

Bankruptcy Judge Slashes Rent Due By Restaurant Tenant During COVID-19

Amundsen Davis Bankruptcy & Creditor's Rights Alert
June 16, 2020

According to at least one bankruptcy judge sitting in the Northern District of Illinois, an appropriately drafted force majeure clause in a lease can excuse a debtor tenant from paying full rent during Illinois' government mandated shutdown over COVID-19. The recently published opinion focused on the force majeure clause between a restaurant tenant and its landlord and read in part:

Landlord and Tenant shall each be excused from performing its obligations or undertakings provided in this Lease, in the event, but only so long as the performance of any of its obligations are prevented or delayed, retarded or hindered by...laws, governmental action or inaction, orders of government ...Lack of money shall not be grounds for Force Majeure.

On February 24, 2020, the restaurant tenant filed its voluntary petition for relief under Chapter 11 of the Bankruptcy Code. According to bankruptcy law, debtors are required to timely perform all obligations they incur during the time of the Chapter 11 case. Regardless, the restaurant tenant did not pay rent to the landlord for the months of February, March, April, May, or June. As a result, the landlord filed a motion to force the restaurant tenant to make the past due rent payments as well as require the timely payment of rent going forward. In response to the landlord's motion, the restaurant tenant asserted that it was not obligated to pay rent under the lease because Illinois Governor J.B. Pritzker's March 16, 2020 Executive Order was a governmental action or order of government which hindered the restaurant tenant's performance. The landlord argued that because the banking system was not shut down by the Executive Order that the force majeure clause was not implicated, that the restaurant tenant was not paying simply because of a "lack of money" as specifically carved out of the force majeure clause, and that the restaurant tenant could have obtained a loan (such as an SBA loan) to assist it in paying rent and therefore the force majeure clause was not triggered. The operative section of that Executive Order stated in part:

Beginning March 16, 2020 at 9:00 p.m. through March 30, 2020, all businesses in the State of Illinois that offer food or beverages for on-premises consumption – including restaurants, bars, grocery stores, and food halls – must suspend service for and may not permit on-

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premises consumption. Such businesses are permitted and encouraged to serve food and beverages so that they may be consumed off-premises, as currently permitted by law, through means such as in-house delivery, third party delivery, drive-through, and curbside pick-up. In addition, customers may enter the premises to purchase food or beverages for carry-out. However, establishments offering food or beverages for carry-out, including food trucks, must ensure that they have an environment where patrons maintain adequate social distancing.

After analyzing both the lease and the Executive Order, Bankruptcy Judge Cassling dismissed each of the landlord's arguments in total, agreed with the restaurant tenant and found that the force majeure clause in the lease was "unambiguously triggered" by the Executive Order. Judge Cassling further found that the Executive Order was "unquestionably" a governmental action and a governmental order, that the Executive Order and its extensions "unquestionably" hindered the restaurant tenant's ability to perform under the lease, and that the Executive Order was "unquestionably" the proximate cause of the restaurant tenant's inability to pay rent. Therefore, Judge Cassling found that the restaurant tenant was excused from paying rent for the months of April, May and June 2020.

However, Judge Cassling's analysis then turned back to the Executive Order and its provisions allowing restaurants to remain open and serve food under special, limited circumstances. Applying that limited authorization to conduct business to the force majeure clause in the lease, Judge Cassling went on to find that to the extent the restaurant tenant could have continued serving food, it was not entitled to the full benefits of the force majeure clause. Specifically, the court held that "the [restaurant tenant's] obligation to pay rent is reduced in proportion to its reduced ability to generate revenue due to the [Executive Order]." To determine the amount of the reduction, Judge Cassling turned to an admission by the restaurant tenant that approximately 75% of its square footage had been rendered unusable by the Executive Order, meaning 25% of its square footage had been available to generate income which could be used to pay rent. Judge Cassling thus decided that the force majeure clause would act to reduce the restaurant tenant's total rent by 75%.

The Judge Cassling opinion could have widespread ramifications for the landlord/tenant relationship both inside and outside of bankruptcy during these times. The opinion should provide tenants – and not just restaurant tenants – a powerful tool to drastically reduce the amount of their rent obligations during these nationwide "stay at home" orders if the leases in question contain relevant force majeure clauses. If you are a tenant entering into a new lease, current world events and this opinion should demonstrate the need for such clauses in every lease. Moreover, the existence of even similar clauses in leases should provide tenants greater leverage to negotiate rent reductions with their landlords during any COVID-19 related shut down. Additionally, while the Judge Cassling

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opinion used a calculation of usable space to determine the proper amount of rent reduction, this was in part because no party provided Judge Cassling with an alternate method to determine that rent reduction. For example, what if the amount of space rendered unusable by the Executive Order was 75%, but the restaurant tenant had experienced a 90% drop in revenue? Might the restaurant tenant have been able to have rent reduced by 90%? A savvy tenant attempting to use the premise of the Judge Cassling opinion going forward might want to be prepared to show exactly how much revenue it lost as a result of any stay-at-home order, compare that to Judge Cassling's usable space model, and be prepared to argue that it is entitled to a rent reduction in the higher amount. However used, this newly published opinion is certain to be a topic of discussion as industries deal with unpaid rent arising from shutdowns because of the coronavirus pandemic.

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