



## Negotiating a Subordination Agreement with a Tenant's Lender

It is not uncommon for commercial landlords to receive requests from their tenants asking to subordinate or waive their interests in any lien or similarly-secured rights to the tenant's personal property in favor of that tenant's lender. Landlords then frequently ask what they need to look out for in these agreements and whether they should reject such agreements entirely. Even if a landlord does not have and/or care about any lien rights on the tenant's property, there are other important factors that should still be considered that may affect the landlord's rights under the applicable lease. The following is a short summary of the main factors to review with respect to any requested subordination agreement.

First and foremost, should a landlord even agree to enter into such an agreement with the tenant's lender? The answer is generally yes. Tenants often require financing in order to kick off their business, including the financing of necessary trade equipment and other inventory and fixtures, which is in the best interest of all parties involved. Most banks require having superior lien rights on some or all of the tenant's personal property in the leased premises in order to approve the tenant's loan. This principal is essentially the same for any subsequent refinance as well.

A tenant's lender will almost always provide its own subordination agreement form, and they are typically relatively short (perhaps a few pages in length). One of the first matters to confirm is the effect the agreement will have on the landlord's existing lien rights. Some form agreements require the landlord to subordinate its interest just as to that particular lender, while other agreements call for the landlord to forever waive all of its lien rights under the lease. If a landlord has existing lien rights under the lease and does not wish to entirely forego that protection, then a specific subordination, rather than a blanket waiver, of those rights should be negotiated.

Another typical clause in these agreements involve rights granted to lenders to enter onto the premises and remove the described collateral under the respective tenant's loan documents, usually in the event the lease is terminated or such tenant defaults under its loan documents. Important considerations for such removal include

- (i) timelines for when the tenant's property can be removed by the lender,
- (ii) whether the lender will have the right to extend such timelines or hold the lease space in exchange for the payment of some form of rent, or for no rent
- (iii) what happens if the lender does not remove the tenant's property, for whatever reason, and

- (iv) what happens if the leased premises is damaged when the personal property is removed by the lender.

Addressing these matters in the applicable subordination agreement can be beneficial to both landlords and lenders as a way to avoid uncertainties and disputes regarding such rights and obligations down the road.

Subordination agreements often also require separate notice to the lender in the event a tenant defaults under its lease with the landlord, with such notice being the most practical method for the lender to learn about the tenant's default. Lenders may request separate rights to cure any such default in the event the tenant fails to do so. Landlords should consider these timelines and whether a maximum number of opportunities to cure a tenant's default should be discussed.

Of course, these parties enter into these agreements hoping that none of these clauses will ever be needed, but in the unfortunate event these issues do arise, it is important to have a clear structure of the rights, obligations, and timelines for the landlord and the lender.

**For more information, please contact [Scott McKaig](#).**