The Law

Lease Requirements Apply to Extensions

by Ron Davis

Must a shopping center tenant pay a full amount of rent for a period when the center's occupancy rate plunges?

Recently posing that question was the clothing retailer Old Navy. And attempting a credible response were the owners of Hastings Village, a Pasadena, CA, shopping center where Old Navy operates a store.

At stake in the answer was a sizable amount of rental money to which both parties laid claim. Moreover, both presented credible arguments that only the law courts could resolve.

Old Navy has leased space at Hastings Village since 1999. The initial term was for five years, but old Navy had the option of extending the tenancy for two additional five-year periods. And that's what Old Navy has done.

A key provision of that lease gave Old Navy another key option. Old Navy could pay a much lesser amount of rent if the center's occupancy rate ever drops below 70 percent.

In 2008, that happened. A retail furniture tenant closed, meaning that the occupancy rate did in fact fall below 70 percent. Old Navy was quick to take advantage of that consequence and started paying the reduced amount of rent.

The center's owners responded by threatening legal action against Old Navy, arguing that the 70-percent occupancy benefit applied to only the first five years of Old Navy's lease term. Old Navy reluctantly paid the full rental amount, but then claimed that the lease allows a rental break during the tenancy at any time the occupancy-rate level falls below 70 percent.

In fact, the language of the lease was somewhat vague as to the leasing periods when the 70-percent standard applied.

But a California court determined that the requirements extended beyond the initial period of the lease. The judge therefore ruled in favor of Old Navy, awarding it a sum of $706,418.22.

The center's owners appealed that ruling.

A California appellate court agreed with the lower court, explaining, “The plain language of the [lease] requirements and remedies shows that they applied to the entire term of the agreement, including extensions…. As an alternate remedy when the requirements were not being met, Old Navy could remain open for business and pay the lesser of the alternate rent or the minimum rent ‘then applicable.’ The five-year limitation limits Old Navy’s obligation to operate the business. It did not limit the application of the lease requirements. It would be unreasonable to find the requirements did not apply after the first five years when the lease specifically sets forth the charges that Old Navy must pay if it closes after the first years and the requirements are being met.”

(Hastings Village Investment Company v. Old Navy, LLC, 2011 WL 2306854 [Cal.App. 2 Dist.])

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