New York Law Journal
SERVING THE BENCH AND BAR SINCE 1888
WWW.NYLJ.COM

An ALM Publication
VOLUME 244—NO. 93
FRIDAY, NOVEMBER 12, 2010

Outside Counsel

Expert Analysis

Default Notices Under Commercial Leases: Avoiding Pitfalls

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The most important document in most commercial lease litigations is the notice of default.

Most litigation under commercial leases arises from tenant defaults.[1] In most leases there is a procedure whereby the landlord may unilaterally end the term prematurely in the event of an uncured material default by the tenant. The first step in the procedure is usually service of a notice of default.

Often, a notice of default is hastily prepared and served to test the waters: perhaps the tenant will cure, surrender possession, or become amenable to a favorable settlement. This approach is fraught with hazard. If litigation ensues, any defects in the hastily prepared notice may sabotage an otherwise meritorious case. On the other hand, where the notice is prepared properly, the landlord has already gone a long way toward preparing its prima facie case. The default has been identified with particularity, the lease provisions giving way to termination have been dissected, and the elements of the landlord's case have been set forth. The notice of default should be prepared in anticipation of litigation.

Context of the Notice

An option to terminate based upon a tenant's default must be exercised in strict compliance with the provisions of the lease. In most cases the tenant must be provided with an opportunity to cure. The means by which this opportunity is provided is the notice of default.

Some commercial leases, particularly older leases, contain a provision known as a "condition subsequent," a right to terminate upon the occurrence of a particular event. The occurrence of the event does not automatically end the term of the lease, it merely gives the landlord the right to end the term, typically by prosecuting an action for ejectment. Much more typical is a "conditional limitation" provision. Under such a clause, the term of the lease automatically terminates upon the occurrence of the stipulated contingency. The landlord may then prosecute a summary holdover dispossess proceeding based on the tenant's holding over in possession after termination.[2] The conditional limitation clause is the norm in modern commercial leasing in New York. Where conditions subsequent are seen it is usually because an attempt to draft a conditional limitation was unsuccessful.

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Under a typical conditional limitation clause, the tenant's failure to cure the alleged default within the stipulated time after service of a written notice of default is the event which triggers the landlord's entitlement to serve a notice of termination. Service of the notice of termination is the final act which effectuates the early end of the lease term.[3] The landlord's right to terminate is thus dependent upon service of a properly prepared notice of default. Unless the notice is prepared and served in strict compliance with the lease and a wide spectrum of case law, there will be no termination, no holdover, and no eviction.

Contents and Service

The law abhors a forfeiture. This is especially so for a forfeiture of an estate in real property, such as a long-term leasehold.[4] Lease provisions giving the landlord the right to terminate are therefore strictly construed. Defects which may seem minor and non-prejudicial will render the notice ineffective.

In many cases the tenant will lack a strong substantive defense on the merits of the alleged default; and the primary issue in the litigation will be whether the landlord's exercise of its right to prematurely terminate was performed in accordance with the procedure required by the terms of the lease and the applicable case law.

The notice of default must be clear, unambiguous and unequivocal. It must place the tenant in a position where it may know with certainty that it must either cure the default or the landlord will serve a notice of termination, and that the term will automatically expire on the date set forth in the notice of termination.[5] A notice of default which states that unless the default is timely cured the landlord will "exercise its remedies under the lease," or that the landlord "reserves all its rights and remedies," will be ineffective.[6]

The notice of default must specifically apprise the tenant of the claimed default. It must specifically describe the facts which constitute the alleged default. It must cite the provisions of the lease alleged to have been violated, as well as the provisions of the lease pursuant to which it is being issued.

The degree of specificity required is considerable. In *Chinatown Apartments Inc. v. Lam*[7] the notice alleged that a "partition" had been erected on the premises in violation of the lease. In fact the tenant had erected a cube-like structure. The landlord maintained that the tenant should have known that the reference to a "partition" meant the structure, and that since the lower court had permitted an amendment of the pleading to allege the structure any ambiguity had

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been dispelled. The Court of Appeals disagreed, stating "since the right to terminate the tenancy pursuant to the terms of the lease was dependent upon service of an adequate notice, a subsequent amendment of the petition, which could not operate retroactively to cure a defect in the notice, did not enhance petitioner's right to relief." The Court stated that the tenant could not be expected to take remedial steps unless the landlord first demonstrated in the notice of default that such steps were required by the lease.

It is essential that the alleged breach be material. Only where a tenant has breached a material covenant of the lease will termination be countenanced. "Equity will intervene to prevent a substantial forfeiture occasioned by a trivial or technical breach. To permit literal enforcement of the instrument in such circumstances…is to elevate the nonperformance of some collateral act into the cornerstone for the exaction of a penalty."[8] If the covenant is designed to effectuate one of the purposes of the lease it will be material.[9]

It must be unequivocally clear that the notice emanates from the landlord. "Where a contract expressly provides that it may be terminated by a notice in writing, the notice must be signed or authenticated by, or at least purport to emanate from, the party who undertakes to give the notice."[10]

In *Siegel v. Kentucky Fried Chicken of Long Island Inc.*[11] a notice of default signed by the landlord's attorney was ineffective where the attorney was not named in the lease as authorized to act for the landlord in such matters, the tenant had never previously dealt with the attorney, and the notice was not authenticated or accompanied by proof of the lawyer's authority to bind the landlord.

The Appellate Division, Second Department, stated that the tenant is "entitled to know whether his landlord is insisting upon the strict performance of all of the covenants of the lease, i.e., whether the only person who is entitled to insist upon full compliance actually desires that these often technical defaults be cured. In addition, and more important, if the tenant is also entitled to know 'with safety' whether the notice to terminate emanates from a person with the requisite authority, for if he acts upon such notice to vacate the premises, he may later be found to have acted at his peril should the landlord prevail in a claim that the notice was unauthorized."

Even where the attorney is named in the lease, the safest course is to have the landlord sign the notice. Where the landlord is not a natural person, the authority of the individual who affixed its signature should be set forth.

The notice must unambiguously set forth the tenant's deadline to cure. Often, the drafter will measure the time to cure by incorporating the language of the lease, for example by stating that the default must be cured "on or before the expiration of 20 days from the date of service of this notice." Such language is problematic and often ineffective. The "date of service" is a mixed question of fact and law which may be open to interpretation.[12] For example, if the notice is served both by hand and by mail, when is the "date of service"? Upon receipt by hand delivery? Upon dispatch by mail? Upon receipt by mail? Even if an answer is readily apparent based on an analysis of the lease, the mere appearance of ambiguity may be enough to significantly delay the case by motion practice.

In the absence of a lease provision to the contrary, a notice served by mail will be deemed given when received; and the time to cure will be computed from the time of receipt. In *Grabino v. Howard Stores Corp.*[13] the lease required a "five (5) days written notice." The notice was dated April 7. It provided that the default must be cured "within five (5) days from the date of this letter." It was served by certified mail. The tenant received it on April 9. The Kings County Civil Court held that the notice was ineffective because it did not provide the required five days notice.

It is noted that even if the lease had provided that notices are deemed given upon dispatch by mail, the tenant could still have argued that the actual time to cure after its receipt of the notice, three days, was unreasonable. As held by the Appellate Division, First Department, in one case, "the provision for three days notice by mail of the termination of the lease, deemed given when mailed, is so lacking in equity and due process as to be ineffective as a predicate for cancellation of the lease."[14]

To avoid ambiguity, the tenant's deadline to cure should be set forth as a date certain. The only question then will be whether the notice will be considered to have been given sufficiently in advance of the date certain so as to provide the tenant with the minimum notice required under the lease. The date certain must therefore be carefully calculated in advance, taking into account the relevant provisions of the lease. This may require strict attention to several interdependent lease clauses. For example the "default" provision may require a "five day notice to cure"; the "notices" provision may require notices to be served by certified mail; and the lease may elsewhere provide that notices are deemed given on the third business day after dispatch.

To be safe, more notice than is required should be provided, so that the tenant cannot legitimately claim prejudice. Providing a few extra days may remedy an otherwise fatal error in the drafting or service of the notice. The cost of giving the tenant a few days extra notice is minimal when compared to the risk of having an otherwise meritorious case dismissed, or delayed by avoidable motion practice.

Conclusion

A key strategic point in litigation is to plan the case in advance so as to avoid as many issues as possible. Every issue is a potential time delay, even if decided favorably. Issue limitation is the key consideration in preparation of a notice of default.

To prematurely end the term of a lease based on a tenant default, there is a chain of events which must occur: (i) a material default, (ii) service of the notice of default, (iii) expiration of the required time period of opportunity to cure, (iv) service of the notice of termination, and (v) commencement and prosecution of a summary holdover dispossess proceeding. Each step is dependent on the others and must be carefully executed. But it is upon preparation of the notice of default that the entire strategy is properly to be planned. A well planned notice of default renders the remainder of the steps relatively simple to perform. On the other hand, less than careful drafting and service of the notice may render the entire effort unsuccessful.

1. Where the alleged default is nonpayment of rent, the landlord may commence a summary nonpayment dispossess proceeding. It is a statutorily required pre-condition to commencement of such a proceeding that the landlord make a "demand of the rent," typically accomplished by service of a written rent demand notice. RPAPL §711(2). The content and service of such notices are governed by extensive statutory and case law outside the scope of this article.

2. Under some circumstances, upon service of the notice of default the tenant may obtain an injunction tolling its time to cure (and thus disabling the landlord from serving a notice of termination) pending adjudication of the tenant's action for a declaratory judgment, commonly known as a *Yellowstone* injunction. A discussion of *Yellowstone* injunctions is beyond the scope of this article.

3. *Kirschenbaum v. M-T-S Franchise Corp.,* 77 Misc.2d 1012, 355 N.Y.S.2d 256 (Civ. Ct. N.Y. Co., 1974).

4. *Lake Anne Realty Corp. v. Sibley*, 154 A.D.2d 349, 545 N.Y.S.2d 828 (2d Dept. 1989).

5. *Kirchenbaum*, supra.

6. See e.g. *Filmtrucks Inc. v. Express Indus. and Terminal Corp.*, 127 A.D.2d 509, 511 N.Y.S.2d 862 (1st Dept. 1987), see also *49 West 12 Tenants Corp. v. Seidenberg*, 6 A.D.3d 243, 774 N.Y.S.2d 339 (1st Dept. 2004).

7. 51 N.Y.2d 786, 433 N.Y.S.2d 86 (1980).

8. *Fifty States Mgt. Corp. v. Pioneer Auto Parks*, 46 N.Y.2d 573, 576-77, 415 N.Y.S.2d 800, 802 (1979).

9. *Harar Realty Corp. v. Michlin Hill Inc.*, 86 A.D.2d 182, 449 N.Y.S.2d 213 (1st Dept.), appeal dismissed, 57 N.Y.2d 836, 455 N.Y.S.2d 763 (1982).

10. *Bannerman v. Hughes*, 188 N.Y.S. 410 (1st Dept. 1921).

11. 108 A.D.2d 218, 488 N.Y.S.2d 744 (2d Dept. 1985), aff'd, 67 N.Y.2d 792, 501 N.Y.S.2d 317 (1986).

12. See *95 River Co. v. Burnett*, 160 Misc.2d 294, 608 N.Y.S.2d 786 (Civ. Ct. N.Y. Co. 1993).

13. 110 Misc.2d 591, 442 N.Y.S.2d 714 (Civ. Ct. Kings Co. 1981).

14. *57 E. 54 Realty Corp. v. Gay Nineties Realty Corp.*, 71 Misc.2d 353, 335 N.Y.S.2d 872 (1st Dept. 1972).