

What WeWork's Ch. 11 Filing Means For Landlords

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On Nov. 6, WeWork Inc. and several hundred of its affiliates filed voluntary Chapter 11 cases in the U.S. Bankruptcy Court for the District of New Jersey.

According to a press release issued simultaneously with the filings, WeWork also intends to file recognition proceedings in Canada under Part IV of the Companies' Creditors Arrangement Act. The press release also states that WeWork's locations outside of the U.S. and Canada are not part of the reorganization process.

WeWork has entered into a restructuring support agreement with holders, representing approximately 92% of its secured notes, to reduce WeWork's funded debt and expedite the restructuring process.

WeWork has also said it expects to have sufficient liquidity to execute the reorganization proceedings and continue business in the ordinary course.

WeWork's Chapter 11 filing has the potential to be one of the most consequential cases in the real estate industry in many years, and presents a number of issues for landlords.

Immediate Consequences

Landlords — and other creditors of WeWork — should be aware that one of the immediate consequences of WeWork's Chapter 11 filing is that the automatic stay takes effect.

In a U.S. bankruptcy proceeding, the automatic stay is a statutory injunction that broadly prohibits creditors from commencing or continuing litigation, lien enforcement, or collection actions against the debtor and any property in which it had an interest, as of the commencement of the Chapter 11 case.

Given the enormous number of entities involved in WeWork's Chapter 11 filing, landlords should promptly confirm whether any of their tenants or other contractual counterparties are part of the Chapter 11 filing.

If they are, landlords should be aware that the automatic stay prohibits them from — among other things — attempting to collect past-due rent, commencing or continuing eviction actions, terminating leases, and applying security deposits.



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However, the automatic stay generally will not prevent landlords from making a draw upon a letter of credit, or enforcing a guaranty against a guarantor that is not part of the Chapter 11 filing.

Issues Landlords Should Consider As WeWork Case Proceeds

WeWork's Chapter 11 stands to present an array of issues, but here are a few that landlords should consider going forward.

Unexpired Leases

The debtor, in the exercise of its business judgment, is given the power to assume, possibly assign or reject unexpired commercial real estate leases, regardless of whether the governing leases include provisions that otherwise prohibit assignment or which would allow termination as a result of a Chapter 11 filing.

Assumption

The power to assume a lease is subject to the requirement that the debtor cure monetary defaults and provide adequate assurance of future performance.

Assignment

A debtor can typically assign a lease regardless of anti-assignment provisions in the lease, but still must cure monetary defaults, and the assignee must provide adequate assurance of future performance.

Rejection

If a debtor rejects a lease, the rejection is treated as a breach of the lease and the debtor is required to surrender the premises to the landlord.

As of Nov. 7, WeWork has already requested court approval to reject leases for a number of locations and surrender those premises to the landlords. Additionally, according to an 8-K filing with cleansing materials, WeWork is considering exiting more than 30% of its active, wholly owned portfolio.

Obligations Pending Assumption or Rejection

Usually, a landlord will be obligated to continue performing under the lease until the debtor decides whether to assume or reject the lease, and the debtor must make its decision within 120 days of the bankruptcy filing, subject to a potential 90-day extension.

At the same time, a major statutory benefit for landlords is that a debtor is required to perform its post-bankruptcy obligations under a commercial real estate lease. However, the debtor can seek court approval to extend the deadline to perform those obligations until up to 60 days after it filed for bankruptcy.

Stub Rent

The term "stub rent" refers to the amount of rent that is due from the date of a debtor's Chapter 11

filing until the next rent payment date.

Landlords should be aware that a debtor may not be required to timely pay prorated rent for the stub period.

Letters of Credit

Landlords can typically draw upon letters of credit issued by nondebtor entities upon a default of the debtor-tenant's obligations, notwithstanding the bankruptcy filing, and without seeking relief from the automatic stay.

Priority of Landlord's Claims

Typically, unpaid rent and other prebankruptcy obligations under a commercial property lease are unsecured claims.

Unpaid obligations arising after the bankruptcy case is filed, but before a lease is rejected, will often — but not always — be afforded administrative expense priority, and thus entitled to full payment.

Upon rejection, a landlord's claim — including for future rent payments — typically will be treated as an unsecured claim and subject to a cap as discussed below.

Caps on Lease Termination Claims

In a Chapter 11 case, a landlord's claim resulting from termination of the lease is statutorily capped at the greater of one year, or 15% not to exceed three years, of the remaining lease term.

Courts have taken differing approaches on the computation of the cap, what types of damages are capped, and the effect of a draw on a letter of credit on the amount of the claim.

However, the cap does not apply to, but instead the landlord retains an additional claim for, any unpaid rent due under the lease, without acceleration, on the earlier of the date on which the case was filed, and the date on which the landlord repossessed, or when the lessee surrendered the leased property.

Next Steps

Now that WeWork has filed Chapter 11, landlords should — if they have not already — assemble and review their lease documents, and understand their contractual rights and remedies.

Further, given the pace at which a Chapter 11 case can unfold, and the complexity of WeWork's case in particular, landlords should familiarize themselves with their rights in a Chapter 11 case and WeWork's proposed treatment of their leases, and be prepared to assert their rights promptly.

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