

Estoppels and SNDAs—Understanding and Negotiating the Landlord’s Lender’s Lease Documents

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Lawyers who represent lenders, commercial landlords, or commercial tenants need to understand the leasing documents required by lenders to landlords. This article provides an overview of such documents, which usually include tenant estoppel certificates and subordination, nondisturbance and attornment agreements, with sample document forms.

A Brief Overview of a Lease Transaction

Simply stated, a lease is the grant by one party (Landlord) to another party (Tenant) of a possessory interest in an estate in land (whether vacant land, an entire house or building, or a portion of a building). In the majority of commercial leases, the Landlord has obtained a loan from a bank or other lender (Lender or Mortgagee) who will be taking a security interest in the property owned by the Landlord, as well as an assignment of the Landlord’s interest in the leases of the property and the rental income derived from the leases and the property as collateral to secure the Landlord’s payment of the loan. The Tenant’s rent payments are part of the income stream the Landlord will use to repay the loan to the Lender.

The Lender made the loan to the Landlord to facilitate the Landlord’s acquisition, development, or redevelopment of property. As part of the terms and conditions of the Lender’s security documents with the Landlord—typically a loan agreement, mortgage, or deed of trust (mortgage), and assignment of rents and leases—there will be certain restrictions and requirements regarding leasing of the property. These requirements can include requirements that the Lender approve any leases of the property by the Landlord. In the case of large commercial or industrial properties, the Landlord’s approval may include approval of the Tenant, including the Tenant’s creditworthiness, and the terms and conditions of the lease. In the case of multifamily leases or leases of smaller spaces in a large facility, the requirement may only be that the Landlord use a form that has been pre-approved by the Lender (allowing minimal changes as may be negotiated by the parties) and that the lease be on market terms (set forth in the loan documents or calculated by the terms of the loan documents). Additionally, the loan documents may restrict the right of the Landlord to amend, modify, terminate, or extend the term of leases without the Lender’s consent.

In most loan documents for commercial properties, there will also be a requirement that all leases of the property be subordinated to the Lender’s liens created by the Security Documents. Why does this requirement exist? A lease creates a possessory lien in favor of the Tenant (the priority of the lien will depend upon the lease terms and date that the Tenant obtained possession of the leased premises). The lien of the Lender’s Mortgage will establish a Lender’s lien on the property and provide the Lender with priority upon filing. Lenders require that the Tenant’s possessory lien be subordinated so that in the event

that the Lender ever forecloses on the property, the Lender's superior lien can be used to terminate any subordinate liens (including the Tenants' rights to possession under their leases). Lenders typically require that the Landlord's lease form expressly state that the Tenant's lien is automatically subordinated to the lien created by the Mortgage held by any first mortgagee.

A typical Mortgage provision may provide as follows:

Mortgagor shall comply with and observe Mortgagor's obligations as landlord under all leases of the Property or any part thereof. Mortgagor, at Lender's request, shall furnish Lender with executed copies of all leases hereafter made of all or any part of the Property. Unless otherwise directed by Lender, all leases of the Property shall specifically provide that such leases are subordinate to this Mortgage; that the tenant under any lease attorns to Lender, such attornment to be effective upon Lender's acquisition of title to the Property; that the tenant agrees to execute such further evidences of attornment as Lender may from time to time request; and that the attornment of the tenant shall not be terminated by foreclosure.

Lenders may also include reservation of the right to not subordinate a Tenant's lien to Lender's lien.

Subordinated liens may be terminated upon a foreclosure of the Property by the Lender (allowing Lender to deliver vacant possession). Depending upon the property and creditworthiness of the Tenants, the Lender may want the leases to continue in the event that the Lender is forced to exercise its remedies under its loan documents (including foreclosing upon the property or taking a deed in lieu of foreclosure to take the Landlord's ownership interest in the property). As noted in the sample provision above, most commercial lenders also require that all leases contain a covenant that the Tenant agree to attorn to (or recognize and accept) the Lender as a successor landlord if the Lender forecloses upon Lender's mortgage interest in the property. When a Landlord is obtaining a new loan, either to acquire or refinance a property, in some cases Lenders may require subordination agreements only from Tenants who have placed their leasehold interest of record (by recording a memorandum of lease), and in other cases Lenders may require subordination agreements from the major Tenants of the property (which can be defined in many ways, but often by the major Tenant's square footage).

In addition to the subordination and attornment requirements, the Lender will typically include a requirement that the Landlord periodically obtain confirmation from its Tenants of certain matters related to the Lease. In particular, these items are the key financial terms of the Lease that the Lender used to underwrite its loan to the Landlord. This confirmation typically is made by requesting that the Tenants execute certificates in favor of the Lender, with the understanding that the Lender is entitled to rely upon all statements made in the certificate and that each Tenant will be estopped from asserting different facts in the future after confirming them in an estoppel certificate to the Lender. The confirmations most often included in estoppel certificates are those that are critical to the underwriting of the Lender's loan to Landlord: (i) the length of the lease term, (ii) the amount of Tenant's monthly rent payment, (iii) confirmation that payment of rent has commenced, (iv) confirmation of any termination rights, and (v) confirmation that neither the Landlord nor the Tenant is in default under the lease. Depending upon the circumstances, in some cases, Lenders will require estoppel certificates only from certain major Tenants, and in other cases, Lenders may require estoppel certificates from the major Tenants and a certain percentage of remaining Tenants, based on the number of tenants or rentable square footage.

In addition to the subordination provisions and estoppel certificate, the Lender typically will require that the Landlord reject payments under the lease more than one month in advance. This is necessary to protect the Lender's income stream in the event of foreclosure.

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As noted above, the Lender's Mortgage will have certain requirements with respect to the Landlord's lease. A typical lease provision for subordination and attornment provides:

Landlord and Tenant covenant and agree that this Lease and any and all renewals, modifications, extensions, amendments, and restatements hereof are subject and subordinate to any security instrument, including, without limitation, any mortgage or deed of trust (Security Instrument), which may now or hereafter be placed upon or affect the Real Property and the Project in which the Leased Premises is located, provided that the holder(s) of such Security Instrument shall agree in writing not to disturb Tenant's possession of the Premises or Tenant's rights under this Lease so long as Tenant is not in default hereunder (subject to any applicable notice or cure periods granted to Tenant). In the event that a Successor Landlord, as defined below, receives title to the Real Property, (i) such Successor Landlord shall be bound to Tenant under all of the terms and conditions of this Lease, (ii) Tenant shall recognize and attorn to Successor Landlord as Tenant's landlord under this Lease, and (iii) this Lease shall continue in full force and effect, in accordance with its terms, as a direct lease between Successor Landlord and Tenant. This clause shall be self-operative, and no further instrument or subordination shall be necessary. For purposes of this Lease, the term "Successor Landlord" shall mean any party that becomes owner of the Real Property, whether pursuant to (i) a foreclosure under the Security Instrument or any mortgage or deed of trust, (ii) any other exercise of the rights and remedies of the holder of the Security Interest, or (iii) delivery by Landlord to the holder of a security interest of a deed in lieu of foreclosure or any of the foregoing.

A typical lease provision for estoppel certificates provides:

From time to time during the Lease Term, within fifteen (15) days of receipt of Landlord's written request, Tenant shall acknowledge, execute, and deliver to Landlord, the holder of any Security Instrument, or any other persons whom Landlord may designate in such request, a statement in writing certifying that this Lease is unmodified and in full force and effect (or if there have been modifications hereunder, that the same is in full force and effect as modified and stating the modifications) and, if so, the dates to which the Rent and any other charges have been paid in advance, and such other items requested by Landlord, including, without limitation, the lease commencement date and expiration date, rent amounts, and that no offsets or counterclaims are present. It is intended that any such statement delivered pursuant to this Paragraph may be relied upon by any prospective purchaser or holder of any Security Instrument (including any assignee of the foregoing) encumbering the Premises.

Subordination, Nondisturbance, and Attornment Agreements

A subordination, nondisturbance, and attornment agreement, typically referred to as an SNDA, is an agreement among the Landlord, the Tenant, and the Lender who has (or will have during the loan or lease term) security with respect to the property leased between Landlord and Tenant. As noted above, SNDAs are generally required by a Lender as a condition precedent in closing a commercial loan transaction with the purpose of subordinating the rights of the Tenant under its lease so that Lender has a superior lien in the property. In exchange for the Tenant's agreement to subordinate, the Tenant requests that the Lender agree not to disturb the Tenant's leasehold in the event that the Lender has to foreclose its superior lien interest in the property (the "nondisturbance" provision of the SNDA).

Diving deeper into an SNDA requires a review of each of its components.

Subordination Provision: This provision covers the subordination of the Tenant's rights under its leasehold to the lien rights of the Lender created through the Security Documents. In the event of a Landlord's

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default under the terms and conditions of the Security Documents, the Lender is granted the first lien position to protect its interest in the Property. The subordination of the Tenant's rights under a lease may be created by Security Documents that are recorded either before or after the Tenant's leasehold interest takes effect. As such, in a case where the Tenant enters into a lease after the Security Documents have been recorded, then the Lender may be able to terminate the Tenant's rights under the lease at foreclosure. By contrast, if the Tenant enters into a lease before the Security Documents have been recorded, then the Lender may have a difficult time terminating the Tenant's rights under the lease at foreclosure—many jurisdictions agree that foreclosure against the Landlord does not affect the Tenant's rights under the lease. We are focusing on leasing subordination in these materials; however, other types of subordination include debt subordination as well as property interest subordination, both taking place in the commercial financing setting.

Nondisturbance Provision: This provision pertains to the agreement between the Lender and the Tenant that the Lender will not terminate the Tenant's subordinate rights under the lease, including the Tenant's possessory rights, at foreclosure. Generally, this is with the caveat that the Tenant must not be in default under the terms and conditions of the lease at the time of foreclosure. If the Tenant is not in default under the lease at the time of foreclosure, then the Tenant's rights under the lease shall be fully recognized. Nondisturbance can also take place in the context of a sublease, whereby the subtenant's rights under the sublease will not be disturbed if the master lease is terminated by the master landlord because of default by the master tenant (sublandlord). One caveat: If the Tenant is an affiliate of the Landlord, the Lender may not be willing to agree to a nondisturbance provision (resulting in a subordination and attornment agreement).

Attornment Provision: In this provision, the Tenant covenants with the Lender that, in the event of a foreclosure, the Tenant's rights under the lease will not be terminated and the Tenant agrees to recognize that the Lender, who would not otherwise be in privity with the Tenant, may enforce the lease as though the Lender were the original party to and beneficiary of the lease, and the Tenant and the Lender will be bound thereby.

The Lender derives benefits from a standard SNDA, which include the following: leasehold liens remain subordinate to the Lender liens until such Lender liens are released; the Tenant will attorn to the Lender as the new landlord upon the Lender or any successor or nominee acquiring the property; the Lender is not liable for any of the Landlord's defaults under the lease, leasing concessions, and common area maintenance reconciliations, unless as expressly set forth in the SNDA; and the Tenant will not exercise certain rights under the lease until the Lender has had an opportunity to cure the Landlord's defaults.

There are other considerations in negotiating an SNDA: the Landlord and the Tenant under the lease that is the subject of the SNDA subordination maintain each of their respective rights under the lease, however modified by the SNDA. Some typical requested covenants in the SNDA that can function as lease modifications (or restrictions on the Landlord and the Tenant) are as follows:

1. The SNDA may restrict any amendment, restrictions, and terminations under the lease by requiring the Lender's consent in each such case, and failure to obtain such consent may render any such amendment, restrictions, and terminations null and void or not require the Lender to be bound if the Lender exercises its rights under the SNDA.
2. The SNDA should require that the Tenant pay future rent to the Lender without Landlord approval and without the Tenant being required to make a default determination by the Landlord. Further, the Tenant should receive full credit for such future rent payment.

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3. The SNDA should contain language that enables the Lender to step into the shoes of the Landlord in the event of the Tenant's default under the lease and to exercise all rights and remedies under the lease.
4. The SNDA should require the Tenant to provide notice to the Lender in the case of the Landlord's default and to allow the Lender to cure such default after the applicable notice and cure period set forth in the lease, thus providing an expanded right for the Lender to protect the Lender's collateral and income stream.
5. Many SNDAs contain provisions that mimic the language in the estoppel certificate to confirm the Tenant's representations of the current status of the lease.

A sample form of SDNA appears at the end of this article.

Estoppel Certificate

From the Tenant perspective, estoppel certificates are important because they can have significant legal consequences, but they can be easily overlooked. Once a Tenant executes and delivers an estoppel certificate, the Tenant is "estopped" or prohibited from asserting a position to the contrary of any of the statements in the estoppel certificate. Estoppel certificates take various forms, but typically they are a series of statements that provide a snapshot of a lease at the time the estoppel certificate is given by confirming certain facts regarding the lease and the Tenant's occupancy of the property that a Lender requires.

There are several things Tenants must consider when completing an estoppel certificate. As a threshold matter, the Tenant should be clear who the estoppel certificate will be in favor of—usually it is the Landlord, the Lender, and successors and assigns of both. As a second preliminary matter, the Tenant must carefully consider each statement it is requested to make in the estoppel certificate.

First, the estoppel certificate will identify all of the lease documents by title, names of parties (original parties and any assignees), and date. All lease documents, including amendments, letter agreements, guarantees, waivers, assignment and assumption agreements, and similar transfer agreements, should be identified and included. If the Tenant has assigned the lease or sublet any portion of the premises, it should be disclosed here as well, with the applicable documents described in the estoppel certificate. The Lender often requires that copies of all lease documents be attached to the estoppel certificate and that the estoppel certificate confirm that the attached lease documents are true, complete, and correct copies in all respects.

Second, the estoppel certificate will confirm that the lease term has commenced (or if it has not yet commenced, confirm when it will commence based on the occurrence of certain events), together with the length of the initial lease term and any renewal terms that are available. If the Tenant has an early termination right or similar right that could shorten the term of the lease, this will likely need to be disclosed in the estoppel certificate as well. It will likely also confirm the rent commencement date and that the Tenant is paying rent pursuant to the lease documents if the rent commencement date has occurred. Another statement that some Lenders have included since the shutdowns that resulted from the COVID-19 pandemic include "Tenant has not, as of the date hereof, requested rent relief from the Landlord and does not anticipate asking for rent relief."

Third, the estoppel certificate will confirm the size and location of the leased premises. It is best here to be as specific as possible in describing the leased premises by using a suite number or any similar designation for the space.

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Fourth, the estoppel certificate will state the material economic terms of the lease. It will state the current monthly base rent as well as monthly installments of additional rent, such as common area maintenance charges, operating expenses, and real estate taxes that the Tenant is paying. As noted above, it is important to the Lender that rent not be paid more than one month in advance, and the estoppel certificate will likely have a statement to this effect. The estoppel certificate may also request that the Tenant confirm any increases in base rent amounts that will occur at later points in the lease term. The Lender will also want the estoppel certificate to recite the amount of any security deposit paid, the form of security deposit (cash or letter of credit), and whether, to the Tenant's knowledge, any portion of the security deposit has been applied by the Landlord.

Fifth, the Lender will require statements in the estoppel certificate as to whether there are any defaults by either the Landlord or the Tenant that are then continuing. These types of statements typically include confirmation from the Tenant that all obligations of the Landlord with respect to concessions (i.e., leasing incentives such as free rent and tenant improvement allowances) have been paid in full and that the Tenant does not have any offsets or deductions against rent available to the Tenant. As the Tenant, it is appropriate to add a knowledge qualifier (i.e., to the Tenant's knowledge) to the beginning of these statements regarding defaults, offsets, and deductions to protect the Tenant in the event that there is a default, offset, or deduction the Tenant is not aware of; otherwise, the Tenant may be deemed to have waived these matters.

Finally, the Tenant should be careful with respect to additional statements in the estoppel certificate beyond confirmation of the facts above (such as representations regarding any potential environmental issues) or agreements that could provide the recipient of the estoppel certificate with additional rights. For example, the estoppel certificate may include a fairly straightforward statement such as "So long as the obligations are outstanding, Lender or its designee may enter upon the property to visit or inspect the property." This statement permits the Lender to inspect the property without restriction when, before the estoppel certificate, such rights would have been subject to any terms and conditions in the Tenant's lease.

As a best practice, once you have reviewed and revised an estoppel certificate to be accurate based on the lease documents, you will need to have your client review and confirm each statement as well to ensure that the Tenant provides an accurate picture of the lease and does not waive any of its rights. Further, make sure that every blank in the estoppel certificate is completed and use "Not Applicable" or a similar designation where needed. If the estoppel certificate will be returned along with an SNDA, the Tenant may want to include a notation on the estoppel certificate that it is not valid unless and until the Tenant receives back a fully executed SNDA.

A sample form of estoppel certificate appears at the end of this article.

Conclusion

Lawyers need to understand the basic requirements of Lenders to Landlords with respect to tenant estoppel certificates and SNDAs and the provisions that need to be included in such documents.