



Insolvency and its effects on commercial leases
The tenant easement as a hedging instrument

Presentation & Agenda

Speakers



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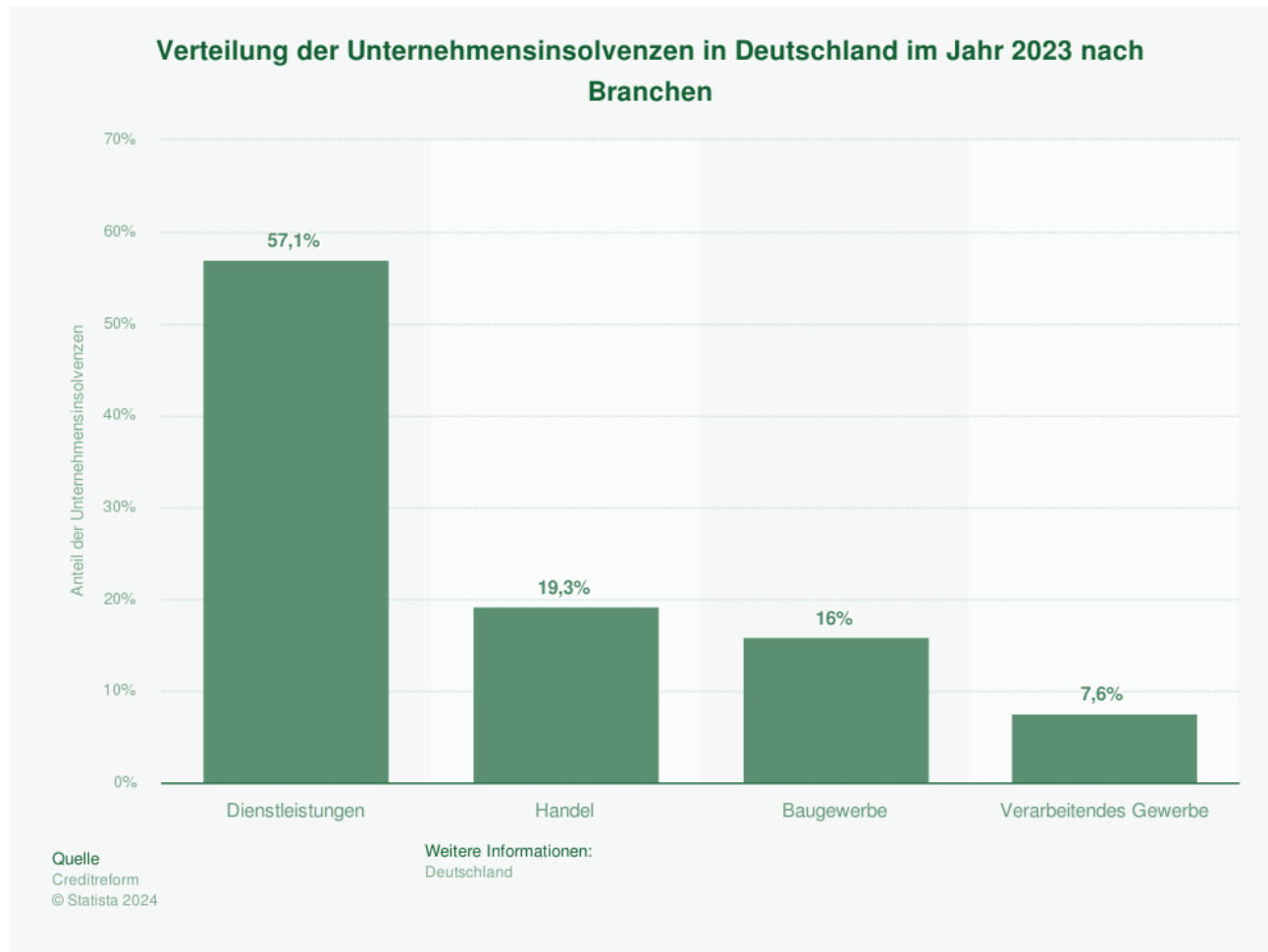
Agenda

- I. Introduction
- II. Insolvency during the tenancy
 - 1. Consequences of landlord insolvency
 - 2. Consequences of tenant insolvency
- III. Tenant easement
 - 1. Use as a hedging instrument
 - 2. Do's and don'ts - avoiding pitfalls
- IV. Questions & Answers



II. Effects of insolvency on the commercial tenancy

Overview of the current situation



- 27.6% more corporate insolvencies in January 2024 than in January 2023

(Source: Federal Statistical Office, press release no. 152 dated April 12, 2024)

II. Effects of insolvency on the commercial tenancy


Overview of insolvency proceedings

- Insolvency proceedings regulate the rights of individual creditors if the debtor is insolvent
- Objective: best possible realization of assets and equal distribution of insolvency assets to creditors
- Initiated by way of application; the local court has jurisdiction
- As a rule, assignment of an insolvency administrator
 - ➔ Transfer of the debtor's assets and power of disposal over the insolvency estate to the insolvency administrator
- Differentiation:
 - **Creditors of the estate:** Can demand full satisfaction from the estate (Sect 53 ff. InsO)
 - **Simple insolvency creditors:** can only demand satisfaction on a pro rata basis (Sect 38 ff., 174 ff. InsO)

II. 1 Consequences of landlord insolvency on the commercial tenancy

II. 1 Consequences of landlord insolvency for the commercial tenancy

Continuation of the tenancy

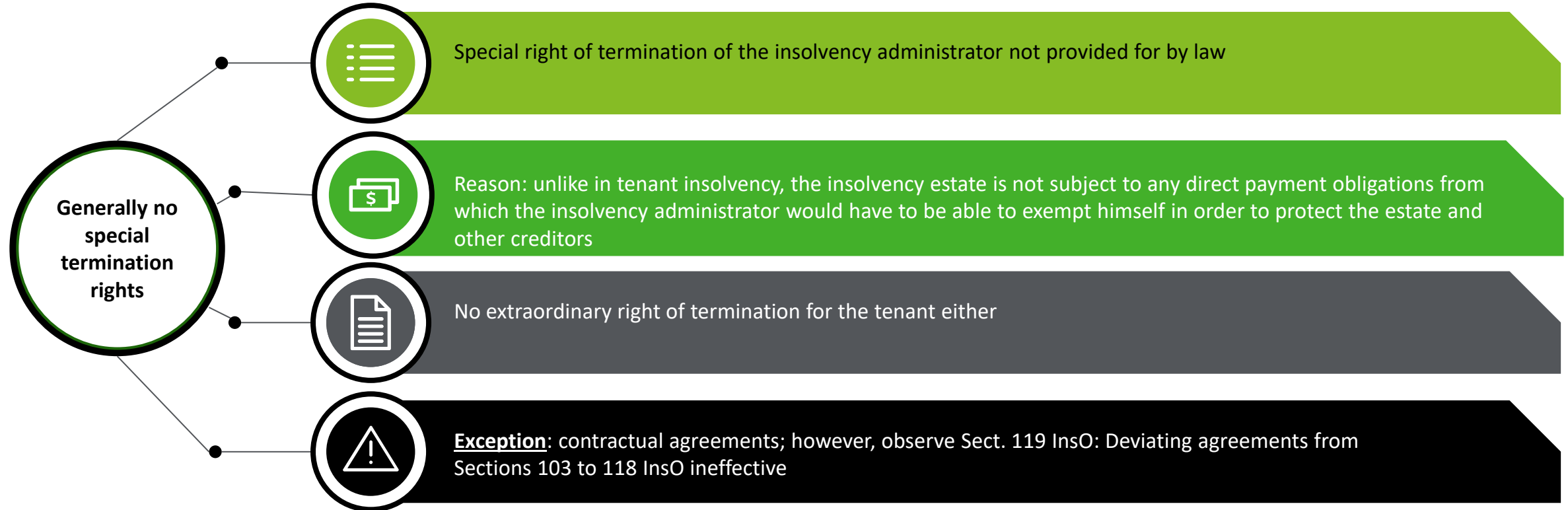
- As a general rule, no influence on the continuation of existing tenancies, Section 108 (1) InsO
  Landlord and tenant obligations continue to apply
- Landlord must continue to fulfill the rental agreement and in particular continue to guarantee the use of the rented property by the tenant
- Obligation of the tenant to continue paying the rent in accordance with the contract; however, to the insolvency estate

Definition of the insolvency estate, Section 35 (1) InsO:

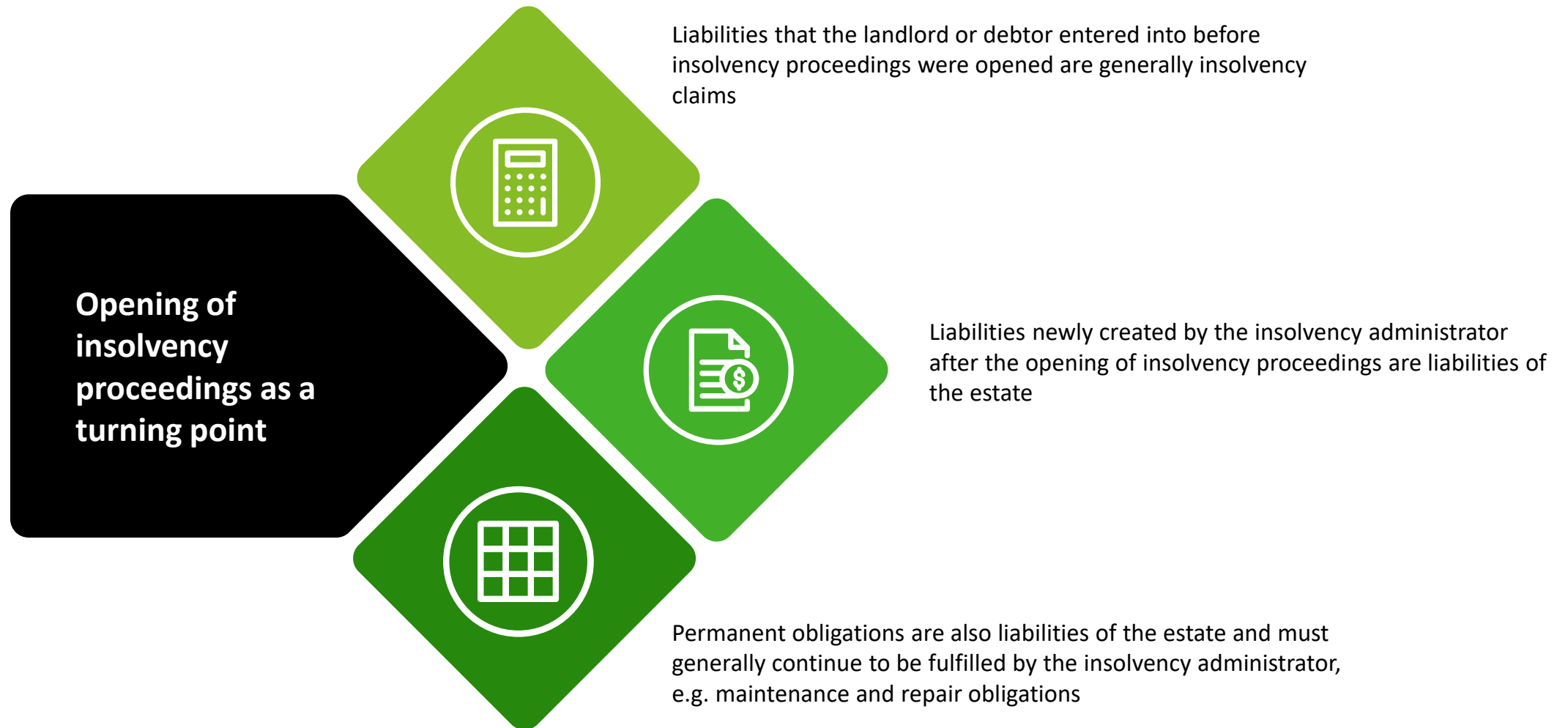
"Insolvency proceedings cover all assets that belong to the debtor at the time the proceedings are opened and that the debtor acquires during the proceedings (insolvency estate)."

- Exception: Rental property not yet handed over → Continued existence possibly only as a settlement relationship

II. 1 Consequences of landlord insolvency for the commercial tenancy



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Consequences for rental security

Cash deposit

- Insolvency-proof separated from assets?
- Otherwise insolvency claim

Bank guarantee

- Generally not affected by insolvency

II. 1 Consequences of landlord insolvency for the commercial tenancy



Consequences for building cost subsidies

Attention with unsecured building cost subsidies!

Coordination with insolvency administrator
advisable



Claims for damages / contractual penalties

Claims prior to the opening of insolvency
proceedings are generally only insolvency claims

Damages due to continued default may be eligible
for compensation as liabilities of the estate

II.1 Consequences of landlord insolvency for the commercial tenancy

Right of termination of the purchaser

- Purchaser has right of termination pursuant to Sect. 111 InsO:

"If the insolvency administrator sells immovable property or premises that the debtor had rented or leased and the purchaser enters into the tenancy or lease in place of the debtor, the purchaser may terminate the tenancy or lease in compliance with the statutory notice period. Notice of termination may only be given for the first date for which it is permissible."

- Secured by right in rem (real security)?

II. 2 Consequences of tenant insolvency for the commercial tenancy

II. 2 Consequences of tenant insolvency for the commercial tenancy

Continuation of the tenancy

Tenancy continues to exist in principle pursuant to Section 108 (1) InsO

Insolvency administrator has right of termination pursuant to Section 109 (1) InsO; notice period generally three months to the end of the month.

If the leased property has not yet been surrendered: right of withdrawal pursuant to Section 109 (2) InsO

In the event of continuation: landlord and tenant obligations continue to apply

II. 2 Consequences of tenant insolvency for the commercial tenancy

Claims of the landlord

- Here, too, a **distinction is made** between insolvency claims and liabilities of the estate:
 - ➔ Claims that arose prior to the opening of insolvency proceedings are **insolvency claims**, Section 38 InsO → quota service
 - ➔ Outstanding claims that arise during the insolvency proceedings are **liabilities of the estate**, Section 53 InsO → priority service

II. 2 Consequences of tenant insolvency for the commercial tenancy

Termination rights



Insolvency administrator

Insolvency administrator's right of termination pursuant to Sect. 109 InsO

Landlord

Landlord has no independent, extraordinary right of termination due to tenant's insolvency

Contract / Law

Landlord's right of termination only in accordance with contractual agreements or statutory provisions

Termination exclusion

Be aware of termination exclusion under Sect. 112 InsO

II. 2 Consequences of tenant insolvency for the commercial tenancy

Rental collateral

- Agreed rental collateral generally remains as rights of the landlord; no obligation to surrender to insolvency estate
- Settlement only to the extent prescribed by law
 - ➔ Offsetting the deposit only against outstanding rental claims arising during insolvency proceedings
 - ➔ Bank guarantee can also be used for claims prior to the opening of insolvency proceedings

II. 2 Consequences of tenant insolvency for the commercial tenancy

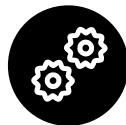
Rights and obligations of the insolvent tenant



Rent payment, further use of the commercial premises



In the event of termination by the insolvency administrator: right to proper settlement: In particular, return of the leased property and release of collateral



In principle, no claim for damages due to termination by insolvency administrator



Opportunity to participate in company restructuring through negotiations with landlord

II. 2 Consequences of tenant insolvency for the commercial tenancy

Landlord's lien

- The statutory landlord's lien (Sect. 578 (1), (2), 562 BGB) grants the landlord a right to separate satisfaction during insolvency proceedings in accordance with Section 50 (1) InsO
- Restriction to rent arrears that have arisen in the last 12 months prior to the opening of proceedings
- Older arrears and compensation claims are no longer secured, but simple insolvency claims
- **Exception:** Pledged savings as rental security
- **Please also note:** Active enforcement required!

III Tenant easement

III. 1 Objective as a hedging instrument



III. 2 Do's and don'ts - avoiding pitfalls

Problems relating to the tenant easement

"a complicated love triangle"

- **Financing of real estate:** In the case of risk assessment by banks, all encumbrances in the land register that take precedence over the land charge to be registered are valued.
- Not all senior charges may be retained in order not to jeopardize the so-called "cover pool eligibility" of the loans.
- **Basic recommendation:** Consideration of the template of the Association of German Pfandbrief Banks (vdp) from 2009
- Older easements that do not comply with the vdp standard often lead to conflicts when the asset is sold or refinanced. The vdp standard should be observed when concluding new agreements.

III. 2 Do's and don'ts - avoiding pitfalls

Basic rules of the tenant easement

- Registration options:

- **Primarily** for financing land charges
- **Subordinated** to financing land charges, but then supplemented by a **so-called "declaration of encumbrance"**

 **Depending on the individual case / individual solution!**

- "Real estate declaration of occupancy": Agreement between owner, tenant and bank!

- **Bank undertakes to** apply for the tenant easement to remain in place in the event of foreclosure if certain conditions are met;
- **The parties to the tenancy agreement undertake** not to amend the tenancy agreement or the content of the tenant easement and to agree compensation for the value of the tenant easement.

III. 2 Do's and don'ts - avoiding pitfalls

Remuneration

- Obligation of the tenant to pay the owner a fee corresponding to the rent otherwise owed when exercising the easement.



Maximum amount agreement (§ 882 BGB)

- Up to EUR 25,000.00 generally unproblematic for banks



Resolving conditions

- e.g. in the event of changes to the content of the easement/the maximum amount by the landlord and tenant without the consent of the mortgagee



Criteria vdp standard (model of the Association of German Pfandbrief Banks), etc.

Basic rules of the tenant easement

III.2 Do's and don'ts - avoiding pitfalls

Problem: Bar to registration due to ineffective clauses in the vdp model

- Fee agreement should become part of the agreement in rem according to the vdp model (thus effective vis-à-vis third parties) → **but:** "in rem" fee agreement ineffective!
- Risk that the land registry refuses to register the easement due to inadmissible content.
- **Solution:** Fee agreement should be moved to the contractual part of the easement agreement.

Contract design

- From the landlord's point of view, it is advisable to include a clause in the contract that enables the landlord to react to changes in market and bank requirements
- e.g. through the tenant's obligation to cooperate in adjustments under certain conditions

III Q&A



**Thank you very
much**
for your attention

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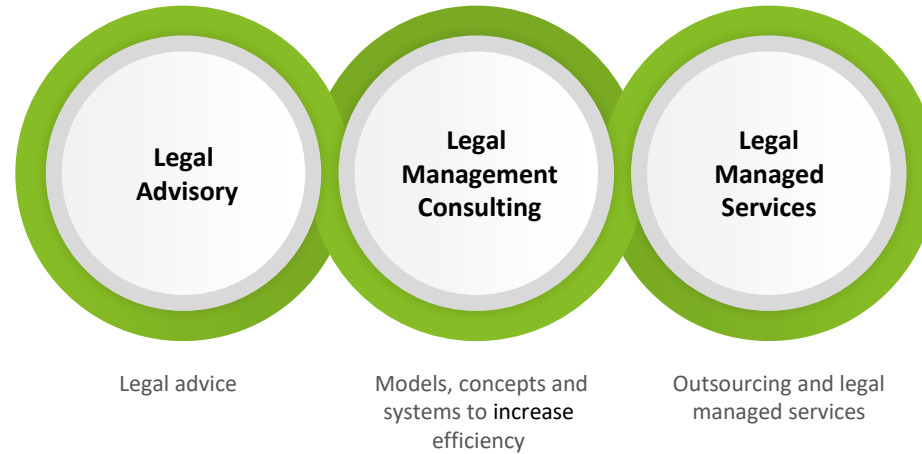
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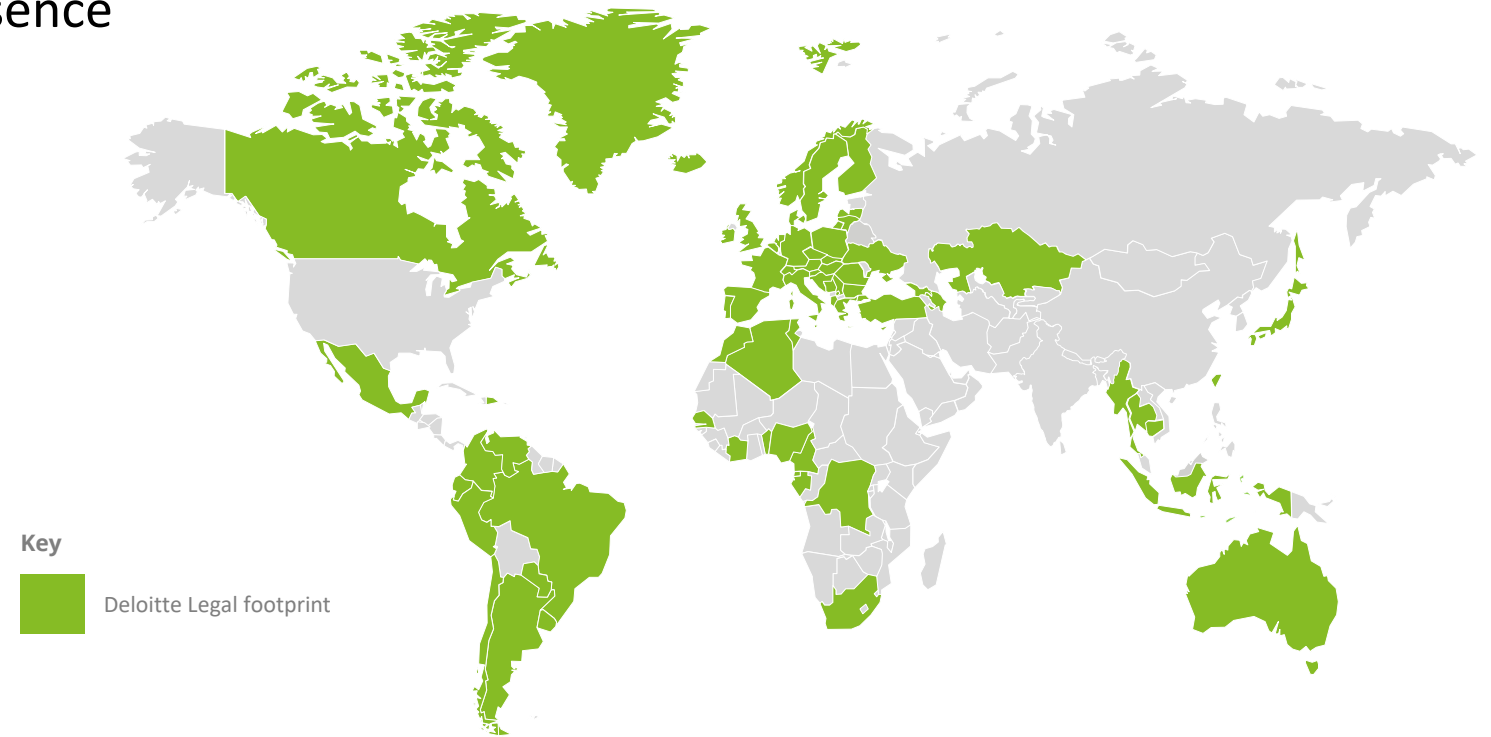


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