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Protecting a Commercial Sublandlord from Its Subtenant's Holdover

By Amy Carper Mena

A commercial landlord's damages are generally foreseeable when a tenant fails to surrender possession of the leased premises at the end of the lease term. Such damages typically relate directly to the amount of rent that the landlord would have received upon a reletting of the premises.

But holdover damages may surprise a commercial sublandlord and its subtenant alike when a subtenant holds over, absent careful drafting of the sublease. In such a situation, the sublandlord may be responsible to the prime landlord for use-and-occupancy or liquidated-holdover damages for the entire leased premises, rather than just for the lower rental rates of typically smaller premises that were subleased by the holdover subtenant. In turn, a holdover subtenant that has knowledge of the prime lease's terms may be startled to find that under New York law, it is ultimately liable for the holdover damages of the entire premises, often at an amount many times its own sublease rental rate. Despite the equitable nature of New York law, an unsuspecting sublandlord may lose its right to such damages through thoughtless drafting of subleases.

The purposes of this article are (1) to identify how a sublandlord can incur liability to its landlord as a result of the subtenant's failure to surrender possession of the subleased premises before the prime lease's termination, and (2) to provide practical guidance to a sublandlord so that there may be a greater likelihood of the sublandlord's recouping its losses if its subtenant holds over.

I. New York Law on Holdover Liability

Under New York law, a tenant must surrender possession of the en-

tire leased premises at the end of the lease term, vacant of any sublease.¹ This mandate is true even where the landlord originally consented to the sublease, and where the subtenant holds over without the sublandlord's permission and against its wishes.² A subtenant's wrongful holdover, therefore, creates a sublandlord's wrongful holdover when it prevents the sublandlord from surrendering possession of the leased premises vacant at the end of the lease term.³

A tenant generally subleases its premises because it has no further use for the space that it leased, or because it leased more space than it currently needs, anticipating that it will later move into such space to accommodate its growing business when the sublease term ends. Usually, the rental charged under a sublease is less than the amount payable under the prime lease. This may occur for one of several reasons: the smaller size of the subleased space; the shorter term of the sublease; or the tenant's lower bargaining position as compared to the landlord's. As a result, the damages payable to the landlord when the subtenant holds over may be more than the rent that the subtenant pays to the sublandlord.⁴ For example, assume that the landlord leases premises at the market rate of \$60 per square foot per year, and the sublandlord subleases the entire premises for \$35 per square foot per year. The damages suffered by the landlord due to the subtenant's holdover hypothetically might be almost twice the subtenant's rent, assuming that \$60 per square foot per year is the landlord's use-and-occupancy charge for the holdover period.

Quite soundly, well-settled law provides that a holdover subtenant that is aware of the sublandlord's liability under the prime lease's terms

is liable for the actual amount of damages owed by the sublandlord for a holdover, and not just for the amount of rent charged at the end of the sublease's term.⁵ This is true even where the holdover subtenant paid a lower rent to the sublandlord than the sublandlord paid under the prime lease for the same premises, as illustrated by the previous example, thereby potentially making the subtenant liable for damages almost twice its own rent. For example, in *Phelan v. Kennedy*, a holdover subtenant whose rent was \$81.82 per month was required to pay the full \$175 per month rental paid under the prime lease to the landlord by the tenant for the four months of the holdover term in which the subtenant remained in possession, on a theory of recovery for breach of the covenant to surrender possession and not as rent.⁶

Moreover, the sublandlord's liability to the prime landlord due to its subtenant's wrongful holdover may be even more out of proportion with the rent charged to the subtenant under the sublease if the subtenant subleased only a portion of the entire premises leased to the sublandlord. This is because a holdover of even part of the premises constitutes a holdover of the entire premises.⁷ Thus, using the same rental figures as stated above (\$60 per square foot per year is tenant's rental; \$35 per square foot per year is subtenant's rental), assume that the subtenant has subleased only half of the entire leased premises. Here, if the subtenant wrongfully holds over, thereby creating a holdover of the entire premises, the sublandlord's liability to the landlord may be almost four times the amount of rent charged under the sublease.

Fortunately for the sublandlord, New York law provides that a subten-

ant wrongfully holding over also is liable for the actual amount of damages owed by the sublandlord where the holdover subtenant subleases only a portion of the total premises leased by the sublandlord from the prime landlord. For example, in *1133 Building Corp. v. Ketchum Comm. Inc.*, the Appellate Division concluded that a holdover subtenant was liable for use-and-occupancy charges of the sublandlord's entire leasehold interest in floors 41 through 45, even though the subtenant subleased and held over only on the 44th floor.⁸ Similarly, in *Syracuse Assocs. v. Touchette Corp.*, the Appellate Division found that the subtenant's liability extended to the entire building leased by the tenant, and not merely to the quarter that it occupied past the term's expiration.⁹

The key to holdover damages is that they must be foreseeable, typically at the time of lease (or sublease) execution. A holdover tenant, therefore, will not be liable for consequential damages of a landlord's lost opportunities where the landlord was unable to deliver to a new tenant the premises that included, in part, the premises held over by the tenant, and where the lease does not provide for such damages.¹⁰ Rather, holdover damages will be limited only to the incidental and use-and-occupancy damages concerning the originally leased premises, unless otherwise provided in the lease.¹¹

II. Drafting Subleases to Protect a Sublandlord's Right to Recover Damages from Its Holdover Subtenant

Despite New York law's equitable nature, sublandlords may inadvertently obstruct their ability to avail themselves of the law's protection due to poor drafting of the sublease.

For example, subleases commonly contain provisions that conflict when it comes to holdover damages. One common scenario is for a sublease to incorporate the prime lease

with the exception that financial terms are deleted and replaced with the sublease's financial terms, and the prime lease's references to the term "premises" in the sublease mean the "subleased premises." As a result, a strict interpretation might result in holdover damages' being limited to damages related only to a holdover of the subleased premises, at the rents stated in the sublease. Another example of poor drafting would be to limit holdover damages or rent in the sublease exclusively to the amount of rent due under the sublease (or some multiplier of same).¹²

A sublandlord can protect its right to recover the full extent of its damages in the event of a subtenant's holdover by several simple techniques. First, the sublease should make clear that the subtenant has fully reviewed the prime lease, and, to the extent feasible, the prime lease should be attached as an exhibit to the sublease. By doing this, a sublandlord can avoid any claim by its subtenant that the subtenant was not aware of the amount of the sublandlord's liability to the sublandlord in the event of a holdover of the entire premises demised to the sublandlord. Frequently, sublandlords redact the rental numbers from the copy of the prime lease provided to the subtenant or attached to the sublease. But if such prime-lease rentals are greater than the sublease rent, sublandlords should not redact them. Second, in addition to containing the customary subordination provision that explicitly states that the sublease is subject and subordinate to the prime lease, the sublease should provide that the subtenant shall not do or permit anything to be done in connection with the sublease or the subtenant's occupancy that will violate the prime lease.

Under a belts-and-suspenders approach, a cautious sublandlord could even include in the sublease a specific disclosure to the subtenant of the actual damages that its holdover will cause, and an indemnification from

the subtenant concerning any such holdover damages in the form of a specifically tailored provision perhaps along the lines of the following:

Subtenant acknowledges that (1) under the prime lease Sublandlord must pay holdover damages to the prime landlord with respect to the subleased premises and the remainder of the [____nd] floor of the building in the aggregate amount of \$_____ per month (the holdover damages payable by Sublandlord with respect to the entire [____nd] floor of the building are collectively referred to in this Sublease as the "Holdover Damages") if Subtenant does not surrender the entire subleased premises from and after the expiration of the Sublease's term, (2) Sublandlord's damages resulting from any failure by Subtenant to surrender timely possession of the entire subleased premises from and after the expiration of the Sublease's term will be substantial and will equal or exceed the Holdover Damages payable during Subtenant's holdover, and (3) the Holdover Damages will be the damages actually suffered by Sublandlord on account of any holdover by Subtenant after the expiration date and are not an estimate thereof. Subtenant shall pay to Sublandlord for each month and each portion of any month during which Subtenant holds over in the subleased premises after the expiration of the Sublease's term, for use and occupancy, the Holdover Damages, notwithstanding anything to

the contrary contained in this Sublease or the prime lease. Subtenant shall pay to Sublandlord the foregoing sums upon demand, in full without setoff, and no extension or renewal of this Sublease shall be deemed to have occurred by such holding over, nor shall Sublandlord be precluded by accepting such aggregate sum for use and occupancy from exercising all rights and remedies available to it to obtain possession of the subleased premises. The terms of section _____ of the prime lease will otherwise be applicable to any failure by Subtenant timely to surrender the subleased premises upon the expiration or sooner termination of this Sublease.

In conclusion, holdover subtenants who are aware of the sublandlord's liability to the landlord in the event of a wrongful holdover are responsible under New York law for landlord's incidental and use-and-occupancy damages when they cause a holdover past the expiration of the prime lease's term. Such liability can often be several times the rent that such subtenant pays under its sublease. A sublandlord, to protect its right to recover from such holdover subtenants, should carefully draft the sublease to avoid any confusion or doubt as to its subtenant's liability in the event of a holdover.

Endnotes

1. See *Stahl Assocs. Co. v. Mapes*, 111 A.D.2d 626, 629, 490 N.Y.S.2d 12, 14 (1st Dep't 1985).
2. *Id.* at 629, 490 N.Y.S.2d at 14–15 (citing *Sullivan v. George Ringler & Co.*, 59 A.D. 184, 69 N.Y.S. 38, *aff'd*, 171 N.Y. 693, 64 N.E. 1126 (1902); *Manheim v. Seitz*, 21 A.D. 16, 47 N.Y.S. 282 (2d Dep't 1897)); see, e.g., 1133 *Building Corp. v. Ketchum Comm. Inc.*, 224 A.D.2d 336, 638 N.Y.S.2d 450 (1st Dep't 1996) (holding that the sublandlord was unable to surrender timely possession of its leased premises because its subtenant remained in possession of the subleased premises without the prime landlord's permission for one month beyond the sublease's and prime lease's expiration date).
3. *Stahl*, 111 A.D.2d at 629, 490 N.Y.S.2d at 14 ("It is well settled that a wrongful holding over by a subtenant is to be deemed the same as a wrongful holding over of the tenant sublessor" (citing *Syracuse Assocs. v. Touchette Corp.*, 73 A.D.2d 813, 424 N.Y.S.2d 72 (4th Dep't 1979); *Goodwin v. Humbert*, 216 A.D. 295, 215 N.Y.S. 20, *appeal dismissed*, 244 N.Y. 584, 155 N.E. 906 (1927))).
4. See *Ketchum Comm.*, 224 A.D.2d at 336, 638 N.Y.S.2d at 450–51.
5. See *id.*; see also *Touchette Corp.*, 73 A.D.2d at 814, 424 N.Y.S.2d 72.
6. 185 A.D. 749, 752, 173 N.Y.S. 687, 690 (1st Dep't 1919).
7. See *Ketchum Comm.*, 224 A.D.2d at 336, 638 N.Y.S.2d at 450–51.
8. *Id.*
9. 73 A.D.2d 813, 424 N.Y.S.2d 72, 74 (4th Dep't 1979).
10. See *437 Madison Ave. Assocs. v. A.T. Kearney, Inc.*, 127 Misc.2d 37, 38, 488 N.Y.S.2d 950, 951 (Sup. Ct. App. Term 1st Dep't 1985). The landlord, in the instant case, entered into a new lease agreement with an incoming tenant that bundled an existing tenant's premises with additional space in the building. When the existing tenant held over, the landlord was unable to deliver timely the incoming-tenant's entire premises. The landlord claimed

- that the holdover tenant should be liable for the rent for the entire premises to be leased to the incoming tenant, not just for the premises leased holdover tenant. The court denied consequential relief to the landlord, finding no reason to depart from the rule limiting landlord's remedy to removal of the tenant, incidental damages, and use and occupation, absent an agreement in the holdover tenant's lease providing otherwise. *Id.* at 38–39, 488 N.Y.S. at 951.
11. See *id.* But note a recent line of Appellate Division, First Department, cases have found that a holdover tenant or subtenant may be liable to a new tenant for tortious interference with contract concerning the new tenant's lease. See *Havana Central NY2 LLC v. Lurney's Pub Inc.*, 49 A.D.3d 70, 72–73, 852 N.Y.S.2d 32, 34 (1st Dep't 2007) (holding tortious-interference-with-contract claim sufficiently plead by new tenant against a holdover tenant where landlord could not timely deliver premises to incoming tenant due to existing tenant's holdover, even though the new lease provided that landlord had no liability to new tenant for failure to deliver timely the premises due to tenant's holdover); *Kronish Lieb Weiner & Hellman LLP v. Tahari, Ltd.*, 35 A.D.3d 317, 829 N.Y.S.2d 7 (1st Dep't 2006) (finding new tenant to have sufficiently plead the causation element of tortious interference of contract and trespass against a holdover subtenant where such holding over delayed delivery of the premises to the new tenant). An analysis of damages owed to third parties as a result of holdovers, based on a tort rather than a contract theory, is beyond the scope of this article.
 12. See *Edward W. Jessen et al.*, 7 *Real Property Service New York* § 69.49 (2008 Cumulative Supp.) A form of sublease provides that holdover rent will be the same rate of rental in effect at the time of the sublease's termination. *Id.*

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