

**Bankruptcy**

- If the landlord is the debtor, there is no Code section governing the time for assumption or rejection which may permit the landlord to reject the lease anytime during the bankruptcy.
- If the landlord assumes the lease, the landlord must cure and provide adequate assurance of future performance.
- If the landlord terminates the lease and the rejection constitutes a breach entitling the tenant under non-bankruptcy law to terminate the lease, the tenant may treat the lease as terminated by the rejection or retain its rights under the lease (including possession and offset rent against any damage or nonperformance by the landlord).

## Commercial Lease Defaults

Tenant Defaults (when the money's gone)

- Nonpayment of Rent
- Abandonment / Going Dark
- Surrender
- Prohibited Transfer
- Bankruptcy

**Nonpayment of Rent**

- Rent may include taxes, insurance, and operating expenses. Unless a lease provides tenant with the right to audit and challenge operating expenses, nonpayment after any contractual notice and cure period will constitute a default.
- Unless the lease provides otherwise, landlord's use of a security deposit to pay any unpaid rent may result in a cure of the default.

**Abandonment / Going Dark**

- Unless the lease includes an operating covenant, the failure to occupy or operate may not constitute a default if rent is paid and other obligations performed by the tenant. In addition, the tenant may negotiate a "go dark" provision.
- Abandonment of the right of occupancy under a lease requires both proof of intent to abandon and acts of abandonment and mere non-use will not create a presumption of abandonment. *Fera v Village Plaza, Inc,* 52 Mich App 532 (1974); *McPheeters v Birkholz,* 232 Mich 370 (1925).
- Abandonment by the tenant does not extinguish the tenant's liability for future rent. *Scott v Beecher,* 91 Mich 570 (1982). If re-rental results in a lower rental payment, the abandoning tenant is liable for the difference in rent. *Stewart v Sprague,* 71 Mich 50 (1888).

**Surrender**

- A valid surrender operates to terminate a lease and the tenant's obligation to continue paying rent. *Pyle v Orzell,* 350 Mich 298 (1957).
- A valid surrender requires a finding that the landlord accepted the tenant's offer of a surrender. *Michigan Lafayette Building Co v Continental Bank,* 261 Mich 256 (1933). Mere acceptance of keys to a leased premises does not constitute a surrender by operation of law. *Bates v Smith,* 259 Mich 454 (1932).
- If the remaining balance of the lease term is more than one year, the surrender must be in writing to comply with the Statute of Frauds. *Barth v Womens' City Club,* 254 Mich 270 (1931).

**Prohibited Transfer**

- Unless the lease provides otherwise, common law permits the tenant to freely sell or assign the lease or sublet the premises. *Patterson v Butterfield*, 244 Mich 330 (1928)

**Bankruptcy**

- If the tenant is the debtor, the tenant has 120 days to assume or reject lease and can get up to a 90 day extension. No more extension permitted without landlord's approval.
- If the tenant assumes the lease, the tenant must cure and provide adequate assurance of future performance. The tenant is now bound by lease and all obligations or liabilities of tenant become an administrative claim of estate.
- If the tenant rejects lease, such rejection acts as a breach of the contract the moment before bankruptcy filing and landlord becomes a general unsecured creditor. The landlord's damage claim against the tenant is limited to the rent reserved (without acceleration) for the greater of one year or 15%, not to exceed 3 years of the remaining lease term.

## Commercial Lease Defaults

### Landlord Remedies (when the money's gone)

- Self Help & Lockout
- Eviction - Summary Proceedings
- Rent & Damage Actions - Rent Acceleratio
- Guaranty Actions
- Other Remedies

**Self Help & Lockout**

- Michigan law has effectively eliminated self-help repossession by the landlord. *Deroshia v Union Terminal*, 151 Mich App 715, 719 (1986). A wrongfully dispossessed tenant can obtain a judgment against the landlord for actual damages, treble damages, and even exemplary damages. MCL 600.2918.

**Eviction – Summary Proceedings**

- Michigan's Summary Proceedings Act (MCL 600.5701, *et seq*) provides a fast and simple procedure for the recovery of real property, particularly where the action is based on non-payment of rent. The procedures for eviction are set forth in the Summary Proceedings Act and Michigan Court Rule 4.201. In most instances, an eviction for non-payment can be completed in about a month. If the tenant appears and raises a factual defense or demands a jury, the period can easily become several months.
- Under common law the landlord has no claim for rent accruing after an eviction which terminates the lease. *Wreford v Kenrick,* 107 Mich 389 (1995). This rule can be modified in a written lease. *Stott Realty Co v Amusement Co,* 195 Mich 684 (1940); *Brochert v Sunset Shores*, 181 Mich App 676 (1989).

**Rent & Damage Actions – Rent Acceleration**

- In the context of the lease of an advertising sign, a rent acceleration clause is enforceable. *Walker v Harrison,* 347 Mich 630 (1957). The courts have yet to address rent acceleration clauses in real estate leases.
- Is accelerated rent and possession an unenforceable penalty? A landlord recovering possession of the leased premises was also permitted to collect accelerated rent for the balance of the lease term as " liquidated damages". *Cummings Properties, LLC v National Communication Corp*, 449 Mass 490 (2007).
- Recoverable damages equal the excess of the agreed rent over the rental value of the property, or the rent the landlord could obtain for the property through reasonable diligence. *Tel-Ex Plaza, Inc v Hardees*, 74 Mich App 131 (1977).

**Guaranty Actions**

- Lease guaranties are enforceable under Michigan law. However, "[a] guarantor may assert both the defenses available to the primary obligor regarding the principal obligation on the debt and any personal defenses that arise out of the guaranty obligation." 11 *Mich Civ Jur. Guaranty* § 27 (West); *In re Allied Supermarkets, Inc.*, 951 F2d 718, 728 (6th Cir 1991) (construing Michigan law).

**Other Remedies**

- Injunctions, declaratory relief and other equitable relief is available since the district courts have equitable jurisdiction. MCL 600.2918, MCL 600.2932(i), and *BeBruyn Produce v Romero,* 202 Mich App 92 (1993).

## Commercial Lease Defaults

Tenant Remedies (when the money's gone)

- Contract Remedies
- Damage Actions
- Self Help - Rent Setoff
- Termination & Vacating the Premises
- Other Remedies

**Contract Remedies**

- Unless the tenant has negotiated specific remedies for the landlord's breach of contract, the tenant is limited to the remedies provided by law.

**Damage Actions**

- Unless the lease provisions limit the nature and type of recoverable damages, damages arising from the breach and special damages within the contemplation of the parties may be recovered. *Wolf v Megantz,* 184 Mich 452 (1915).
- The tenant's recovery of damages for lost profits, physical damage, etc., will be subject to mitigation under general contract and damage principals.
- Tenant may recover actual damages and treble damages if the landlord uses self-help in lieu of the judicial process to forcibly dispossess the tenant. *Deroshia v Union Terminal Piers,* 151 Mich App 715 (1986).

**Self Help – Rent Setoff**

- Under common law all lease covenants were independent and a breach by the landlord did not justify a rental setoff by the tenant. *Reaume v Wayne Circuit Judge*, 299 Mich 305 (1941).
- The common law rule may be subject to question since the Court of Appeals upheld a commercial tenant's right of a rental offset based on a landlord's breach of the covenant of repair. *Anchor Inn v Knopman,* 71 Mich App 64 (1976).

**Termination & Vacating the Premises**

- When a landlord materially breaches the lease, the tenant is entitled to terminate it without liability. *Karpp* v *Royer, 362* Mich 64, 68 (1960).
- Constructive eviction (whether or all or a portion of the premises) terminates the obligation to pay rent, if the tenant abandons the premises within a reasonable time. *Kuschinsky v Flanigan,* 170 Mich 245 (1912); *Panagos v Fox,* 310 Mich 157, 161 (1944).
- Untenantable buildings statute. MCL 554.201.
- Termination rights permitted at law may be undermined by specific lease provisions prohibiting any right of termination by the tenant.

**Other Remedies**

- Injunctions, declaratory relief and other equitable relief is available since the district courts have equitable jurisdiction. MCL 600.2918, MCL 600.2932(i), and *BeBruyn Produce v Romero,* 202 Mich App 92 (1993).

## Commercial Lease Defaults

Mitigation (when the money's gone)

- Landlord Mitigation
- Tenant Mitigation
- Real Estate Principles / Contract Principles

**Landlord Mitigation**

- Rent claims are accorded a unique status when it comes to mitigation. Under common law, a lease is treated as a conveyance of real property for a specified duration. *Lipsitz v Schechter*, 377 Mich 685, 687 (1966). Because the lease is treated as a conveyance, the landlord has no duty to mitigate in an action to collect rent. *M & V Barocas v THC, Inc,* 216 Mich App 447 (1996); *Winshall v Ampco Auto Parks, Inc*, 417 F Supp 334 (1976).
- In *Frohling v Bischoff*, 73 Mich App 496 (1977) and *Jefferson Development v Heritage Cleaners*, 109 Mich App 606 (1981) the Michigan Court of Appeals imposed the obligation to mitigate damages on the landlord when the tenant vacated/abandoned the premises and stopped paying rent.
- There is no obligation, however, to mitigate damages arising out of a wrongful holdover by the tenant. *McCullagh v Goodyear Tire & Rubber Co*, 342 Mich 244, 356 (1955).
- One court's effort to harmonize the distinction between these mitigation rules is found in *In re Palace Quality Servs Indus*, 283 BR 868, 885 (Bankr ED Mich 2002).

**Tenant Mitigation**

- Except as mitigation is applied under contract/damage principles, no specific case law requiring mitigation by the tenant.

**Real Estate Principles / Contract Principles**

## Commercial Lease Defaults

Assessing the Position (when the money's gone)

- Lease Default Provisions
- Tenant/Guarantor Collectability
- Realistic Alternatives

**Lease Default Provisions**

**Tenant/Guarantor Collectability**

**Realistic Alternatives**

## Commercial Lease Defaults

Workouts (when the money's gone)

- Forbearance & Rent Abatement Agreements
- Termination & Surrender Agreements
- Lease Amendments

**Forbearance & Rent Abatement Agreements**

- Confirm inability to pay

**Termination & Surrender Agreements**

- Deliver of possession/subtenant issues
- Surrender payments.
- Condition of leased premises.
- Unknown liabilities.

**Lease Amendments**

- Agreements to amend a lease are generally controlled by statute. MCL 566.1. This statute has been construed as requiring either consideration or a writing, but not both. *Green v Millman Bros, Inc*, 7 Mich App 450 (1967); *Minor-Dietiker v Mary Jane Stores, Inc*, 2 Mich App 585 (1966).

## Commercial Lease Defaults

- Conclusions

When the money's gone
Will you be my friend
Float a small row boat
till our ship comes in

## Commercial Lease Defaults (when the money's gone)

Cher: "When The Money's Gone" Songwriters: Bruce Roberts & Donna Terry Weiss

When the money's gone
Will you be my friend
Float a small row boat till our ship comes in
When the winter nights chill us to the soul
Will you feed the fire
Spin the straw to gold
When the money's gone

When the money's gone
Will you get cold feet
Will you still be there if the ends don't meet
If we're in the red, just forget the green
Take a bus with me
No more limousines
When the money's gone
Will you still want me

*[Chorus:]*
Oh what a fine life I give to you
All you ever want
Will you still be there
Will you pull me through when the cash don't come
And if you're mine
Will you still love me wherever we fall
When the money's gone

Oh, will you want me baby
Oh, will you need me baby
Oh, will you love me baby
When the money's gone
Money, money, money's gone

When the money's gone
No more caviar
Will you eat fast food in a beat up car
Live life modestly, lost in lotto dreams
Will you find your way through it all with me
Through it all with me

*[Chorus (+repeat)]*
And a mile off the shore
Flies a bird who'll land no more
As the tide pulls the sea
So you always will pull me
forever more

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The following materials were adapted from Chard & Shoffner, *Michigan Lease Drafting and Landlord-Tenant Law*, copyright c 2002-2010, The Institute of Continuing Legal Education, Ann Arbor, Michigan; and from Shoffner, "Evictions: A Basic Roadmap for Handling Nonpayment Actions," *Michigan Bar Journal* (December 2003).

## I. LANDLORD'S REMEDIES

This section reviews the common law and statutory remedies available to the landlord for breach of lease. In many cases these remedies can be modified, expanded or negated by agreement of the parties, so it is important to start any analysis by reading the lease. The remedies examined here include: (a) self-help; (b) eviction; (c) rent actions; (d) damage actions; (e) equitable remedies; (f) recourse against security; and (g) recourse against guarantors.

### A. SELF HELP

Michigan law has effectively eliminated self-help repossession by the landlord. *Deroshia v Union Terminal*, 151 Mich App 715, 719 (1986). A wrongfully dispossessed tenant can obtain a judgment against the landlord for actual damages, treble damages, and even exemplary damages. MCL 600.2918; *Shaw v Cassar*, 558 F Supp 303 (ED Mich 1983) (exemplary damages). These damages may be recovered even if the landlord was legally entitled to the premises. *Deroshia, supra.*

The current status of Michigan law is considerably different from that which existed under early common law and which still exists today in the majority of other jurisdictions. Under common law, the landlord was allowed to use reasonable force to remove tenants. *Deroshia, supra.* The Michigan legislature originally modified this rule to prohibit forceful repossession by the landlord, regardless of the propriety of the tenant's possession. *Id.* In 1977, the statute was further amended to virtually eliminate self-help. MCL 600.2918.

Under MCL 600.2918 (1) it is unlawful to use force or threat of force to evict the tenant. Additionally, the landlord is prohibited from terminating or interrupting essential services such as heat, water, electric or gas, or by using noise, odor or other nuisances to demean the premises. MCL 600.2918 (2). The landlord cannot change, alter, or add locks, or board up the premises to prevent entry. *Id.* Moreover, the landlord may not remove, retain, or destroy the tenant's personal property. *Id.*

The prohibition against interference is so broad that it is actually much easier to consider those instances where the landlord may act. Specifically, there are three instances where the landlord may lawfully interfere with the tenant's right to possession. The statute exempts the landlord from liability if the landlord: (1) acted pursuant to court order; or (2) interfered temporarily with possession only as necessary to make needed repairs or inspection and only as provided by law; or (3) believed in good faith the tenant had abandoned the premises, and after diligent inquiry had reason to believe the tenant does not intend to return, and current rent is not paid. MCL 600.2918(3). If the landlord acted pursuant to a court order, the legal soundness of the order is

irrelevant. *Robinson v Michigan Consol Gas Co*, 918 F2d 579 (6th Cir 1990) (construing MCL 600.2918). However, the immunity extended by the statute is not unlimited. *Sickles v Hometown America, LLC*, 477 Mich 1076 (2007). Unless the landlord can demonstrate one of three exceptions, interference with the tenant's possession is unlawful. MCL 600.2918 (4) grants injunctive relief to the tenant to regain possession, which may be joined with its claim for damages. Actions under the statute are, however, restricted by a very short statute of limitations: 90 days to commence an action for possession and 1 year for damages. MCL 600.2918 (6).

Self-help is one area where the landlord is unable to enhance its position through creative drafting. MCL 600.2918(5) provides that the statutory provisions against self-help may not be waived. In summary, unless the tenant abandons the premises, there is no effective method to legally regain possession, except by court order. Because the sanctions are serious, it is incumbent for the landlord to obtain court approval prior to undertaking any action which may interfere with the tenant's possession.

## B. RENT ACTIONS (POSSESSION JUDGMENTS)

Michigan's Summary Proceedings Act (MCL 600.5701, *et seq*) provides a fast and simple procedure for the recovery of real property, particularly where the action is based on non-payment of rent. The procedures for eviction are set forth in the Summary Proceedings Act and Michigan Court Rule 4.201. The Court Rule provides direction on everything from the preparation of the complaint to the filing of the appeal. The State Court Administrative Office (SCAO) has prepared a corresponding series of special forms for use in eviction actions, copies of which can be found near the end of the Handbook. There is an SCAO form for: (a) the demand for possession; (b) the complaint; (c) the summons; (d) escrow orders; (e) the judgment of possession and (f) the order of eviction. These forms can be obtained from the court clerk, but they are also available at the Michigan Courts website (http://courts.mich.gov). In addition to convenience, there are important reasons to use the SCAO forms. The judges and court clerks are familiar with these forms and will expect to see them used. Moreover, the forms are specially designed to comply with the requirements imposed by the Summary Proceedings Act and the Michigan Court Rules. Many of these requirements have been incorporated into the approved forms, thereby helping to ensure compliance.

### 1. EVICTION TIMELINE

The first question typically asked by the landlord is this: how long will it take to evict the tenant for non-payment of rent? In most instances, an eviction for non-payment can be completed in about a month. If the tenant appears and raises a factual defense, the period can easily become several months. If the

tenant prevails on its defense, it may ultimately remain in possession until the end of its term. The following timeline will help to provide an overview.

If the landlord elects to serve by mail, the eviction process starts on Day Zero with service of the demand. Slightly more than a week must pass between the mailing of the demand and the filing of the complaint. Although the action begins with a “7-day" demand, the actual period is usually longer due to the additional time requirements imposed by various Court Rules (see, MCR 1.108(1)). The demand period usually runs to around Day 8.

After the demand period has elapsed, the complaint can be filed. In most district courts the court clerk schedules the matter for trial when the complaint is filed. The period between the filing of the complaint and the initial trial date is generally within 10 days. This period may be modified by local court rule (MCL 600.5735(4)). The following district courts have adopted such rules: 1st, 2A, 12th, 18th, 27-2nd, 81st, 82nd and 95-B. This period may have to be extended, however, if the summons and complaint cannot be served on the tenant at least 3 days before the scheduled trial date (MCL 600.5735(2)(b)). The initial trial date is generally around Day 17.

If the initial trial date results in a judgment, there is an additional 10-day period in which the tenant may redeem its leasehold by paying the delinquent rent (MCL 600.5744(a). If the rent is not paid, the landlord may apply to the court for an order of eviction. The order of eviction is usually entered around Day 28. If the tenant doesn’t move, the court officer must make arrangements with the landlord for the eviction. This will take some additional time, but the period is typically days rather than weeks. Because the tenant usually pays the rent or moves out before being physically evicted, the matter is often resolved in less than a month.

If the tenant appears on the initial trial date with a factual defense, the process can take substantially longer. By raising a defense and filing a jury demand, the tenant can prolong the procedure, perhaps by several months. Although the Court Rule requires the action to be tried within 56 days (MCR 4.201(J)(1)), this mandate is not always honored, particularly in commercial cases. After the judgment is entered, the tenant has the right to appeal, which can take another couple of months. All told, a non-payment action can take less than a month or as long as a year, depending on the nature of the defense and how hard the tenant fights. With this overview in mind, we turn to the details of the procedure.

## 2. EVICTION PROCEDURE

**Preparation for eviction:** For attorneys, the initial step in the eviction process is to gather information and documents, beginning with the demand and lease. If the landlord has already served the demand, it should be reviewed to ensure that it was properly prepared and served. If there is a written lease, double check the notice and remedy provisions. The landlord's attorney should request a copy of all communications between the parties. An exchange of hostile correspondence is often a sign that the issues will extend beyond the simple inability to pay. Knowledge gleamed from such correspondence will give the attorney some forewarning of issues that may be raised on the initial trial date.

**Demand for possession:** A "Demand for Possession Non-Payment of Rent" (DC 100a) is the SCAO form required to start a non-payment action (MCL 600.5714(1)(a)). Do not confuse this form with those required to commence alternative types of actions, such as the notice to quit form used in termination actions. The Summary Proceedings Act is very specific about the contents of the demand (MCL 600.5716). The demand must (a) be in writing, (b) be addressed to the person in possession, (c) state the address or brief description of the premises, (d) state the reasons for the demand, (e) state the amount due, and (f) indicate the time allowed to take remedial action. The demand must be dated and signed by the landlord, its attorney or agent. If the demand is being sent to a residential tenant, it should be signed and served by the landlord, rather than its attorney, to avoid problems under the Fair Debt Collection Practices Act, which imposes a number of additional requirements on the collection process. More information about the FDCPA requirements can be found in "Michigan Summary Proceedings and the Fair Debt Collection Practices Act: A Sea Change for Landlord's Lawyers?" 26 *Michigan Real Property Review* 31 (1999). Additionally, because the SCAO form consists of several pages, it is important for the landlord to serve the "tenant's copy" which states "How to Get Legal Help" and retain the copy containing the "proof of service".

There are several ways in which the demand may be served (MCL 600.5718). The demand may be served by delivering it personally to the tenant. Alternatively, the demand may be given to a member of the tenant's family or household, or to the tenant's employee, with a request that it be delivered to the tenant. If service is made on a person other than the tenant, that person must be of suitable age and discretion, and the service must actually occur at the premises. An equally valid and significantly easier method is to serve the demand by first-class mail addressed to the tenant. If the demand is mailed, the date of service is deemed to be the next regular day for the delivery of mail. Because of this presumption, service by regular mail is usually preferable to other types of service.

**Summons and complaint:** Once the demand period has passed, the landlord can file its eviction action, usually in the District Court where the property is located (MCL 600.5706). Again, there are SCAO forms for both the summons (DC 104) and the complaint (DC 102a). The eviction action may be joined with a claim for a money judgment, provided the amount sought in the monetary claim is within the District Court's jurisdiction (MCR 4.201(G)).

Although non-payment actions have their own form of complaint, distinct from other types of eviction, the summons form is the same for all types of eviction. The summons form for eviction actions, however, is not the same as the summons form used in other civil actions. Do not, under any circumstances, use the general civil summons form (MC 01) to commence an eviction action. When the action is filed, the court clerk will schedule the initial trial date and write that date directly on the summons form. The summons must include advice to the tenant on several matters, such as its right to an attorney (MCR 4.201(C)(2)). These advice requirements are easily met through use of the SCAO form.

The Court Rule establishes a number of requirements for the eviction complaint (MCR 4.201(B)). The complaint must (a) comply with the general pleading requirements, (b) describe the premises, (c) allege non-payment of rent, (d) state the rental periods and rate, (e) state the amount due when the complaint was filed, and (f) indicate the dates on which additional payments will become due. A copy of the demand must be attached to the complaint, along with a copy of the lease, if there is one.

**Service of process:** The Court Rule is very precise on the question of service (MCR 4.201(D)). A copy of the summons and complaint must be served on the tenant by mail. Unless the court does the mailing and keeps a record, the landlord must attach a postal receipt to the proof of service. In addition to the mailing, the tenant must also be served in one of three ways: (1) by one of the methods provided in the general court rules, (2) by delivering the papers at the premises to a member of the tenant's household of suitable age, who is informed of the contents, and who is asked to deliver the papers to the tenant, or (3) by posting on the premises, assuming certain conditions have been met (MCR 4.201(D)(3)). If the local court offers service by a court officer, always accept that opportunity. The judge will trust the propriety of such service, which will be particularly important if the tenant fails to appear and the landlord wants a default judgment.

**Initial trial date:** The tenant may appear on the initial trial date and assert its answer orally (MCR 4.201(F)(1)(b)). Unlike other civil actions, eviction cases are scheduled for trial and may even be adjudicated without a written answer to the plaintiff's complaint. This means that the landlord must anticipate defenses that might be raised on the initial trial date. The attorney

should discuss potential defenses with the landlord to ensure that appropriate evidence will be ready for presentation. It may be helpful to review "Real Evidence: Special Rules for Real Estate Disputes," 80 *Michigan Bar Journal* 28 (2001). If the tenant raises a significant defense, or one that the landlord is simply not prepared to meet, the landlord can ask for an adjournment should the issue merit delay.

A SCAO escrow order form (DC 109) and judgment form (DC 105) should be prepared before going to court on the initial trial date. As noted previously, if the tenant raises a meritorious defense and files a jury demand, the judge will adjourn the trial date, sometimes for weeks or even months. If this occurs, the judge will usually order the tenant to pay rent into escrow while the case is pending (MCR 4.201(H)). This is typically accomplished on the landlord's oral motion (which is permissible under MCR 119(A)(1)), which should be made immediately after the judge determines that an adjournment is appropriate. The escrow order should be prepared and ready for entry as soon as the judge rules. Moreover, because time really is of the essence in eviction cases, a judgment form should also be prepared in advance for immediate entry once the judge rules. The last thing the landlord needs is any delay over entry of the judgment.

**Judgment, redemption and eviction:** The Court Rule contains several requirements for the eviction judgment (MCR 4.201(K)). The court must mail or deliver a copy of the judgment to both parties before the post-judgment time periods will begin to run. The tenant has 3 business days to ask the court to set aside a consent judgment if the tenant was not represented by counsel at the time it was entered (MCR 4.201(I)). All non-payment judgments must state the rent due at the time of trial, which cannot include any accelerated rent, and the time period and conditions for redemption. The judgment must inform the tenant that it may file a post-trial motion (MCR 4.201(M)) or an appeal (MCR 4.201(N)) within 10 days after the judgment enters.

Unlike termination actions, the tenant has an absolute and undisputed right of redemption in a non-payment case. If the tenant pays the amount set forth in the judgment within the redemption period, no eviction occurs (MCL 600.5744(4) & (6)). Alternatively, the filing of a post-trial motion may stay the eviction, provided certain conditions are met, which may include the filing of a bond and the deposit of an additional month's rent into escrow. If the tenant files a claim of appeal, the court must stay the eviction if the tenant also posts an appeal bond and continues to pay rent into escrow while the appeal is pending. Because the court rule provides a truncated appeal period from possessory judgments, both parties must be careful about timing if they plan to appeal.

Obtaining a judgment is not the final step in the eviction process. If the tenant fails to pay the amount due and does not otherwise obtain a stay of

enforcement, the landlord may request an order of eviction (MCR 4.201(L)), which is also referred to as a "writ of restitution" by the Act. The request is made by application, which is incorporated into the SCAO order of eviction (DC 107). Once the order has been signed by the judge, the landlord must contact the court officer, who will then serve the order on the tenant. If the tenant fails to leave, the court officer will work with the landlord to make arrangements for the physical eviction. Once the tenant is evicted, the landlord may change the locks and again assume full control over the property.

### C. RENT ACTIONS (MONEY JUDGMENTS)

A landlord's action for rent has been recognized as a distinct cause of action from other available remedies for breach of a lease. *M & V Barocas v THC, Inc*, 216 Mich App 447, 450 (1996). Rent differs in kind from the usual contractual obligation. 1 Friedman on Leases, 4th ed., §5.101 at 104. This is because "[t]echnically, rent is something which a tenant renders out of the profits of the land which he enjoys." *Kresge Co v Woodward Ave Corp*, 270 Mich 218 (1935). *See, Munson v County of Menominee*, 371 Mich 504 (1963). Thus, the concept of "rent" may include money, service, or specific property, as long as the tenant is conveying it to the landlord as compensation for the use of the demised premises. *Id.*

The concept of "rent" is tied to the temporal use and productivity of land. Because of this, liability for rent does not accrue until the applicable time period has passed. Hence, rent "is not regarded as a debt until it becomes due and payable." 1 *Friedman on Leases*, 4th Ed, §5.101 at 104; *Petovello v Murray*, 139 Mich App 639, 645 (1984). The fundamental tie between the use of land and the temporal nature of that use has two ramifications upon any claim for rent. First, the claim for rent accrues with the passage of time. Second, if this use and occupation should end, the rent would never become due.

Because the tenant's use and occupancy of the property is terminated by its eviction, the landlord has no claim for rent accruing after reentry. *Wreford v Kenrick*, 107 Mich 389 (1995). It is important to note, however, that this common law rule can be modified by agreement in a written lease. *Stott Realty Co v Amusement Co.*, 195 Mich 684, 690 (1940); *Longcor v Homeopathic College*, 210 Mich 575 (1920); *Brochert v Sunset Shores*, 181 Mich App 676 (1989).

This rule was applied in the foreclosure context by the Michigan Supreme Court in *Dolese v Bellows-Claude Neon Co*, 261 Mich 57 (1932). In *Dolese*, the plaintiff brought an action for rent following the foreclosure of the property which was the subject of a lease. The *Dolese* Court denied any claim for rent subsequent to the expiration of the redemption period. The trial court held, and the Michigan Supreme Court affirmed, that: "[t]he lease was extinguished by

the foreclosure and the expiration of the equity of redemption, and that, therefore, she could not recover the rent." *Dolese, supra*, 59. The foreclosure extinguished the lease and with it any claim for rent *Id.* Moreover, it is irrelevant that the tenant's action somehow contributed to its eviction. *Longcor v Homeopathic College*, 210 Mich 575, 580 (1920) ("The eviction of a tenant from the demised premises either by the landlord or by title paramount, is a bar to any demand for rent . . ."). Similarly, a subtenant cannot be held liable to its sub-landlord for the period subsequent to the termination of all rights of the sub-landlord in the leasehold premises due to foreclosure. *Cohn v Mary Lee Candies, Inc,* 293 Mich 157 (1940).

Rent claims are accorded a unique status when it comes to mitigation. Under common law, a lease is treated as a conveyance of real property for a specified duration. *Lipsitz v Schechter*, 377 Mich 685, 687 (1966). Because the lease is treated as a conveyance, the landlord has no duty to mitigate in an action to collect rent. *M & V Barocas v THC, Inc,* 216 Mich App 447 (1996); *Winshall v Ampco Auto Parks, Inc*, 417 F Supp 334 (1976).

From the landlord's perspective, there are benefits and detriments about rent actions. The main benefit is that the landlord has no obligation to mitigate, so the tenant cannot raise mitigation as a defense. The main detriment is that because rent is an installment obligation, the landlord is limited to the recovery of past due rent only. Additionally, the landlord may lose its rent claim entirely if the tenant's right to possession is terminated by foreclosure or eviction.

## D. DAMAGE ACTIONS

The basic principle of damages with respect to the breach a contract was established in 1854 by the decision of *Hadley v Baxendale*, 9 Exch 341; 156 Eng Rep 145 (1854). Under the rule of Hadley v Baxendale, "the damages recoverable for breach of contract are those that arise naturally from the breach or those that were in the contemplation of the parties at the time the contract was made." *Kewin v Massachusetts Mut Life Ins Co*, 409 Mich 401, 415 (1980). Hadley v Baxendale was incorporated into the lease context at the turn of the century by the Michigan Supreme Court in *Wolf v Megantz*, 184 Mich 452 (1915). Essentially there are two types of damages, those general damages which naturally arise from the breach and such special damages as may have been actually within the contemplation of the parties at the time they entered into the contract.

**General Damages:** General damages are those that arise naturally from the breach. Over the past five hundred years, the common law has clearly identified those damages which naturally arise from the breach of a real estate lease. The contract/market differential has been embraced as the appropriate rule of general damages under Michigan Law. In *Leo v Pearce Stores Co*, 57 F

2d 340 (ED Mich 1932), the District Court for the Eastern District of Michigan stated: "[i]t is well settled that the proper measure of damages presently recoverable by a lessor under a lease for years, from the lessee therein, on an abandonment constituting a breach thereof by the lessee, is the present value of the difference between the fair rental value, at the time of such breach, of the leased premises for the balance of the unexpired term and the total agreed rent for such unexpired term." *Id*, 341 (emphasis added) (construing Michigan law, as expressly noted in a connected opinion, *Leo v Pearce Stores Co*, 54 F 2d 92, 93 (ED Mich 1931)).

The contract/market differential remains the general rule in Michigan. *In Tel-Ex Plaza, Inc v Hardees*, 76 Mich App 131 (1977) the Court stated "[t]he general measure of damages applied where an agreement to lease is breached by the prospective lessee is the excess of the agreed rent over the rental value of the property, or the rent plaintiff could obtain for the property through reasonable diligence." *Id*, 134. The difference between contract and market rent is the type of damage which may fairly and reasonably be considered as arising naturally from the breach of a lease. The contract/market differential is determined at the time of the breach. *Leo, supra*, 57 F2d at 341; *accord, Zimmerman v Miller*, 206 Mich 599 (1919). Because the differential involves the calculation of two potentially disparate rent streams over the period following the breach, it must be reduced to present value as of the date of the breach. *Leo, supra*, 341; *accord Freeman v Lanning Corporation*, 61 Mich App 527 (1975).

**Special Damages:** In addition, or as an alternative, to those damages which arise naturally from a breach, the landlord may be entitled to special damages, as long as such damages where within the contemplation of the parties. *Bateman v Blake*, 81 Mich 227 (1890). Those damages which do not naturally flow from an alleged breach are referred to as special damages. *Van Pembrook v Zero Mfg Co*, 146 Mich App 87, 107 (1985); *Stockler v Rose*, 174 Mich App 14, 45 (1989). In cases for breach of lease, the landlord's lost profits are considered special damages. *Brodsky v Allen Hayosh Ind, Inc*, 1 Mich App 591 (1965). Special damages for lost profits have been allowed in two instances. First, where the tenant holds over in violation of the lease, the landlord is entitled to special damages, including lost profits and other expenses incurred by the landlord. *McCullagh v Goodyear Tire & Rubber Co*, 342 Mich 244 (1955); *Pasieczny v Bonkowski*, 260 Mich 107 (1932); *Hitchcock v Pratt*, 51 Mich 263 (1883). Secondly, where the landlord is to construct a building specifically for the tenant and there is no "market for the plaintiff's rental premises" special damages may also be appropriate. *Brodsky, supra*, 597.

**Statutory Damages:** The landlord is entitled to statutory damages if the tenant wrongfully holds over after the termination of the lease. The Ejectment Statute provides that: "[a]ny person who is ejected or put out of any lands or

tenements in a forcible and unlawful manner, or being out is afterwards held and kept out, by force, if he prevails, is entitled to recover 3 times the amount of his actual damages or $200.00, whichever is greater, in addition to recovering possession.: MCL 600.2918 (1). Refusal to peacefully surrender possession may be considered a use of force by the tenant. *De Bruyn Produce Co v Romero*, 202 Mich App 92, 106 (1993) ("the refusal to leave peaceably, thus requiring removal by force, constitutes a holding by force…"). Under Ejectment Statute the landlord is entitled to treble damages. *Hitchcock v Pratt*, 51 Mich 263 (1883)

**Mitigation of Damages**: Michigan cases addressing this issue date back to the 1957 decision of the Michigan Supreme Court in *Fox v Roethlisberger*, 350 Mich 1 (1957). In *Fox*, the Michigan Supreme Court expressly declined to decide whether a commercial landlord had any obligation to mitigate damages. Noting that the issue was "knotty and profound" the Michigan Supreme Court acknowledged that prior decisions seemed, "obliquely at least, to imply that we might be inclined to place some burden on the landlord to mitigate damages in these situations". The Court sidestepped the issue, however, stating "we do not think it is necessary to grapple with these large prickly questions to decide this case." After an extensive review of the landlord's actions, the Court noted that if there were an obligation to mitigate damages, it had been satisfied by the landlord. Because the landlord had, in fact, taken reasonable steps to mitigate its damages, it was irrelevant whether the obligation existed or not.

In *Frohling v Bischoff*, 73 Mich App 496 (1977) and *Jefferson Development v Heritage Cleaners*, 109 Mich App 606 (1981) the Michigan Court of Appeals imposed the obligation to mitigate damages on the landlord. In both cases, the tenants had vacated their premises and stopped paying rent to their landlords. In each, the Michigan Court of Appeals imposed an obligation on the landlords to mitigate damages by undertaking reasonable efforts to re-lease the premises.

The public policy behind the doctrine of mitigation was examined by the court in *Tel-Ex Plaza, Inc v Hardees Restaurants, Inc*, 76 Mich App 131, 134-135 (1977). The *Tel-Ex* Court stated that the injured party must make every reasonable effort to minimize the loss suffered and the damages must be reduced by any benefits accruing to the plaintiff as a consequence of the breach. *Id.* Under the avoidable consequences doctrine, the landlord is not allowed to recover for losses he could have avoided by reasonable effort or expenditure. *Id.* The landlord has a duty to do whatever may reasonably be done to minimize its loss. The *Tel-Ex* Court also noted that closely related to the avoidable consequences rule is the requirement that any benefit to the plaintiff arising from or as a result of the breach must reduce the damages otherwise payable. *Id.* These two doctrines require the landlord to take reasonable steps to mitigate its damages and minimize its loss.

There is no obligation, however, to mitigate damages arising out of a wrongful holdover by the tenant. *McCullagh v Goodyear Tire & Rubber Co*, 342 Mich 244, 356 (1955). There is, moreover, no obligation to mitigate in a defense to collect rent. *M & V Barocas v THC, Inc,* 216 Mich App 447 (1996); *Winshall v Ampco Auto Parks, Inc*, 417 F Supp 334 (1976). One court's effort to harmonize the distinction between these two mitigation rules is found in *In re Palace Quality Servs Indus*, 283 BR 868, 885 (Bankr ED Mich 2002).

## E. EQUITABLE REMEDIES

The landlord is entitled to injunctive relief to enforce its lease. *De Bruyn Produce Co v Romero*, 202 Mich App 92, 107 (1993); *Wertheimer v Hosmer*, 83 Mich 56 (1890); *Borman's v Great Scott*, 433 F Supp 343, 347 (ED MI 1975). In *Wertheimer*, the Michigan Supreme Court addressed the issue of whether injunctive relief was appropriate in connection with the enforcement of the use covenant in a commercial lease. As stated by the *Wertheimer* Court: "It is not only a question merely of damages, but the right of the complainants to control the premises or to put them to such uses as they might deem best." *Wertheimer*, *supra*, 62. As noted by the *Wertheimer* Court, lease covenant have value beyond the direct economic consequence of their breach, they also relate to the landlord's ability to control what goes on at its premises, a right that can often be of paramount importance.

The traditional factors for injunctive relief where summarized in the context of a lease dispute in *De Bruyn Produce Co v Romero*, 202 Mich App 92, 107 (1993). The *De Bruyn* Court stated: "[t]he factors to be considered before a preliminary injunction may be issued are: (1) the likelihood that the party seeking the injunction will prevail on the merits; (2) the danger that the party seeking the injunction will suffer irreparable injury if the injunction is not issued; (3) the risk that the party seeking the injunction would be harmed more by the absence of an injunction than the opposing party would be by the granting of the relief; and (4) the harm to the public interest if the injunction is issued. An additional consideration is whether an adequate legal remedy is available." *De Bruyn Produce Co, supra*, 107 (1993) (footnote 11) (citations omitted). With respect to the requirement of irreparable injury, the Federal Court has held that a special rule applies in cases of breach of lease. *Borman's v Great Scott*, 433 F Supp 343, 347 (Ed MI 1975) (construing Michigan common law). The *Borman's* Court held: "[f]urther, when dealing with the enforcement of leasehold covenants, the damages of the party seeking to enforce the covenant and to obtain an injunction are generally held to be impracticable or inadequate. Accordingly, this defendant-movant need not make a factual showing of irreparable harm and the Court will proceed to scrutinize the enforceability of the clause in the context of the requirement of the likelihood of success on the merits." *Borman's*, *supra*, 347. This is

generally in accord with the reasoning in *Wertheimer* and recognizes the particular importance of control in landlord-tenant relationships.

A limitation on the right to injunctive relief is found in those cases where the injunctive relief would require continuous supervision and involvement in business operations by the court. As stated by the Michigan Supreme Court: "[a] mandatory injunction to compel defendant to furnish services during the term of the lease and the renewal would require continuous supervision by this court. Specific performance will not be decreed under such circumstances." *Laker v Soverinsky*, 318 Mich 100, 104 (1947); *accord, 8600 Associates v Wearguard Corporation*, 737 F Supp 44 (ED Mich 1990) (refusing specific performance of operating covenant in commercial lease).

**F. SECURITY DEPOSITS & LANDLORD LIENS**

**Security Deposits:** The landlord's right to recover damages against a tenant's security deposit is the subject of extensive statutory regulation in the residential lease context. MCL 554.601, et seq. There is no similar regulation of security deposits in the commercial context. Therefore, the lease controls the rights of the parties.

**Landlord Liens:** The term "landlord lien" can be used to describe two distinct types of interest. The first is simply a consensual lien taken by the landlord in the same manner as any other creditor. The second and more commonly understood meaning is that of a special lien or interest the landlord acquires in a tenant's property due solely to the existence of the landlord/tenant relationship. Such an interest is sometimes created by statute, but often arises as part of a state's common law.

Although there is no statute establishing the existence of a landlord's lien in Michigan, the absence of clear Michigan case law left the area a fertile source for argument for many years. Furthermore, the decision in *Kresge Co v Twelve Seventy-Five Woodward Ave Corp*, 270 Mich 218 (1935) provided some support for the concept of an equitable lien, although the facts of the case extended only to rent paid by a sub-tenant during the prime-tenant's insolvency.

The Michigan Court of Appeals and Supreme Court have resolved the issue. *Shurlow v Bonthuis*, 218 Mich App 142 (1996), *rev other grounds*, 456 Mich 730 (1998). In *Shurlow*, the landlord and tenant entered into a written lease which contained the grant of an express lien against the tenant's property to secure payment obligations under the lease. As stated by the Michigan Court of Appeals "Michigan has neither enacted a statutory lien nor recognized a common law landlord's lien..." *Shurlow v Bonthuis*, 218 Mich App at 147. The *Shurlow* Courts determined, however, that the landlord could nonetheless

have a consensual lien just like any other creditor, but that such a lien was within the scope of the Uniform Commercial Code.

### G. GUARANTIES

Lease guaranties are enforceable under Michigan law. However, "[a] guarantor may assert both the defenses available to the primary obligor regarding the principal obligation on the debt and any personal defenses that arise out of the guaranty obligation." 11 *Mich Civ Jur. Guaranty* § 27 (West); *In re Allied Supermarkets, Inc.*, 951 F2d 718, 728 (6th Cir 1991) (construing Michigan law).

### H. TERMINATION OF THE LEASE

There is no common-law right to evict a tenant or to terminate a lease based on a simple breach of lease by the tenant. *United Coin Meter Co v Lasala*, 98 Mich App 238 (1980); *Erickson v Bay City Glass Co*, 6 Mich App 260 (1967). However, the parties may establish that right by agreement within the lease. *United Coin Meter Co.; Erickson.* When a power of termination has been incorporated into the lease, it will be construed against the landlord. *Steinberg v Fine*, 225 Mich 281; *see generally* John G. Cameron, Jr., *Michigan Real Property Law* §20.52 (ICLE). Note that a "right of reentry" is not the same thing as a "power of termination." See *Erickson* for an extended discussion of their distinction.

The right to terminate has been historically referred to as a *right of forfeiture.* The right is now generally referred to as a *power of termination. See* MCL 600.5714(1)(c)(i). If the landlord fails to include such a right within the lease, it is generally precluded from terminating based on anything less than a material breach. As explained by the Michigan Supreme Court:

> The lease contains no condition that a breach by plaintiff of any or all of the covenants would give defendants the right to terminate the tenancy. The common method in drafting leases is to gather some or all of the covenants, by reference, into a condition subsequent, an agreement by the parties, that a breach by the tenant of any or all of the covenants on his part shall give the landlord the right to terminate the tenancy by means and in a manner usually indicated. The lease contains no such condition. The defendants here had no right to forfeit, or to re-enter and repossess the premises, because of a breach of the covenant in question, whether express or implied.

*McPheeters v Birkholz*, 232 Mich 370, 376–377, 205 NW 196 (1925); *see also In re State Highway Comm'r*, 365 Mich 322, 112 NW2d 573 (1961).

In the absence of a power of termination, a material breach is required before a landlord may terminate or rescind the lease. *Walker & Co v Harrison*,

347 Mich 630, 635, 81 NW2d 352 (1957); *Erickson.* One consideration in determining whether a breach is material is whether the non-breaching party obtained the benefit which he or she reasonably expected to receive. *Walker & Co, supra.* Although a material breach may justify rescission or termination, it is not without risk if exercised outside the safety of a well-defined power of termination clause. *Id* at 635.

The common-law rules have been modified by statute in Michigan in a couple of narrow ways. The legislature has created a statutory basis for termination in limited circumstances, even when a power of termination is not present in the lease. MCL 554.134(2) states: "[i]f a tenant neglects or refuses to pay rent on a lease at will or otherwise, the landlord may terminate the tenancy by giving the tenant a written 7-day notice to quit." The summary proceedings act includes MCL 554.134 as a basis for eviction, along with the traditional method of termination pursuant to a power of termination.

## II. TENANT REMEDIES

This section reviews the common law and statutory remedies available to the tenant for breach of lease by the landlord. In many cases these remedies can be modified, expanded or negated by agreement of the parties, so it is important to start any analysis by reading the lease. The remedies examined include (a) self-help by setoff against rent; (b) self-help through abandonment of the premises; (c) statutory actions for equitable and legal relief; (4) damage claims for money judgments; and (d) equitable remedies.

### A. SELF HELP (SET OFF)

Michigan law allows some self-help remedies for tenants. The most common form of self-help is simply withholding rent. Under the common law, all lease covenants were independent. *Reaume v Wayne Circuit Judge*, 299 Mich 305 (1941). Because lease covenants were independent, a breach by the landlord did not justify suspension or setoff by the tenant. *Id.* The tenant's obligation to pay rent continued even though the premises had been destroyed (*Standard Drug Store v AE Wood & Co*, 206 Mich 564 (1919)) or taken by eminent domain (*Pierson v H R Leonard Furniture Co*, 268 Mich 507, 522 (1934)). Thus, under the common law the only defense to an action for eviction was proof of payment. *Rome v Walker*, 38 Mich App 458, 463-464 (1972). Because of this, eviction proceedings had no need for equitable jurisdiction. *Reaume*, *supra*. Therefore evidence of breach by the landlord was "irrelevant" evidence in an eviction action. *Reaume v Brennan*, 299 Mich 305, 307-308 (1941). The decision in *Reaume* is based both on substantive law (the independent covenant doctrine) and then-existing procedure (the eviction statute conveyed no equitable jurisdiction).

Procedurally, MCL 600.5637(5) now allows tenants to raise many affirmative defenses, including specifically a breach by the landlord if such breach "excuses the payment of rent." The *Rome* Court has held that while the phrase "which excuses the payment of rent" is undefined, it is clear from an examination of the language of MCL 600.5646(3) that the Legislature intended that any defense which the tenant may have which is based on the landlord's breach can now be raised in an eviction action. *Id.* Additionally, the District Court, which hears summary proceedings, also now has equitable jurisdiction. MCL 600.8302. There is no longer a procedural barrier to suspension or setoff.

Substantively, in the context of residential leases, there are now implied covenants concerning fitness and repair that are established by statute. MCL 554.139. These covenants have been determined to be mutual, rather than independent, of the tenant's obligation to pay rent. *Rome v Walker*, 38 Mich App 458 (1972). Although the independent covenant doctrine has been overridden by statute in the residential lease context, MCL 554.139 does not, however, apply to commercial leases. *Rome, supra.* The practical vitality of the independent covenant doctrine was, however, brought into question even in the commercial lease context by the decision of Court of Appeals in *Anchor Inn v Knopman*, 71 Mich App 64 (1976), which upheld a commercial tenant's right to setoff rent based on the landlord's breach of a covenant of repair. Although the independent covenant doctrine continues to exist, after *Anchor Inn* its application is not without controversy. A discussion of the subject is set forth in Commercial Leases: Effect of Landlord's Breach on Tenant's Obligation to Pay Rent, 17 *Mich Real Prop Rev* 75 (1990).

Self-help is a remedy that, at least for tenants, has come a long way since 1970. Prior to *Rome* and *Anchor Inn*, the tenant had no common law right to suspend or setoff rent because of breach by the landlord. In the residential context, *Rome* held the covenants of fitness and repair to be mutual, rather than independent covenants. The practical impact of this decision was to condone self-help by residential tenants, at least in this limited context of fitness and repair. In the commercial context, *Anchor Inn* provides support for extension of the doctrine of setoff where the landlord has failed to make repairs. It should be noted, however, that use of setoff or suspension is not without risks in the commercial context. If the tenant has a valuable lease which is important to its business, it will want to get some sort of judicial blessing instead of using self-help.

### B. SELF-HELP (ABANDONMENT)

The tenant may have a self-help remedy in the manner of abandonment, if certain conditions are established. Under Michigan law, "[a] breach of the covenant of quiet enjoyment that amounts to an eviction or constructive eviction is a defense to an action for rent. However, a tenant who chooses to assert that

defense must vacate the premises." Cameron, *Mich Real Prop Law* §20.32 (ICLE 3rd Ed) (citations omitted). Constructive eviction terminates the obligation to pay rent. *Kuschinsky v Flanigan,* 170 Mich 245 (1912). The conditions constituting a constructive eviction have been broadly defined to protect the tenant from a landlord's indifference. As stated by the Michigan Supreme Court: "[a] constructive eviction may be defined as any disturbance of the tenant's possession by the landlord or by someone under his authority whereby the premises are rendered unfit for occupancy for the purposes for which they were demised, or the tenant is deprived of the beneficial enjoyment of the premises, if the tenant abandons the premises within a reasonable time." *Panagos v Fox,* 310 Mich 157, 161 (1944) (emphasis added). The concept of constructive eviction has been broadly applied to wide variety of conditions affecting the tenant's enjoyment of the premises, including failure to provide heat (*DeBruyn Brothers Realty Co v Photo Lith,* 31 Mich App 487 (1971)); failure to repair *Panagos v Fox,* 310 Mich 157, 161 (1944); failure to change a stairway (*Lynder v SS Kresge,* 329 Mich 359 (1951)); failure to provide services (*Everson v Albert,* 261 Mich 182 (1933)); interference with light and air (*Dunton v Sweet,* 210 Mich 525 (1920)), leaving building materials on premises *Kuschinsky v Flanigan,* 170 Mich 245 (1912), or simply changing the use of related areas (*Coulter v Norton,* 100 Mich 389 (1894)).

The doctrine of constructive eviction focuses on the condition of the premises. In addition, a landlord materially breaches a commercial lease where the breach of an express covenant in the lease renders the tenant unable to operate its business. *Karpp* v *Royer,* 362 Mich 64, 68 (1960). When a landlord materially breaches a lease, the tenant is entitled to abandon the premises without liability for rent or damages. *Karpp,* states: "[d[eprivation of the beneficial use and enjoyment of leased premises as a result of the breach of a material covenant has been held to be sufficient to justify the abandonment of the premises by a tenant, particularly where, after notice, a reasonable time to remedy the defect has been given the landlord." *Karpp,* 362 Mich at 68. If the premises cannot be employed to their stated commercial use, there is a material breach of the lease, which may justify abandoning the premises.

## C. STATUTORY ACTIONS

This section reviews the statutory remedies available to tenants. The two main statutes are MCL 600.2918 and MCL 600.2932. The former involves equitable and monetary remedies for unlawful interference and the later with equitable and declaratory relief regarding possession.

**Unlawful Interference:** Michigan's Ejectment Statute extends a number of remedies to the tenant for breaches by the landlord involving interference with possession. At early common law, a landlord could use reasonably force to remove a holdover tenant or other unauthorized occupant of his land. *Deroshia*

*v Union Terminal Piers*, 151 Mich App 715, 718 (1986). In the interest of protecting the peace, this rule was modified by statute to prohibit forceful entry by the landlord. *Id.* The statute was held to prohibit forceful self-help regardless of whether or not the tenant was in rightful possession of the premises. *Gallant v Miles*, 200 Mich 532 (1918). The Ejectment Statute was amended in 1977 to add a subsection eliminating self-help altogether, even where not forceful, except in certain narrowly defined circumstances. *Deroshia, supra*, 718. This amendment virtually eliminated the landlord's right to self-help in favor of judicial process to remove a tenant wrongfully in possession. The amendment was intended to prevent parties from taking the law into their own hands in circumstances which are likely to result in a breach of peace. *Id.*

The Ejectment Statute provides treble damages for forceful dispossession. MCL 600.2918 (1). Treble damages are determined by tripling the amount awarded for actual damages suffered by the tenant as a result of the dispossession. Since actual damages can include lost profits, the significance of the statute is substantial. The Ejectment Statute draws a distinction between forceful dispossession and other types of interference. MCL 600.2918 (2). The actions which fall into the latter category are specifically identified by the statue and include removal of personal property, changing locks and interfering with utility services. MCL 600.2918 (2) (a)-(g).

Under the Ejectment Statute a tenant who is unlawfully dispossessed is entitled to recover actual damages suffered as a result of the landlord's use of self-help rather than judicial process. If a commercial tenant in lawful possession is dispossession and has suffered lost profits, is entitled to their recovery. *Deroshia, supra*, 722. However, a holdover tenant who is not in lawful possession cannot recover lost profits. *Id.* A holdover tenant's damages are limited to those suffered as a direct result of the landlord's use of the improper procedure, which may include such items as lost, destroyed or damaged equipment and spoiled perishable goods, as well as extra expenses directly incurred because of the landlord's use of self-help. *Id.*

The Ejectment Statute expressly extends the tenant the right to injunctive relief, in addition to its claim for statutory damages. MCL 600.2918 (4). Moreover, the tenant's rights under this Ejectment Statute cannot be waived. MCL 600.2918 (5). They can, however, be lost by inaction. The Ejectment Statute has a particularly short (90 day) statute of limitations attached to it. MCL 600.2918 (6). It is important to keep this statute of limitations firmly in mind.

**Declaratory and equitable relief:** The tenant also has a statutory right to declaratory and equitable relief. RJA Section 2932 provides: "Any person, whether he is in possession of the land in question or not, who claims any right

in, title to, equitable title to, interest in, or right to possession of land, may bring an action in the circuit courts against any other person who claims or might claim any interest inconsistent with the interest claimed by the plaintiff, whether the defendant is in possession of the land or not." MCL 600.2932(1). Actions under RJA Section 2932 are equitable in nature. MCL 600.2932(5). Declaratory relief is appropriate to determine landlord-tenant rights. *BeBruyn Produce v Romero*, 202 Mich App 92, 106 (1993).

## D. DAMAGE ACTIONS

The rule of damages with respect to breach of contract was established in 1854 by the decision of *Hadley v Baxendale*, 9 Exch 341; 156 Eng Rep. 145 (1854) Under the rule of Hadley v Baxendale, "the damages recoverable for breach of contract are those that arise naturally from the breach or those that were in the contemplation of the parties at the time the contract was made." *Kewin v Massachusetts Mut Life Ins Co*, 409 Mich 401, 415 (1980). Hadley v Baxendale was incorporated into the lease context at the turn of the century by the Michigan Supreme Court in *Wolf v Megantz*, 184 Mich 452 (1915). Essentially there are two types of damages, those general damages which naturally arise from the breach and such special damages as may have been actually within the contemplation of the parties at the time they entered into the contract.

**General Damages:** Traditionally, the tenant's general damages for breach of lease are the difference between the actual rental value (in light of the beach) and the rent reserved. *Jarrait v Peters*, 145 Mich 29 (1906). The rule is the same whether the leased property is a farm, a house, or business premises. *Taylor v Cooper*, 104 Mich 72 (1895). In recent years it has become accepted that lost profits naturally arise as the result of the landlord's breach of a retail lease. This issue was raised by the landlord in *Redinger v Standard Oil Co*, 6 Mich App 74 (1967).

**Special Damages:** In addition to general damages which the law presumes will arise from the breach of a lease, the law will allow recovery of those other types of damage, provided they were fairly within the contemplation of the parties when the lease was made, or might have been foreseen as a consequence of a breach of its covenants. *Wolf v Megantz*, 184 Mich 452 (1915).

## E. EQUITABLE REMEDIES

Both the District Court and Circuit Court have equitable jurisdiction when it comes to landlord-tenant disputes. The Circuit Court has express equitable jurisdiction under both MCL 600.2918 and MCL 600.2932. MCL 600.2918(4) is particularly important. The statute states: "A person who has lost possession or whose possessory interest has been unlawfully interfered with may, if that

person does not peacefully regain possession, bring an action for possession pursuant to section 5714(1)(d) of this act or bring a claim for injunctive relief in the appropriate circuit court."

The District Court also has broad jurisdiction to grant equitable relief, but only after jurisdiction has been established under MCL 600.5704. The statute states: "In addition to the civil jurisdiction provided in sections 5704 and 8301, the district court has equitable jurisdiction and authority concurrent with that of the circuit court in the matters and to the extent provided by this section. " MCL 600.8302. There is amply statutory jurisdiction to support equitable relief for the tenant, regardless of the forum.

**Specific performance:** Under certain circumstances, the tenant may be entitled to specific performance of lease. *Ann Arbor Iron & Metal Co v Zaidman*, 272 Mich 532 (1935). Nonetheless, specific performance of a lease is a remedy of grace and not a matter of right. *Laker v Soverinsky*, 318 Mich 100, 104 (1947). The test of whether or not it should be granted depends upon the peculiar circumstances of each case. *Id.* The granting of this equitable remedy lies within the discretion of the court. *Id.* Specific performance may be denied if the tenant has an adequate remedy at law. *Continental & Vogue Health Studios, Inc v Abra Corp*, 369 Mich 561, 566 (1963); *8600 Associates v Wearguard Corporation*, 737 F Supp 44 (ED Mich 1990) (refusing specific performance of operating covenant in commercial lease).

In *Continental*, the court refused to enforce a covenant to restore a premises destroyed by fire because the tenant had an adequate remedy in law. The *Continental* Court noted, however, that: "[w]ere the situation here presented one in which plaintiff corporation were in physical possession of the leased building, or one of them; or were there some particular benefit from the location, by reason of a developed clientele conditioned to doing business with the plaintiff at that location, which plaintiff would have lost by defendant's failure to rebuild or restore, another result might have been reached." *Id*, 566. Because specific performance is clearly a matter of discretion, care must be taken to fully explain to the Court why legally remedies are inadequate.

Another limitation on specific performance is the amount of supervision required by the court. As stated by the Michigan Supreme Court: "[a] mandatory injunction to compel defendant to furnish services during the term of the lease and the renewal would require continuous supervision by this court. Specific performance will not be decreed under such circumstances." *Laker v Soverinsky*, 318 Mich 100, 104 (1947); *accord 8600 Associates v Wearguard Corporation*, 737 F Supp 44 (ED Mich 1990) (refusing specific performance of operating covenant in commercial lease). When seeking specific performance, the tenant should tailor its request to limit judicial involvement to a minimum.

**Injunctive relief**: The tenant may be entitled to injunctive relief to enforce its lease. Under common law, the tenant is entitled to an injunction if it makes the requisite showing. *Galper v US Shoe Corp*, 815 F Supp 1037 (ED Mich 1993); *De Bruyn Produce Co v Romero*, 202 Mich App 92, 107 (1993) (footnote 11) (citations omitted). With respect to the requirement of irreparable injury, the Federal Court has held that a special rule applies in cases of breach of lease. *Borman's v Great Scott*, 433 F Supp 343, 347 (ED MI 1975). The *Borman's* Court held: "In summary, it is axiomatic that an individual seeking to have a preliminary injunction issue must show that he has or will be subjected to irreparable harm. However, an explicit showing is not required where those damages are impracticable or inadequate to ascertain. Further, when dealing with the enforcement of leasehold covenants, the damages of the party seeking to enforce the covenant and to obtain an injunction are generally held to be impracticable or inadequate. Accordingly, this defendant-movant need not make a factual showing of irreparable harm and the Court will proceed to scrutinize the enforceability of the clause in the context of the requirement of the likelihood of success on the merits." This is generally in accord with the reasoning in *Wertheimer v Hosmer*, 83 Mich 56 (1890).

In addition to the common law basis for an injunction, MCL 600.2918 provides a statutory right to injunctive relief if the tenant has been dispossessed or if its rights have been unlawfully interfered with by the landlord. The Ejectment Statute states: "A person who has lost possession or whose possessory interest has been unlawfully interfered with may, if that person does not peacefully regain possession, bring an action for possession pursuant to section 5714(1)(d) of this act or bring a claim for injunctive relief in the appropriate circuit court." MCL 600.2918(4). It would appear that the Ejectment Statute acknowledges that dispossession and unlawful interference are injuries for which there is no adequate remedy at law. RJA 2918 (4) would also appear to establish that there is no harm to the public interest if such an injunction is entered.

An area where injunctive relief is particularly valuable to the tenant is in enjoining termination. In *Galper v US Shoe Corp*, 815 F Supp 1037 (ED Mich 1993), the Federal District Court addressed the issue of whether a commercial tenant could bring an action in the Circuit Court to enjoin the landlord from proceeding with an eviction action in the District Court. The *Galper* Court upheld the injunction entered by the Circuit Court, finding that eviction of the tenant would result in irreparable injury "in the form of damage to her reputation as a professional." *Id*, 1044.

## III. BANKRUPTCY

### A. TENANT'S BANKRUPTCY

The tenant's rights in bankruptcy are significantly affected, and to a large extent determined, by reference to the United States Bankruptcy Code. The Bankruptcy Code divides tenants into two categories, residential and non-residential, which it treats quite differently. While there is some disagreement among the bankruptcy judges over what constitutes residential property, *compare In re Independence Village, Inc*, 52 BR 715 (ED Mich 1985) and *In re Sonora Convalescent Hospital*, 69 BR 134 (ED Cal 1986), the typical commercial lease for office, retail, or industrial use will almost always fall into the category of nonresidential property.

**Automatic Stay:** Upon the filing of a bankruptcy petition by or against a tenant, all collection and enforcement actions, including summary proceedings, are automatically stayed. 11 USC 362(a). The automatic stay is similar to an injunction, except that it arises as a matter of law immediately with the filing and requires no motion or evidentiary hearing to become effective. An automatic stay violation can be punished with contempt of court, 11 USC 362(h), and other sanctions including the imposition of damages, costs and attorney fees, whether the landlord is aware of the bankruptcy or not, 11 USC 362(h).

Potential violations of the automatic stay are not always obvious. For example, under Michigan law, termination of a lease also results in the termination of all sub-tenancies. *Cohn v Mary Lee Candies, Inc*, 293 Mich 157 (1940). Termination of a lease may, therefore, result in a violation of the stay if the subtenant is in bankruptcy. *In re 48th Street Steakhouse*, 835 F2d 427 (2d Cir 1987).

In most instances, the landlord is required to file a motion to lift the stay before any action can be taken to recover possession. Generally, the motion must establish either (1) that the tenant does not have any equity in the property and that the premises are not necessary to an effective reorganization or (2) some other appropriate *cause* to grant the relief. 11 USC 362(d). *Cause* is not defined by the statute but is determined on a case-by-case basis by the bankruptcy court. The failure to provide adequate protection of the landlord's interests, including failing to insure or maintain the premises, has been construed as cause for lifting the automatic stay.

An exception to the foregoing rules is contained in 11 USC 362(b)(10), which provides that the filing of a bankruptcy case does not operate to stay "any act by a lessor to the debtor under a lease of nonresidential real property that has terminated by the expiration of the stated term of the lease before the

commencement of or during a case under this title to obtain possession of such property." In other words, if the stated term expires either before or during the case without an affirmative act by the landlord, the automatic stay no longer applies. *See Frenchtown Villa v Meadors*, 117 Mich App 683 (1982). Because of the severity of sanctions for violation of the stay, the landlord should proceed on this basis only in the clearest of situations.

The difficulty in making such an assessment is illustrated by *In re OH Holding Co*, 132 BR 568 (ED Mich 1991), in which the landlord had sent a notice of default that it claimed terminated the lease before the bankruptcy petition was filed. The court decided that, because Michigan's summary proceedings act provided the tenant with an absolute right of redemption where termination was based on nonpayment of moneys due under the lease, the tenant's redemption right became part of the estate and that interest could be redeemed even though the lease had been terminated. In light of *OH Holding,* any postpetition action taken by the landlord before the redemption period expired would constitute a violation of the stay, even though landlord held a prepetition state court judgment terminating the tenancy.

Application of the automatic stay is, therefore, extremely broad. Generally, any affirmative action, such as sending a termination, or even a nonrenewal, notice is covered. However, the automatic stay does not toll or restrain the mere passage of time. *In re Margulis*, 323 BR 130 (Bankr SDNY 2005). It does not stop a contract from terminating by its own terms as long as the termination does not depend on a postpetition act. *Moody v Amoco Oil Co*, 734 F2d 1200, 1213 (7th Cir 1984). As are result, the enforceability of certain lease provisions should be drafted with the automatic stay in mind. "Evergreen" provisions (those that renew for additional periods absent some affirmative act) should be avoided or at least thoroughly considered before they are included in a lease.

**The Landlord's Claims:** Although stayed from taking certain actions to enforce pre-petition defaults, the landlord nonetheless enjoys a preferred status over the tenant's general unsecured creditors (at least before tenant rejects or assumes the lease as discussed below). Importantly, the tenant must timely perform all obligations of the lease arising from and after the bankruptcy filing until the lease is assumed or rejected, including payment of the contract rent. 11 USC 365(d)(3). The rent accruing during this period is entitled to priority as an administrative expense and generally must be paid on a current basis. Whether this requires proration of an obligation, such as real estate taxes, that comes due after the petition date but covers both the prepetition and postpetition period (accrual method) has not been dealt with uniformly by bankruptcy courts. However, the Sixth Circuit in *In re Koenig Sporting Goods, Inc*, 203 F3d 986, 989 (6th Cir 2000), found the billing date method (as opposed to the accrual method) is appropriate under the unambiguous language of section 365(d)(3). *See, e.g., In re Montgomery Ward Holding Corp*, 268 F3d 205, 211

(3d Cir 2001) (debtor required to pay entire tax bill including prepetition portion).

If the lease is subsequently rejected by the tenant, the rejection constitutes a breach of lease under the Bankruptcy Code. The breach is deemed to have occurred immediately prior to the bankruptcy filing, and the landlord's damage claim is treated as an unsecured claim to the extent it exceeds any prepetition security deposit or other security held by the landlord. Both the secured and unsecured portions of the claim, however, are limited in amount to (1) the rent reserved in the lease, without acceleration, for the greater of one year or 15 percent, not to exceed three years of the remaining lease term, plus (2) any unpaid rent due under the lease without acceleration. 11 USC 502(b). When the lease is rejected, the landlord can also pursue recovery of possession. 11 USC 365(d)(4). The unsecured claim for future rent runs from the earlier of (a) the petition date and the date the landlord repossessed, or (b) the date the tenant surrendered the property.

If the lease is assumed by the tenant, all financial obligations (including the contract rent) become administrative expenses of the estate. Additionally, the lease is treated as a post-petition contractual obligation of the tenant's bankruptcy estate, at least until the lease is assigned with court approval. As modified by the 2005 Act, the Bankruptcy Code now expressly provides that the tenant may reject a lease even after it has been assumed. If the tenant assumes a lease and then rejects it, the administrative priority for the claims arising from rejection are limited to monetary obligations (other than those arising from or related to a "failure to operate" or a "penalty provision") due under the lease for two years following the later of (i) the rejection date or (ii) the date of actual turnover of the premises. This cap on the administrative claim applies without reduction or setoff for any reason except for sums received from an entity other than tenant, such as a guarantor. Any sums remaining due under the lease are treated as a general unsecured claim subject to the 11 USC 502(b)(6) cap.

**Acceptance or Rejection of the Lease:** Generally, subject to the bankruptcy court's approval, the tenant may assume or reject any unexpired lease based on the tenant's business judgment. *In re Federated Dept Stores*, 131 BR 808 (SD Ohio 1991). Business judgment concerns the tenant's commercial viability, not that of the landlord or other creditors.

A commercial lease will automatically be "deemed rejected" if the tenant fails to file a motion to assume or reject the lease within the earlier of (i) 120 days after the Chapter 11 case is filed, and (ii) the date the confirmation order is entered. 11 USC 365(d)(4)(A). The bankruptcy court may extend this 120-day period for an additional 90 days upon a showing of cause. 11 USC 365(d)(4)(B)(i). Further extensions are permitted with the landlord's prior written consent. 11 USC 365(d)(4)(B)(ii).

If a lease is deemed rejected by the passage of time, the tenant must immediately surrender the premises to the landlord. 11 USC 365(d)(4). If the lease is rejected by motion, there is a conflict among Michigan's bankruptcy courts whether to order the turnover of possession or lift the automatic stay to allow the landlord to proceed in state court. *In re Chris-Kay Foods East, Inc*, 118 BR 70 (ED Mich 1990); *In re Cybernetic Services, Inc*, 94 BR 952 (WD Mich 1989); *In re Urbanco*, 122 BR 513 (WD 1991). If temporary use of the premises will assist the tenant, the bankruptcy court may allow the tenant to remain in possession provided it pays a reasonable rental for the property.

Assumption of the lease means that the tenant has committed to carrying out the obligations of the lease. The tenant must assume or reject the entire lease, not just its favorable terms, except for "anti-assignment" provisions. If assumed, the trustee may generally assign the lease despite a lease clause prohibiting assignment without the landlord's consent. 11 USC 365(f)(1), (3).

The tenant may not, however, assume or assign a commercial lease that was terminated under applicable state law prior to the bankruptcy. Whether a lease has been irredeemably terminated prepetition is a question of state law. *In re OH Holding Co*, 132 BR 568 (ED Mich 1991). If the tenant had a right to redeem under Michigan law at the time of filing, that right may be exercised in bankruptcy. *Id.*

If the lease was in substantive default at the time of filing, the tenant may not assume the lease unless the tenant: (1) cures or provides adequate assurance that the tenant will promptly cure all defaults; (2) compensates or provides adequate assurance that the tenant will promptly compensate the landlord for any actual pecuniary loss resulting from the default; and (3) provides landlord adequate assurance of future performance under the lease. 11 USC 365(b)(1).

The tenant need not cure the following defaults as a condition to assumption: (1) tenant's insolvency or financial condition before the closing of the bankruptcy, (2) the bankruptcy filing, (3) appointment of a bankruptcy trustee, (4) the satisfaction of any penalty rate or penalty provision relating to a default to perform nonmonetary obligations under the lease, or (5) past defaults in nonmonetary obligations that are impossible to cure by nonmonetary acts, but that are currently being performed in accordance with the lease. 11 USC 365(b). Lease clauses defining these events as a default are unenforceable in bankruptcy. 11 USC 365(e).

There are special rules for determining adequate assurance of future performance as a condition for assumption of shopping center leases. Cases addressing what constitutes a shopping center include *In re Sun TV and Appliances, Inc*, 234 BR 356 (D Del 1999); *In re Goldblatt Bros, Inc*, 766 F2d 1136 (7th Cir 1985); *In re Ames Dept Stores, Inc*, 127 BR 744 (SDNY 1991); *In*

*re 905 Intern Stores, Inc*, 57 BR 786 (ED Mo 1985); *In re Joshua Slocum, Ltd*, 922 F2d 1081 (3d Cir 1990). The tenant must provide adequate assurance: (1) of the source of rent and other consideration due under the lease, and for an assignment, that the proposed assignee's financial condition and operating performance will be similar to tenant's at the lease commencement; (2) that any percentage rent will not decline substantially; (3) that assumption or assignment of the lease is subject to all the lease provisions, including radius, location, use, or exclusivity provisions; (4) that assumption or assignment will not breach any such provision contained in any other lease, financing agreement, or master agreement relating to the shopping center; and (5) that assumption or assignment will not disrupt any tenant mix or balance in the shopping center.

**Assignment of the Lease:** As discussed above, if the tenant can assume the lease, it may also assign it. 11 USC 365(f)(1). Moreover, provisions that provide a rent increase upon assignment are likewise unenforceable. *In re David Orgell, Inc*, 117 BR 574 (CD Cal 1990). Assignment relieves the tenant from liability for any breach occurring after the assignment, regardless of what the lease may say to the contrary. 11 USC 365(k). The Bankruptcy Code expressly overrides Michigan law, which imposes continuing liability on the assignor, absent a release by the landlord. The landlord may require a security deposit from the assignee, which is substantially the same as the security deposit required from similar tenants.

## IV. WORKOUTS, CONCESSIONS & AMENDMENTS

There are very few legal restrictions on workout and concessions. Michigan's fraudulent conveyances statute provides that an agreement to change, modify, or discharge, in whole or in part, any contract, obligation, or lease of real property will not be deemed invalid because of an "absence of consideration" but only if it is "in writing and signed by the party against whom it is sought to enforce the change, modification, or discharge." MCL 566.1; *see also Barth v Women's City Club*, 254 Mich 270, 273 (1931) (surrender of lease required to be in writing). Because simply continuing the performance of a preexisting duty or legal obligation is not generally considered adequate consideration to support a lease modification, agreements to reduce rent or grant lease concessions typically must be in writing. *Green v Millman Bros, Inc*, 7 Mich App 450, 455 (1967). Consideration for modification has been found, however, under certain circumstances, such as where there is no obligation in the lease to occupy and conduct business in the premises but the tenant agrees to continue operating its business at the premises in return for rent concessions. *See Minor-Dietiker v Mary Jane Stores, Inc*, 2 Mich App 585 (1966). Generally, MCL 566.1 is deemed to require either additional consideration or written agreement, but not both.

Workouts and concessions are rarely discussed in vibrant real estate markets where rents are rising and vacancy rates are low. If the tenant cannot pay, the landlord promptly evicts the tenant and replaces the tenant with another; there is not a lot to be discussed. Soft or depressed markets are another thing entirely. In a down market, the landlord would often rather accept less rent than to have no rent at all. Shopping centers and malls present an additional level of concern for the landlord. Empty retail spaces provide no "draw" for the center and can create a negative perception in the community. These factors can hurt other tenants' businesses and reduce percentage rent payments to the landlord. The loss of an anchor tenant may trigger co-tenancy provisions and affect the marketability of all the space within the center. These are serious concerns for any landlord, but may be "life and death" concerns for a struggling retail center.

The tenant's leverage to negotiate concessions comes from a variety of factors: its own non-collectability; the landlord's inability to re-lease the premises for more rent than it can get from the current tenant, even after concessions; the length of time it will require the landlord to find a replacement tenant; the impact of vacancy on other tenants; and the costs the landlord can incur in connection with re-leasing, such as commissions and build-out costs. The first factor is usually the most important. If the landlord believes that it can evict the tenant and still collect a judgment for all its damages against that tenant, or a guarantor, it is far less likely to negotiate any significant concessions.

Because the tenant's weak financial condition is both its moral justification ("I really want to honor my agreement, but I just can't do it in this economy") and leverage ("you'll get nothing otherwise"), the process typically starts with the tenant turning over financial information to demonstrate that the landlord has little or nothing to gain through traditional lease enforcement. This information often includes the tenant's tax returns, financial statements, monthly profit and loss statements, gross and net sales information, information about tenant's other leases, personal financial information of guarantors, and perhaps some kind of a business plan for the tenant's recovery. This information allows the landlord to assess the situation and to determine how far it is willing to go to keep the tenant in the premises.

It is best to execute a written forbearance agreement before entering into any negotiations concerning lease concessions. There are too many issues, like waiver and estoppel, that can otherwise arise. The landlord will generally want to resolve a few matters up front as a condition to the negotiations. The landlord will want the tenant and any guarantor of the lease to acknowledge that the lease and guaranty are in full force and effect. The landlord will also want a release of any claims or defenses the tenant or guarantor may have against it. If the tenant or guarantor believes there is some sort of a breach, it is best to get that fact out in the open and talk about it as part of the negotiation process. It

can always be carved out of the release, if necessary. If the lease involves a multitenant property, the landlord should ask for a confidentiality agreement. If other tenants learn that the landlord is granting concessions, they will certainly want some too. The landlord will also want to set a deadline for the expiration of the negotiation period particularly if there is an interim reduction in rent.

Because the landlord is granting concessions, this is also a good time to revisit the landlord's wish list of rights that it did not get as part of the initial lease. The landlord may want to relocate the tenant to less desirable space; add a termination or relocation provision for future use; extend the term of the lease; eliminate exclusives, options, or rights of first refusal; or impose or increase the tenant's financial reporting requirements. In addition, this is a good time to consider additional security, such as a guaranty or a lien against the tenant's personal property.

If the tenant cannot continue its business despite lease concessions, a surrender agreement may be the best option. If the tenant has already abandoned the premises, these negotiations simply focus on payment and release as in any other civil matter. If the tenant is still in possession, the parties need to focus on exactly what is expected concerning the condition of the premises on surrender.

Both landlord and tenant should carefully check their third-party agreements to determine if there are any restrictions on their ability to negotiate concessions. Many non-disturbance agreements between the tenant and the landlord's mortgagee may restrict certain changes or modifications to the lease, particularly those affecting the payment of rent. In addition, the landlord may need lender approval from its mortgagee. If it is a multitenant property, the landlord should make sure that the proposed modifications do not conflict with rights extended to other tenants and that it does not trigger co-tenancy clauses or other provisions that would allow them to terminate their own leases.

# V. FORMS

## A. LEASE ENFORCEMENT FORBEARANCE AGREEMENT

**Lease Enforcement Forbearance Agreement**

This lease enforcement forbearance agreement (Agreement) is made as of **[date]** (Effective Date) among **[name]** (Landlord), **[name]** (Tenant), and **[name]** (Guarantor).

RECITALS

A. Landlord and Tenant entered into a lease **[date of lease]** (Lease).

B. Guarantor entered into a guaranty of the Lease **[date of guaranty]** (Guaranty).

C. Tenant is in default under the terms of the Lease.

D. Tenant has provided the following explanation for its default: **[insert explanation]**.

E. Landlord is willing to temporarily forbear enforcing its rights under the Lease and Guaranty, but only upon the express terms set forth in this Agreement and only during the Forbearance Period.

F. Guarantor has expressly consented to this Agreement.

The parties therefore agree as follows:

1. The Forbearance Period will start on the Effective Date and terminate on the earlier of (a) **[expiration date]**, (b) Tenant's default under this Agreement, or (c) Tenant's default under the Lease.

2. During the Forbearance Period, Tenant must pay to Landlord, in advance, on or before the first day of each calendar month, monthly rent in the reduced amount of $**[amount]** (the Temporary Reduced Rent). Notwithstanding the Lease, during the Forbearance Period, Tenant's payment of the Temporary Reduced Rent will be deemed sufficient payment of Rent to avoid default under the terms of the Lease. With this exception only, Tenant agrees to otherwise comply with all the other terms and conditions of the Lease.

3. During the Forbearance Period, Landlord agrees that it will not seek to enforce, by litigation, eviction, or otherwise, any Rent payment otherwise due to Landlord under the terms of the Lease. However, that this forbearance does not waive Landlord's right to enforce any right or remedy after the termination of the Forbearance Period.

4. Landlord, Tenant, and Guarantor agree to meet and discuss a possible amendment to the Lease. No party shall have any obligation to enter into any amendment to the Lease, and each party will negotiate in its own best interest, as determined in its sole discretion. Tenant and Guarantor agree to furnish to Landlord, within **[number]** days, information Landlord may request from time to time, including but not limited to the following: (a) Tenant's federal income tax and Michigan business tax returns for the past **[number]** years; (b) Tenant's certified financial statements for the past **[number]** years; (c) monthly profit and loss statements for the past **[number]** months; (d) detailed gross and net sales information for the past

**[number]** months; (e) information on Tenant's other leases within the State of Michigan; (f) the personal financial information of the Guarantor; and (g) a business plan for Tenant's recovery.

5. If the Forbearance Period terminates by expiration or default, without the execution of a written amendment to the Lease, then (a) Tenant shall pay Landlord, within **[number]** days of termination, the difference between the Temporary Reduced Rent and the Rent otherwise due under the terms of the Lease (the Rent Shortfall); and (b) Landlord may, in its sole discretion, do any one or more of the following: enforce the Lease in accord with its terms; enforce the Guaranty in accord with its terms; or exercise any and all rights and remedies under Michigan law in a manner that Landlord, in its sole and exclusive judgment, may determine, including without limitation undertaking summary proceedings for eviction of Tenant.

6. Tenant and Guarantor acknowledge that they have requested Landlord to forbear from enforcement of the Lease and Guaranty, that the forbearance extended by this Agreement is satisfactory to Tenant and Guarantor, and that this forbearance is in the best interests of Tenant and Guarantor.

7. Tenant and Guarantor reaffirm all of the terms and conditions of the Lease and Guaranty and acknowledge that, except as provided here, all Rent will continue to be due and payable in full.

8. Tenant and Guarantor acknowledge that, notwithstanding anything to the contrary, Landlord is not required to extend the term of this Agreement beyond the Forbearance Period.

9. Tenant and Guarantor and their related or affiliated corporations, partnerships, entities, individuals, successors, and assigns release, discharge, and acquit Landlord and all of its related or affiliated corporations, partnerships, entities, individuals, successors, and assigns from all claims Tenant and Guarantor, jointly or individually, or any of their related or affiliated corporations, partnerships, entities, individuals, successors, and assigns, have or may have, arising out of, or in any manner relating to the Lease, the Premises, the condition of the Premises, or any other matter, known or unknown.

10. Tenant and Guarantor acknowledge and represent that this Agreement is entered into as the free and voluntary act of Tenant and Guarantor. Tenant and Guarantor are not acting under any duress, undue influence, misapprehension, or misrepresentation by Landlord or the agent, attorney, or any other representative of Landlord.

11. This Agreement will not be modified in any manner, except by written agreement signed by all parties. This Agreement contains all the representations and agreements of the parties concerning forbearance and negotiation; there are no representations or agreements beyond those expressly set forth in this Agreement.

12. No negotiation or course of dealing between Landlord, Tenant, and Guarantor nor any failure or delay in exercising any rights or remedies under the Lease, the Guaranty, this Agreement, or existing by law may operate as a waiver of any right or remedy with respect to the Lease or Guaranty; and no single or partial exercise of any right or remedy may operate as a waiver or preclusion to the exercise of any other rights or remedies Landlord may have in regard to the Lease or Guaranty.

13. This Agreement will be governed by the laws of the State of Michigan and must not be construed against any party.

14. Guarantor expressly consents to this Agreement and waives any defense to enforcement of the Guaranty.

15. Tenant and Guarantor will keep in complete confidence and not divulge the existence, contents, or provisions of this Agreement to anyone without the written consent of Landlord (unless ordered to do so by a court of law or administrative body). A breach of this covenant of confidentiality will be deemed a default of this Agreement and, in addition to subjecting Tenant and Guarantor to all of Landlord's rights or remedies under the Lease and Guaranty, will result in the automatic termination of the Forbearance Period and Tenant's immediate payment to Landlord of the Rent Shortfall, without further notice to Tenant.

16. This Agreement will bind all of the parties and their respective heirs, personal representatives, successors, and assigns. This Agreement may be executed in counterparts and delivered by fax or e-mail.

LANDLORD

**[Name of landlord]**

By: /s/____________

**[Typed name of authorized signer]**

Its: **[Title of authorized signer]**

TENANT

**[Name of tenant]**

By: /s/____________

**[Typed name of authorized signer]**

Its: **[Title of authorized signer]**

GUARANTORS

**[Name of guarantor]**

By: /s/____________

**[Typed name of authorized signer]**

Its: **[Title of authorized signer]**

## B. LEASE SURRENDER AGREEMENT

**Lease Surrender Agreement**

This lease surrender agreement (Agreement) is made as of **[date]**, among **[name]** (Landlord), **[name]** (Tenant), and **[name]** (Guarantor).

RECITALS

A. Landlord and Tenant entered into a lease **[date of lease]** (Lease).

B. Guarantor entered into a guaranty of the Lease **[date of guaranty]** (Guaranty).

C. Tenant is in default under the terms of the Lease.

D. Landlord is willing to accept Tenant's surrender of the Premises, but only on the express terms set forth in this Agreement.

E. Guarantor has consented to this Agreement.

The parties therefore agree as follows:

1. Tenant shall pay Landlord $**[amount]** in certified funds (Surrender Payment) on or before **[date]** (Payment Date).

2. Conditioned upon Landlord's receipt of the Surrender Payment on or before the Payment Date, (a) Landlord will accept Tenant's surrender of the Premises on **[date]** (Surrender Date); and (b) the Lease and Guaranty shall be deemed terminated, effective on the Surrender Date. If this condition is not satisfied, this Agreement will be deemed null and void, and the Lease and Guaranty will continue in full force and effect.

3. Tenant and Guarantor agree to surrender the Premises to Landlord on the Surrender Date in the physical condition required by this Agreement (Required Condition). Notwithstanding anything to the contrary, Tenant and Guarantor will be jointly and severally liable to Landlord for all costs, expenses, and damages incurred by Landlord if the Premises are not surrendered on the Surrender Date in the Required Condition, including without limitation the costs and reasonable attorney fees incurred to enforce this Agreement. The Required Condition shall include: **[insert detailed description]**.

4. Conditioned on Landlord's receipt of the Surrender Payment on or before the Payment Date, effective on the Surrender Date, Landlord, Tenant, and Guarantor release, discharge, and acquit one another and all of their related or affiliated corporations, partnerships, entities, individuals, successors, and assigns from all claims they have or may have, arising out of or in any manner relating to the Lease, the Guaranty, the Premises, the condition of the Premises, or any other matter, known or unknown. Notwithstanding the foregoing, this release will not release Tenant or Guarantor from any obligation undertaken pursuant to this Agreement, including without limitation their obligation to surrender of the Premises on the Surrender Date in the Required Condition.

5. The parties acknowledge and represent that this Agreement is entered into freely and voluntarily, without duress, undue influence, or misrepresentation.

6. This Agreement will not be modified or amended in any manner, except by written agreement signed by all parties. This Agreement contains all the representations and agreements of the parties concerning surrender, termination, and release. There are no representations or agreements beyond those expressly set forth in this Agreement.

7. This Agreement will be governed by the laws of the State of Michigan and must not be construed against any party.

8. Tenant and Guarantor will keep in complete confidence and not divulge the existence, contents, or provisions of this Agreement to anyone without the prior written consent of Landlord (unless ordered to do so by a court of law or administrative body).

9. This Agreement will bind all of the parties and their respective heirs, personal representatives, successors, and assigns. It may be executed in counterparts and delivered by fax or e-mail.

LANDLORD

**[Name of landlord]**

By: /s/____________

**[Typed name of authorized signer]**

Its: **[Title of authorized signer]**

TENANT

**[Name of tenant]**

By: /s/____________

**[Typed name of authorized signer]**

Its: **[Title of authorized signer]**

GUARANTORS

**[Name of guarantor]**

By: /s/____________

**[Typed name of authorized signer]**

Its: **[Title of authorized signer]**