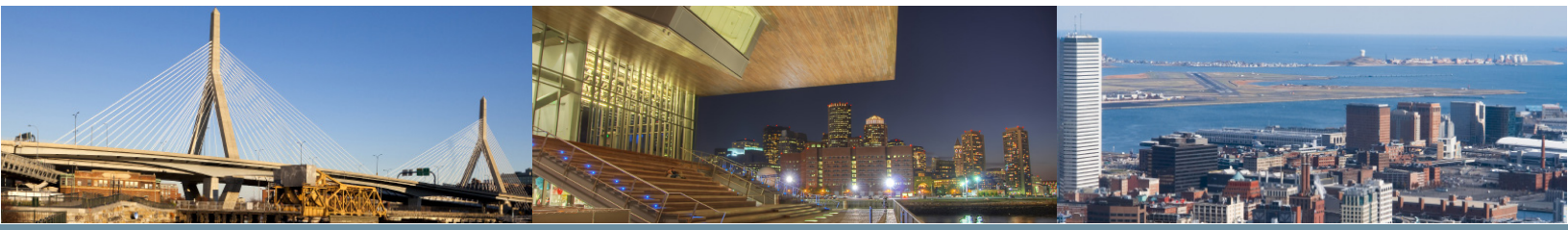

# Retail Tenants Continue To Seek Relief From Leases Due To Covid Induced Business Interruptions, While Results Remain Favorable For Landlords

**by Stephen F. Willig**
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In the New York area, litigation has continued between commercial landlords and tenants of all sizes seeking relief from, or changes to, lease terms due to hardships resulting from COVID-19 business interruption. While the volume of cases are diminishing, there remain some noteworthy decisions that reflect how landlords and tenants have fared in seeking relief.

In The Gap v. Ponte Gadea, Judge Laura Taylor Swain of the Southern District of New York was presented with a case of a commercial tenant seeking relief on a wide array of theories. There, the Gap entered into a lease in 2005 with defendant Ponte Gadea to operate two "first-class retail businesses," a Banana Republic and a Gap store, at 130 East 59th Street in Manhattan. The lease term was to end on January 31, 2021. In response to the New York State ordered shut down of all non-essential businesses, and other actions, the Gap decided on March 17, 2020, to close all stores in the US, Canada and Mexico and later announced it stopped paying rent on all stores in North America as of April 2020. Ponte Gadea then issued a notice of termination of the lease on June 8. Also on that date, New York stores were permitted to re-open for curbside pickup. On June 22, patrons were allowed back into retail stores at 50% capacity. The Gap used the Banana Republic store leased from Ponte Gadea for curbside pickup but decided not to reopen either the Gap or Banana Republic store for patrons (while it did open other Manhattan stores).

In order to avoid eviction and payment of rent, the Gap argued the shutdown constituted a "casualty" within the meaning of the lease which would excuse lease payments. The Court disagreed, holding a "casualty" applied to a singular event with a physical impact to the premises. Next, the Court considered the argument of frustration of purpose, setting forth a party's lease obligations can be forgiven where "a 'wholly unforeseeable event renders the contract valueless to one party.'" Judge Swain noted the fact that the transaction may not have been as profitable to one party as originally anticipated was not sufficient to support a frustration claim. Also, the cause of the frustration must have been unforeseen. In this case, force majeure terms of the lease enumerated government preemption due to a public emergency (hence, the event was foreseeable). Also, the purpose was not totally frustrated because the Gap was permitted to use the premises for business purposes such as storage, then curbside pickup and finally reopening. The Gap voluntarily chose not to use the premises for those purposes.

The next argument raised by the Gap was impossibility of performance. This required an unforeseeable event rendering performance impossible. Again, performance was not rendered impossible and the cause was foreseen and provided for in the force majeure terms.

The Gap's remaining arguments were equally unpersuasive to the

Court. Failure of consideration did not apply, as the Gap continued to have use of the premises as its due consideration under the lease. Mutual mistake did not allow Gap out of the lease either, as the lease properly reflected the terms the parties had agreed to. The Gap also sought to reform the contract (i.e. change it to allow for relief from rent in the circumstance), but here again the terms of the lease were as originally intended by the parties.

Thus, the Gap was unsuccessful in each of its arguments, and Judge Swain held that Ponte Gadea was entitled to summary judgment determining that the lease was terminated as of June 15 and entitling it to damages for a holdover tenancy.

Walsam v 214 West 29th Street Tenant, LLC. (a New York Supreme Court, New York County case) is another case that garnered some media attention, although having only a tangential connection to COVID. A commercial landlord sued a WeWork tenant accusing it of perpetuating a shell game in connection with property on West 29th Street in Manhattan where it leased seven floors. As most know, WeWork is in the business of sub-leasing office space, and the complaint here alleged WeWork had transitioned from subleasing to primarily small firms and freelancers to Fortune 500 companies, so-called "Enterprise" users. Those users required open floor plans with top-of-the-line electrical and HVAC systems, and this was the intent of the property leased to WeWork in 2018. The landlord, Walsam, allegedly spent substantial money building out the space for that purpose. As a consequence, a term of the lease provided that if WeWork defaulted, Walsam would assume all subleases.

WeWork defaulted on the lease, presumably due to financial difficulties brought about by COVID. Walsam contended that, in violation of the lease, WeWork undertook to move all of its subtenants out of the building to other WeWork locations. Walsam sued seeking a declaratory judgment that it held all rights under the subleases, that there had been a fraudulent transfer of the subleases by WeWork to "John Does" and there had been breaches of the contract. However, shortly into the case the matter was dismissed on the basis that WeWork had since demonstrated it was current with its lease obligations and reaffirmed its commitment to the lease. Walsam has appealed.

Another retail tenant was sued by its landlord in A/R Retail v Hugo Boss. In a May 2021 decision by Justice Cohen of the New York Supreme Court, New York County, Commercial Division, the Court ruled on many of the same theories that had been raised in The Gap case discussed above, and some additional arguments, all with the same results.

Hugo Boss leased a two-floor retail store from A/R Retail in 2012 for a 13-year term. The store was one of the largest in a luxury indoor shopping center (the "Shops") and was intended to provide Hugo Boss with a visible and highly trafficked retail location. The Shops were closed on March 17, 2020, by government directive. Hugo Boss paid rent in April, noting it reserved rights in doing so, and later wrote to A/R Retail contending it was entitled to rent abatements during the pandemic. The Shops were reopened to the general public on September 9, 2020, but business has not been the same. Among other things, A/R Retail decreased the operating hours of the Shops by 20%.

Justice Cohen considered Hugo Boss' arguments in defense of non-payment and ruled consistent with Judge Swain in The Gap. In particular, the leased premises had not been destroyed by a casualty (the Court upholding the criteria that a casualty was a specific onetime event, not a pandemic) or a hazard such as a fire. The frustration of purpose argument did not apply either, as it requires the entire purpose of the contract to have been so completely frustrated that the transaction would have been useless to both parties. Partial frustration such as where business has been reduced but where a tenant could continue the use of the premises did not satisfy the doctrine. Moreover, foreseeability of the event (the pandemic) negates application of the doctrine because it could then be provided for in the lease. The Court noted that the force majeure term of the lease made a provision for just such an occurrence as the pandemic. In the same way, the impossibility defense did not allow Hugo Boss to escape the terms of the lease as that applies only when performance is impossible due to the destruction of the subject matter of the contract or the means of performance. Here again, foreseeability, as evidenced by the force majeure clause, doomed this argument as well.

The Court also discussed the merits of the reformation argument (similar to the argument in The Gap case), although that claim was time-barred. Reformation is not intended to alleviate a hard bargain, Justice Cohen noted, but is intended solely to implicate the true intentions of the parties and the agreement. The lease embodied the agreement between the parties at the time.

Having thus disposed of every argument made by Hugo Boss, Justice Cohen awarded A/R Retail summary judgment on its claim for breach of the lease.

As we can see, the pandemic was hard on retail tenants with regard to lease obligations. Frustration of purpose, hazard and casualty were not fertile bases to avoid lease terms because the premises were not physically impacted, and business could proceed in some form. The courts most often held commercial tenants to the terms of their bargains, while limiting any relief to the force majeure terms (many of which provided for pandemics and government-imposed business shutdowns). Given these results, we are not likely to see many more efforts made to gain legal relief by tenants.

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