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A Non-Exhaustive Discussion of Assignment and Sublease Considerations, for Exhausted Commercial Landlords

This has been a challenging year for commercial property owners, and the challenge is not over. As more and more businesses have the opportunity to reopen at pre-pandemic capacity, it may become more clear who actually survived and who may never recover. Those that are unable to bounce back as restrictions relax may find themselves needing to reduce operations, or close locations. As that happens, commercial landlords—many of whom have seen unprecedented requests for rent relief and other concessions over the past year—may see more requests from tenants seeking to assign their leases or sublease space.

Business owners may assume that they have the right to bring in a substitute tenant. However, by statute, lease agreements in Texas are not subject to assignment or subletting without the prior consent of the property owner. This can be changed by agreement in the lease, but if the lease is silent as to rights to assign or sublet, then the landlord's prior consent is required. This sometimes comes as a surprise to tenants, as it is the exact opposite of the general rule that contracts are freely assignable unless otherwise agreed. Replacing a tenant in distress with a new tenant may be the best solution under the circumstances, but is not as simple as changing a nameplate. There are a number of important considerations on the landlord's side.

Upon receiving a request for consent to an assignment or sublease, commercial landlords should first revisit the lease document. This is particularly true for landlords that have inherited existing leases upon purchasing a project and may not be as familiar with the content of the lease form. For example, the lease could specify a period for the landlord to request information or otherwise respond, after which approval (or disapproval) is deemed. The lease may also state that a landlord will not unreasonably condition, withhold or delay its consent and could include language defining criteria for a reasonable basis for withholding consent. Although less likely in a commercial lease, it is also possible that the lease is silent on assignment or subletting, which may actually give the landlord more discretion in its response.

When the landlord has an understanding of its rights and options to respond, there are several substantive items to consider regarding the proposed transfer document. There is some overlap in landlord considerations for a proposed sublease or assignment, as well as areas that are more relevant to one or the other.

In an assignment, the original tenant is assigning all of its rights as the tenant to the assignee. The landlord's obligations shift from the original tenant to the assignee tenant, although the original tenant may retain some liability to the landlord if not expressly released. If there was a

guarantor, the guaranty would also carry over to the obligations of the assignee tenant, unless the guaranty document provided otherwise or the landlord agrees to a release. The assignment agreement presented to a landlord for consent may include requested releases, as well as terms for disposition of the original tenant's security deposit and notice addresses for the assignee tenant.

With a sublease, the original tenant remains the "tenant" and retains some rights to reenter possession of the space, such as upon subtenant default or if the sublease does not cover the complete term or entire premises. The landlord's obligations to the tenant do not become direct obligations to the subtenant, unless the landlord otherwise agrees. It is critical in a sublease agreement that the landlord understands any new obligations it is asked to undertake and that insurance, waivers of subrogation and indemnifications in favor of the landlord and its lender are expressly extended to apply to the subtenant. Landlord approval requirements for alterations and improvements to the premises should be extended to apply to subtenant requests as well.

Although a sublease may not begin as a direct agreement between the subtenant and landlord, it could become so if the landlord agrees to attorn to the subtenant on the sublease terms in the event that the primary tenant defaults. Such an agreement could be requested in the sublease consent or in a separate agreement required by the subtenant's lender. All documents the landlord is requested to sign should be carefully reviewed with this in mind.

Whether the tenant's proposed transfer is a sublease or an assignment, the landlord's loan documents should be reviewed to determine whether any lender consent requirements may be applicable. Loan documents may also contain requirements for the borrower/landlord to obtain estoppels and subordination, non-disturbance and attornment agreements from tenants that could apply to an assignee or subtenant. The tenant and proposed transferee may not be focused on landlord's lender's requirements or address them in their agreement. The landlord will need to consider them and require that they be adequately addressed in order to avoid potentially defaulting on loan covenants.

Another third party to consider is a franchisor. If the original tenant is a franchisee, then the lease may include provisions or a separate addendum with terms required by the franchisor. These rights often include agreements by the landlord, in the event of a default under the lease or the franchise agreement, to facilitate the franchisor's transferring the space from a failing franchisee to a new franchisee. The landlord will need to keep any obligations it has to the original tenant's franchisor in mind, to avoid risking exposure for breaching them.

Many leases provide that the tenant, perhaps up to a certain amount, will pay the Landlord's attorneys' fees and costs to review a proposed assignment or sublease. Consider making the effectiveness of Landlord's consent contingent upon receipt of the amount due. If the lease provides that tenant will pay over to the landlord all or part of any consideration from the subtenant or assignee that could be considered profit, then the consent document should address arrangements for calculation, verification and delivery of these sums as well.

Every transaction has its own twists, and the set of considerations described in this article is not exhaustive. However, these are matters not to overlook in responding to a deceptively simple request for consent to a sublease or assignment.

For more information, please contact Susan George.