Using Tenant Estoppel Letters to Cut to the Chase

By Brent C. Shaffer

Tenant estoppel letters cut to the chase. These devices, customarily used in commercial real estate transactions, inform lenders and buyers of the tenant’s understanding of the lease agreement. An estoppel letter can also elicit information that will determine whether a proposed project is financeable.

A real estate lender’s primary concern is not about market value or replacement value of a property but rather the income stream from the property and the continuous receipt of that stream. In a closing with hundreds of pages of documents, the humble estoppel certificate, often being a document of two pages or less, is typically the only independent verification of all of the underwriting assumptions about the loan’s repayment source. More importantly, the estoppel certificate comes directly from the tenant, which is the ultimate source of the loan repayment.

Because the tenant estoppel letter verifies the assumptions made in the loan approval process, its significance to the real estate transaction can be greater than the landlord’s rent roll. The tenant estoppel letter not only confirms the rent roll figures and certain terms of the lease that have been reviewed and relied upon by the lender, but it also seeks to bring to light any potential conflicts and problems in the future flow of the income stream. In addition, a properly worded tenant estoppel certificate can be used to “smoke out” any liabilities and exposures of the landlord (or a purchaser, foreclosing lender, or purchaser at a foreclosure sale) to the tenants. For this reason, the estoppel letter should be required for both noncredit tenants (i.e., those that are not required for the real estate’s self-sufficiency) as well as for credit tenants. The importance of a tenant estoppel certificate diminishes only to the extent that a transaction is underwritten using repayment sources other than real estate rents.

Case Law Involving Tenant Estoppel Certificates

A tenant estoppel letter is a representation by a party signing the certificate to the addressee of the certificate. It is given effect not on the basis of contract law principles but on alternative theories of promissory estoppel and waiver. Although a tenant estoppel certificate is not a contract, it can serve to modify or amend the lease, to clarify defects in leases, and to prevent the tenant from raising other affirmative defenses.

Estoppel Letters

Using Tenant

Tenant Estoppel Letters

To Cut to the Chase

By Brent C. Shaffer

Because the tenant estoppel letter verifies the assumptions made in the loan approval process, its significance to the real estate transaction can be greater than the landlord’s rent roll.

1. Promissory Estoppel. Promissory estoppel arises if the recipient can demonstrate the existence of a clear and unambiguous statement upon which the recipient reasonably relied and sustained an injury as a result of such reliance. In re Calero, Inc. - NY, 217 B.R. 121, 134 (Bankr. S.D.N.Y. 1998). Thus if a lender or purchaser receives an estoppel certificate that contains a statement that is later contradicted, repudiated, or challenged by the tenant, the lender may be able to defeat the tenant’s challenge because of contrary representations in the estoppel certificate.

2. The language in the estoppel certificate is strictly construed against the drafting party. Grandnorthern Inc. v. West Mall Partnership, 359 N.W.2d 41, 45 (Minn. Ct. App. 1984). A statement that a lease “has not been assigned, amended, modified, supplemented, or rescinded since the date of the Lease” did not preclude a tenant’s claim that the lease had not been “extended.” Id. Cases such as Grandnorthern have led practitioners to insert strings of seemingly repetitive synonyms in estoppel certificates.

3. Equitable Estoppel. A recipient of an estoppel certificate can also claim that a tenant is estopped from asserting matters in conflict with the contents of the certificate on the basis of equitable estoppel. Equitable estoppel theoretically differs from promissory estoppel in that it requires different elements of proof. In practice, however, the cases dealing with estoppel certificates tend to ignore the distinctions between the two, with the resulting “estoppel” theory containing elements of both. For example, in applying equitable estoppel to a landlord estoppel certificate under Illinois law, a federal district court required that six elements be met: (1) the signer of the estoppel certificate must have had knowledge at the time the representations were made that they were untrue; (2) the truth regarding the representations must be unknown to the recipient of the estoppel certificate when the representations were made and when the representations were acted on by the recipient; (4) the signer of the certificate must intend or reasonably expect that his or her conduct or representations will be acted upon by the recipient of the certificate or the public generally; (5) the recipient of the certificate must have in good faith relied upon the misrepresentation to his or her detriment; and (6) the recipient of the certificate would be prejudiced if the maker of the certificate is permitted to deny the misrepres-
The importance of a tenant estoppel certificate diminishes only to the extent that a transaction is undertaken using repayment sources other than real estate rents.

As of April 9, 1992.\textsuperscript{2} Transfers Ins. Co. v. Lifelong Enter., Inc., 799 F. Supp. 641, 645 (E.D. La. 1992). In that case, the court found that the estoppel letter had confirmed a termination date of April 30, 1992. Similarly, estoppel certificates with terms that vary from the lease have led courts to entertain terms of the lease in accordance with the estoppel certificate. In a New York case, for example, a lease stated that the tenant had to pay its pro rata share of management fees “normal and usual for the market area.” Red N’ Bath of Spring Valley, Inc. v. Spring Valley P’ship, 586 N.Y.S.2d 416, 417 (N.Y. App. Div. 1992). The tenant had signed a tenant estoppel certificate in which it stated that it had had that obligation and in which it acknowledged that management fees were “four (4) percent of the gross rentals paid to the Landlord under all leases of the Premises.” The court held that the tenant was estopped from claiming that normal and usual management fees were some lesser amount. Id. at 417–18. On the basis of such cases, a statement in an estoppel certificate that contradicts a provision of the lease, even when the lease contains an integration clause and a clause providing that it cannot be amended except by an instrument signed by both landlord and tenant. As a written instrument, an estoppel certificate must trump oral testimony, for example, in interpreting any missing language in leases. Such a result is evidenced by the California appeals court decision in Plaza Freeway Ltd. P’ship v. First Mountain Bank, 96 Cal. Rptr. 2d 865 (Cal. App. 2000). In that case, the landlord and tenant failed to comply with the typical lease provision for space under construction and stated that the parties would execute a memo confirming the commencement date of the lease. On appeal, the court determined that the commencement date was as stated in an estoppel certificate of a successor landlord, so that the tenant failed to exercise a lease extension option in a timely manner. The court applied Section 622 of the California Evidence Code, which states that “facts recited in a written instrument are conclusively presumed to be true as between the parties,” and thus disregarded the tenant’s testimony regarding a later opening and commencement date. Id. at 866, 874.

Lease Provisions Regarding Tenant Estoppel Certificates

For a project to be financeable, its leases must include a provision requiring the tenant to sign an estoppel certificate when requested by the landlord or the landholder’s lender. Such language should be contained in a separate section of the lease, independent from language requiring execution of subordination, nondisturbance and attorney agreements, so that the estoppel certificate requirements can easily be identified and not be inadvertently tied to other lease provisions. The estoppel certificate section should require the tenant’s direct execution of a certificate and set forth what language is to be included in the certificate, the time period within which the certificate is to be delivered, and the consequences for the tenant’s failure to deliver the estoppel certificate within the requested time period. The tenant has sign the estoppel certificate within the requested time period. The reason for this approach is that the certificate, the time period within which the certificate is to be delivered, and the consequences for the tenant’s failure to deliver the estoppel certificate within the requested time period. Therefore, if the tenant consents to the lease is in full force and effect;

• the commencement date of the lease;

• the termination date of the lease;

• whether there are any remaining options to lease additional space in the landlord’s buildings;

• whether there is any right to purchase the lease premises;

• whether the tenant is in default under the lease;

• the base rent or minimum rent payable under the lease;

• the percentage rent payable under the lease;

• current common area maintenance charges payable by the tenant under the lease;

• the security deposit posted with the landlord by the tenant;

• whether any rent has been prepaid;

• the date through which rents have been paid (together with a statement that all previous taxes, insurance and other charges have been paid in full);

• that the tenant is in occupancy of the premises and is open for business.

Lenders also seek to add additional items to this list, such as:

• that the landlord has completed all improvements required to be made by the landlord to the leased premises;

• that the tenant has not violated any applicable environmental laws or transported, used, or generated any hazardous substances;

• that the tenant will provide the lender an additional cure period to remedy landlord defaults;

• that the tenant has not simultaneously send the lender copies of all notices sent to the landlord;

• that the tenant is solvent;

• that the tenant is not in bankruptcy and has not made an assignment for the benefit of creditors;

• that the tenant has not subleased or assigned the lease;

• the tenant’s notice address;

• that the tenant has made no agreements regarding free rent;

• that the landlord has performed all maintenance obligations under the lease;

• that the tenant is not a party to any litigation regarding the premises; and

• that the tenant will not modify the lease without the lender’s prior written consent.

Many of these “additional items” theoretically are subsumed by the more general statements in the first group above, such as the statement that the tenant is not in default under the lease. But to the extent that estoppel certificates are strictly construed, this further clarification may be prudent.

• Requested Form. An alternative to the itemized list of contents is a simple lease requirement that the tenant sign an estoppel certificate requested by the landlord. Obviously, giving an estoppel statement in the form requested by the landlord should be completely unacceptable to a tenant, because such an estoppel certificate could remove substantial leverage of the tenant in dealing with the landlord. In future disputes, including disputes about lease problems that have arisen but of which the tenant has no knowledge because of lack of investigation. On the other hand, “reasonably requested” language permits the ten-
request almost every week. The problem with this third approach is that when the lease is executed by the landlord, the lender (construction, permanent, and refinancing) is not usually a party or even a factor in the negotiations. A third alternative, which is almost universally found in leases to credit or anchor tenants, is the estoppel certificate, which is almost always attached, even in accordance with an attached form. One cannot underestimate the helpfulness of this approach for a chain store tenant, who is likely a tenant in a number of locations nationally, will receive at least one estoppel certificate attached to the lease. Similarly, when a lender requests an estoppel certificate, a strong tenant has an advantage in its interpretation of the language of the certificate itself, especially if it is a key tenant from which the lender absolutely must have an estoppel certificate. Often, some small noncredit tenants may try to withhold estoppel certificates in the affirmative defenses. This approach could backfire, however, because the landlord has more to lose if it seeks to enforce a lease against a small tenant the tenant's failure to comply with the lease requirements to deliver an estoppel certificate. Some small, unsophisticated tenants may view the estoppel certificate request from the landlord as an opportunity to extract additional considerations when the lease contains clear language requiring a satisfactory estoppel certificate. In this situation, the landlord should be certain that it understands its legal exposure while at the same time to convince the lender not to pressure the landlord into having to make concessions to the tenant to obtain the certificates. The appropriateness of the statements in the tenant estoppel certificate depends largely on four factors: the estoppel certificate requirements in the lease, as discussed above; the overall bargaining power and leverage of the tenant, especially when viewed in comparison to the other tenants in the project; the nature of the project itself, and the true nature of the financial transaction (i.e., whether it is a true "real estate loan" for which the rent stream is the primary or only source of repayment. Regardless of these four factors, however, there are additional concerns that nearly always apply for estoppel certificate clauses. Effect of Lease Language. The estoppel certificate clause in a lease usually sets forth only in general terms the requirements to be contained in the certificate. Lenders will typically ask for more. A tenant with significant clout, whose lease is sufficient to make the project viable, often will attempt to limit the term of the lease, thereby preserving the benefit of any language negotiated when the lease is drafted. In certain situations in which such a position is that the loan is based on the strength of the project and the strength of the certificate so that an estoppel certificate will be made even though the estoppel requirements contained in the lease may not be entirely palatable to the lender. Although the tenant wants to have a financially healthy landlord, the tenant may reason that it is better off challenging the statements made by the landlord on the tenant's behalf later, rather than providing the estoppel certificate itself. To help the landlord guard against this gamesmanship, land- landlords are especially notorious for making sure that the "bottom line" estoppel certificate requirements in the lease are not only satisfied but also that the certificate is not "generous" or "generally" worded. Although a tenant may have the legal right to restrict the representations in the certificate to the specific language required in the lease, the tenant may not be able to do so. The tenant may reason that the landlord is likely to do it and is better off making the certificate to the minimum language of the certificate itself, especially if it is a key tenant from which the lender absolutely must have an estoppel certificate. The belief that the lender may need to withhold estoppel certificates in the loan. The most onerous tenant is that the loan is based on the nature of the financing transaction, and to prevent the tenant from raising other affirmative defenses. tenant's verification of the lease terms and status of the lease relationship, the lender is left with no independent verifi- cation of the underlying assumptions of the "laundry list" suggested above (at least if qualified) consists entirely of reasonable statements.

**Attached Form.** A third alternative, which is almost universally found in leases to credit or anchor tenants, is the estoppel certificate, which is almost always attached, even in accordance with an attached form.

**Authorizing the Landlord to Sign.** To deal with the landlord's dilemma if a recital tenant does not produce a lender's requested estoppel certificate in time for a loan closing, many leases contain a clause that allows the landlord to sign an estoppel certificate as tenant's attorney-in-fact if the tenant delays beyond a specified number of days. Although not entirely free from doubt, case law validating powers of attorney in loan documents indicates that such provisions naming the landlord as a tenant's attorney-in-fact for this limited purpose are enforceable if they are "coupled with an interest." See Win v. Rousemaner's Adm., 21 U.S. 174, 219 (1823) (a power of attorney given as security or coupled with an interest is irrepealable even upon the death of the principal). Although such clauses exist, however, do not and should not rely on such a certificate. Without the tenant's verification of the lease terms and status of the lease relationship, the lender is left with no independent verifi- cation of the underlying assumptions of the "laundry list" suggested above (at least if qualified) consists entirely of reasonable statements. Some practitioners believe that the power of attorney clause is useful in putting pressure on the tenant to sign the certificate within the required peri- od. But the tenant may believe that project financing is not jeopardized by its failure to deliver this certificate. Some may reason that it is better off chal- lenging the statements made by the landlord on the tenant's behalf later, rather than providing the estoppel certificate itself. To help the landlord guard against this gamesmanship, lan-

**Nature of Project.** Language that is essentially an affirmative defense to an estoppel certificate will depend on the nature of the project and the terms of the particular lease. For example, statements about base rent or common area main- tenance charges alone are not sufficient for retail leases with percentage rent provisions. Estoppel certificates obtained for construction loans when the tenant is not yet in occupancy will obviously need to omit statements about the landlord's completion of all construction obligations under the lease. The condition of the premises, statements about the tenant's being in occupancy, and several other options are suggested. **Nature of Financing Transaction.** The type and source of the financing also affect whether or not the lender requires in the estoppel cer- tificate. The most onerous tenant estoppel certificate forms still come from traditional institutional lenders, such as pension funds and life insur- ance companies. These requirements become less flexible as the dollar amount of the financing exceeds certain thresholds. Life insurance compa- nies and pension funds ask for most of the statements discussed in this article, initially unqualified, and often require- other provisions that may more prop- erly be classified as lease amendments. Such provisions may include state- ments about future compliance with environmental laws, requirements for copies of all notices and corre- spondence to the landlord, the ten- ant's right to withhold estoppel certificates, and clauses that the landlord is not to assert defenses against successor tenants. **Tenant Bargaining Power.** Generally, the lender absolutely must have an estoppel certificate. Similarly, when a lender requests an estoppel certificate, a strong tenant has an advantage in its interpretation of the language of the certificate itself, especially if it is a key tenant from which the lender absolutely must have an estoppel certificate. Often, some small noncredit tenants may try to withhold estoppel certificates in the affirmative defenses. This approach could backfire, however, because the landlord has more to lose if it seeks to enforce a lease against a small tenant the tenant's failure to comply with the lease requirements to deliver an estoppel certificate.

Although a tenant may have the legal right to restrict the representa- tions in the certificate to the specific language required in the lease, the tenant may not be able to do so. The tenant may reason that it is better off making the certificate to the minimum language of the certificate itself, especially if it is a key tenant from which the lender absolutely must have an estoppel certificate. The belief that the lender may need to withhold estoppel certificates in the loan. The most onerous tenant is that the loan is based on the nature of the financing transaction, and to prevent the tenant from raising other affirmative defenses.
defaults that have not yet come to light. The lender may reject such a qualified statement on the basis that the tenant could perform requisite due diligence to verify the facts. In practice, however, such due diligence is nearly impossible and certainly not possible in the time frame typically required for delivery of the estoppel certificate. In addition, even if a tenant were comfortable in doing this, such an unqualified statement can remove nearly all of the tenant’s leverage in dealing with the landlord in future situations.

One example of rights that a tenant may be relinquishing by stating that there are no defaults under the lease relates to the landlord’s calculation and billing of common area maintenance charges. An unqualified statement in the estoppel certificate could mean that the tenant is giving up rights to audit the calculation of these charges. This is a particular dilemma in leases in which monthly expense charges are paid based on estimates and then later reconciled when records are available. The careful lender also should prune budding problems that have not yet ripened into an actual event of default. One way to do this is through a “no default” clause in the estoppel certificate that states that there is no condition existing that, after the giving of notice or the expiration of any applicable cure period or lapse of time, would be a default.

Statements to the effect that all rent has been paid through a certain date or that no rent has been paid in advance also deserve special scrutiny. Although it is probably not prejudicial to a tenant to state the current amount of additional rent or monthly common area maintenance charges due. Less beneficial to a tenant, but a possible compromise that may preserve the tenant’s ability to recover, would be to make cross-references to lease sections containing the formulas for such rents and state that the tenant has paid all such rent “in accordance with the terms of the lease.”

Other statements that the tenant will want to avoid making (and, conversely, that the lender will want) are that insurance proceeds will be applied as stated in the lender’s mortgage or deed of trust, not as negotiated in the lease; that amendments to lease provisions require the prior approval of the lender (although the tenant may accept such a requirement if the lender’s consent is not to be unreasonably withheld or delayed); and that the tenant will simultaneously send to the lender all notices sent to the landlord (the tenant may agree to notices sent at about the same time or may want to limit required notices to the lender to notice of conditions that would allow the tenant to terminate the lease or of material defaults of the landlord).

The tenant may wish to limit to the “tenant’s actual knowledge” or “knowledge without investigation or inquiry” several other statements that are commonly requested, such as statements about environmental conditions, about the landlord’s satisfactory completion of the tenant improvements, confirming no right by law to terminate the lease, that the tenant’s use complies with applicable zoning or land-use requirements, and that the tenant’s fit-out of the premises is in compliance with all applicable laws.

The landlord must be extremely vigilant in making sure that the “bottom line” estoppel certificate requirements in the lease are sufficient to satisfy its likely sources of financing.