

NYC LOCAL LAW 1932-A MAY ALLOW INDIVIDUAL GUARANTORS OF CERTAIN COMMERCIAL LEASES OR RENTAL AGREEMENTS TO LIMIT PERSONAL LIABILITY

Hodgson Russ Real Estate Alert
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NYC Local Law 1932-A, signed by Mayor de Blasio on May 26, 2020, temporarily prohibits the enforcement of personal liability provisions of lease or rental agreements for certain commercial tenants in NYC impacted by COVID-19 during the period March 7, 2020 to September 30, 2020. As discussed below, the new law may not accomplish fully its intended purpose and is likely to create uncertainty for tenants, landlords, and guarantors concerning its scope and application.

I. What Types of Businesses are Protected?

The bill amends Title 22 of the Administrative Code of the City of New York and temporarily prohibits the enforcement of personal liability provisions (partially or in full) in commercial leases or rental agreements involving four categories of COVID-19 impacted retail tenants:

1. Businesses that were required to stop serving food or beverages for consumption on premises pursuant to Executive Order 202.3 (i.e., restaurants and bars);
2. Businesses that were required to cease operations altogether pursuant to Executive Order 202.3 (e.g., gyms, fitness centers, movie theaters);
3. Non-essential retail businesses that were required to close and/or subject to in-person restrictions pursuant to Executive Order 202.6, and
4. Businesses that were required to close to the public as a result of Executive Order 202.7 (e.g., hair salons, barbershops, tattoo or piercing parlors and related personal care services)

II. What Types of Guarantors Are Protected?

In order to invoke the protections offered by Local Law 1932-A, the guarantor must be: 1) a natural person; and 2) the personal liability provisions must be in the lease or rental agreement. The statute does not protect tenants who signed a lease or rental agreement in their own name. A guarantor which is a limited liability company, a corporation or other entity is also not protected.

Attorneys

Krystal Daniels
Amy Fitch
Warren Gelman
Andrea Gervais
Joseph Goldberg
Elizabeth Holden
Peter Lutz
Brianna Szopinski
Sujata Yalamanchili

Practices & Industries

Real Estate Leasing

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III. What Personal Liability Obligations Are Covered?

Local Law 1932-A temporarily precludes enforcement of personal liability obligations in commercial leases or other rental agreements, wholly or partially, to pay rent, utility expenses and taxes owed by the tenant or fees and charges relating to routine building maintenance.

IV. When Must the Default Occur?

The protections afforded by Local Law 1932-A are limited in time. In order to seek protection under the statute, the guarantor must show that the “default or other event causing [the guarantor] to become wholly or partially personally liable for such obligation occurred between March 7, 2020 and September 30, 2020, inclusive.”

V. What Happens Next?

Local Law 1932-A rewrites and upsets the parties’ bargained for expectations for a host of existing leases and rental agreements. For this reason alone, the statute will almost certainly be subject to legal challenge on constitutional grounds as representing an impermissible impairment of existing contracts. In addition, Local Law 1932-A does not specifically address the typical situation where the guarantor has executed a written guaranty separate and apart from the actual lease or rental agreement. Thus, a court will need to decide whether a separate written guaranty will nonetheless be enforceable against the guarantor because the guaranty is not part of the “commercial lease or other rental agreement.”

Additional confusion (and gamesmanship) is likely to arise given that the protections afforded by the Local Law 1932-A are limited in time, *i.e.*, the defined default period is March 7, 2020 to September 30, 2020. It does not take too much imagination to foresee that one unintended consequence of Local Law 1932-A may be to encourage a tenant in a precarious financial condition to accelerate a default to ensure that the default occurs prior to the September 30, 2020 deadline and thereby seek to insulate the guarantor from personal liability. So, too, it may be anticipated that certain landlords will attempt to push out the default date past September 30, 2020 by applying the tenant’s security deposit to outstanding rent or other arrears arising prior to September 30, 2020.

In short, the statute creates uncertainty for guarantors, tenants and landlords alike and it will take years for these issues to work their way through trial and appellate courts. Perhaps this will encourage all parties to negotiate rather than to litigate their differences, especially given the collective challenges posed by the COVID-19 business landscape.

For any questions you have on NYC Local Law 1932-A, contact Joseph Goldberg (646.218.7615).

Please check our Coronavirus Resource Center and our CARES Act page to access information related to both of these rapidly evolving topics.

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