Managing Commercial Real Estate Leases: California

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A Q&A guide to state laws and customs on managing commercial real estate leases in California. Answers to questions can be compared across a number of jurisdictions (see Managing Commercial Real Estate Leases: State Q&A Tool).

Letters of Intent

1. Is it customary in your jurisdiction for letters of intent to bind the parties?

In California, letters of intent for commercial leases are typically drafted so that they do not bind the parties.

California contract law governs whether letters of intent relating to commercial leases bind the parties. In determining whether a letter of intent constitutes a binding contract, or merely an agreement to make an agreement, courts consider the specific facts of a case, including:

- The content of the letter of intent, such as whether it contains the essential terms of a lease.
- The parties' intent, as demonstrated by:
  - the construction of the letter of intent in light of the circumstances surrounding the negotiations;
  - the plain language of the instrument; and
  - the conduct of the parties.

(*Munoz v. Patel*, 81 Cal. App. 5th 761, 772 (2022); *Cal. Food Serv. Corp. v. Great Am. Ins. Co.*, 130 Cal. App. 3d 892, 897 (1982); *Beck v. Am. Health Grp. Int'l, Inc.*, 211 Cal. App. 3d 1555, 1562 (1989) (*superseded on other grounds*).)

In California, the best practice to avoid characterization of the letter of intent as a binding lease is to include explicit non-binding language disclaiming any intent to create a present lease. If a letter of intent states it is non-binding, a court is unlikely to decide to the contrary.

In addition, all California contracts, including leases, are subject to an implied duty of good faith and fair dealing (*Copeland v. Baskin Robbins U.S.A.*, 96 Cal. App. 4th 1251, 1260 (2002)). To prevent a potential claim for breach of the implied duty, it is recommended that a California letter of intent:

- Include a disavowal of any obligation of either party to negotiate.
- Grant either party the right to withdraw from negotiations at any time and for any reason (or no reason).
- Acknowledge that neither party may rely on the letter of intent or on the success or failure of any negotiations.

Term and Renewals

2. If the lease term expires on a Sunday, can the tenant surrender the premises on the next business day or is there a risk that the landlord will claim a default?

Absent a lease provision to the contrary, if a California commercial lease term expires on a Sunday (or any holiday or non-business day), occupation of the premises by the tenant on the next calendar day would be a holdover (*Gans v. Smull*, 111 Cal. App. 4th 985, 989-90 (2003)).

For more information on holding over in California, see:

Standard Document, Office Lease Agreement (Multi-Tenant Gross Lease) (Pro-Landlord Short Form) (CA): 18.2 Holdover.

Practice Note, Landlord's Rights and Remedies (Commercial Lease) (CA): Eviction for Failure to Vacate After Expiration of the Term.

3. If a commercial tenant extends its lease term, are the tenant's options (such as a termination or renewal option) automatically included in the extension term when the lease is silent?

In California, the specific terms of the lease generally govern whether a tenant's options are included in an extension term.

Absent a lease provision to the contrary, an express extension of the term of a lease is under the same terms and conditions as the original lease. The California Court of Appeal has held that a tenant's right to cancel the lease that was contained in the original lease continued during the extension period (*Smith v. Arthur D. Little, Inc.*, 276 Cal. App. 2d 391 (1969)).

Guarantors

4. If a guaranty does not expressly require a guarantor's consent to a lease amendment, can a guarantor still be held liable for the lease as amended?

In California, a commercial lease guaranty is interpreted based on its specific content.

Absent guaranty language to the contrary, the general California rule is that unless indemnified by the principal (in the case of a lease, the tenant), a guarantor can be exonerated from liability if, without the consent of the guarantor, the guaranteed obligations are modified (Cal. Civ. Code § 2819). Landlords typically insist that guarantors waive their rights to exoneration (Cal. Civ. Code § 2856).

For additional guarantor waivers typically included in California guaranties, see Standard Document, Guaranty of Nonrecourse Carveout Obligations (Commercial Real Estate Loan) (Pro-Lender) (CA).

5. If the lease is assigned, is the guarantor automatically released from the obligations under the lease or is an express release required?

In California, assignment of a commercial lease by the tenant does not automatically release the tenant or the guarantor of the lease from the obligations under the lease. An express release is required. (*Samuels v. Ottinger*, 169 Cal. 209, 211–12 (1915).)

The Premises

6. In your jurisdiction, is there a customary procedure for measuring a tenant's premises and the building?

In California, conventions regarding measurement of premises are left to local practice. The Building Owners and Managers Association (BOMA) standards of measurement are used commonly, but not universally, particularly regarding retail leases.

For more information on BOMA and measuring the premises in California, see Standard Document, Office Lease Agreement (Multi-Tenant Base Year Modified Gross Lease) (Pro-Landlord Short Form) (CA): Premises: Definition.

7. Can a landlord access a commercial tenant's premises without the tenant's prior consent? Can the tenant refuse to give the landlord access?

In California, with certain limited exceptions, the landlord in a commercial lease does not have a common law right of entry onto the premises. Rather, the specific provisions of the lease govern entry. Typically, the landlord retains the right to enter to:

- Perform repairs.
- Meet obligations under the lease.
- Show prospective tenants, purchasers, and lenders the property.
- Inspect the premises to determine the tenant's compliance.

Notice is usually required and specified, except in emergency situations.

Increasingly common in commercial leases are provisions barring the landlord from entering certain protected portions of the premises due to the sensitive or confidential nature of the tenant's business conducted on the premises.

For more information on Landlord access in California, see Standard Document, Office Lease Agreement (Multi-Tenant Base Year Modified Gross Lease) (Pro-Landlord Short Form) (CA): Section 25.3 and Drafting Note: Landlord Access.

8. If the lease is silent, what rights does a commercial tenant have when the premises are damaged by fire or flooding? In particular, can the tenant terminate the lease?

California Civil Code provisions permit a tenant to terminate its lease if all or a material portion of a commercial premises is destroyed (Cal. Civ. Code §§ 1932(2) and 1933(4)). However, these provisions are customarily expressly waived in California commercial leases.

For more information on a commercial tenant's waiver of its statutory right to terminate, see Practice Note, Common Tenant Waivers (Commercial Lease) (CA): Casualty.

Landlord Lien Rights

9. Does a landlord have any statutory or common law lien right on a commercial tenant's personal property, inventory, and equipment?

In California, absent an express grant of a UCC lien right or attachment obtained after the filing of a lawsuit, a landlord has no lien rights in any of its tenant's' personal property.

10. When a commercial lease is not clear regarding the ownership of leasehold improvements, is the tenant or landlord deemed the owner of the improvements?

In California, a landlord is deemed to be the owner of improvements a tenant makes to the premises, except if the improvements constitute trade fixtures (Cal. Civ. Code § 1013; *Goldie v. Bauchet Props.*, 15 Cal. 3d 307, 313 (1975)). Under Section 1019 of the California Civil Code, trade fixtures belong to the tenant and can be removed from the premises. Trade fixtures are personal property used in tenant's trade.

A landlord has no duty to pay a tenant for leasehold improvements absent a contrary lease provision.

Compliance with Laws

11. In your jurisdiction, do most commercial leases require the tenants to comply with all laws governing the premises?

In California commercial leases, the parties' obligations to comply with applicable laws are usually negotiated by the parties. It is common for:

- The tenant to be responsible for compliance with laws for the interior of the premises, excluding structural matters.
- The landlord to be responsible for compliance with laws for exterior improvements, structural matters, and interior improvements that are constructed by the landlord.

The longer the term of the lease, the more likely that the tenant assumes greater responsibility for the costs of legal compliance.

Zoning and Building Laws

Both the landlord and the tenant are responsible for zoning compliance. The tenant is typically responsible for building code compliance:

- Relating to the tenant's improvements.
- If the tenant's alterations are required as a result of a change in the use of the premises by the tenant.

If the lease is silent on the issue, the landlord is generally responsible for all other building code compliance.

Environmental Laws

Compliance with environmental laws is generally the landlord's responsibility, unless the lease specifies otherwise or the tenant causes or permits the contamination. The tenant may also be found responsible for compliance with environmental laws based on factors, including the length of the lease and whether the lease is a ground lease, demonstrating that the tenant is, for all practical purposes, the owner of the property in question or should otherwise be equitably responsible for the work (*Brown v. Green*, 8 Cal. 4th 812 (1994)).

CASp Inspection

Every commercial lease agreement must state whether the subject premises have undergone inspection by a Certified Access Specialist (CASp). If a CASp has:

- Inspected the premises:
  - the lease must state whether the inspection determined that the premises met all applicable construction-related accessibility standards; and
  - the landlord must provide the tenant with a copy of any CASp report at least 48 hours before lease execution. If the report is not provided, the prospective tenant has the right to rescind the lease based upon the information contained in the report up to 72 hours after executing the agreement. (Cal. Civ. Code § 1938(c).)
- Not inspected the premises, the lease must include the language specified in Section 1938(e) of the California Civil Code.

(Cal. Civ. Code § 1938.)

Unless the parties to the lease agree otherwise, any repairs or modifications needed to correct violations of construction-related accessibility standards that are noted in a CASp report are the responsibility of the commercial property owner or landlord (Cal. Civ. Code § 1938(c)).

For more information and forms on the CASp regulation, see Standard Document, Industrial/Warehouse Lease (Pro-Landlord with Pro-Tenant Optional Provisions) (CA): Section 26.13 and Drafting Note, Certified Access Specialist Disclosure.

Subordination, Non-Disturbance and Attornment Agreements (SNDA)

12. Is it customary in your jurisdiction for SNDAs to be recorded by the parties to a commercial lease?

Subordination, non-disturbance and attornment agreements (SNDAs) are commonly recorded by the parties, with the following exceptions:

- Commercial leases with tenants with little or no bargaining power (for example, small shop leases).
- Office leases, unless the tenant is leasing a significant amount of space or performing a significant amount of work for which they will incur substantial costs.

Assignment and Subleasing

13. In your jurisdiction, what rights does a commercial tenant customarily have if the landlord fails to respond timely or unreasonably withholds its consent to a tenant's request to assign its lease or sublet its premises?

In California, the tenant's rights depend on the lease terms. If the lease is silent, a tenant has an unrestricted right to transfer its interest in the premises. Or a landlord can restrict a commercial tenant's ability to transfer its leasehold interest, including absolutely prohibiting transfer of the tenant's interest. (Cal. Civ. Code §§ 1995.210(a) and 1995.230.)

The landlord can withhold consent to a transfer subject to any express standard (Cal. Civ. Code § 1995.250). If the lease requires a landlord's consent for a transfer but provides no standard for giving or withholding consent, the restriction must be construed to include an implied standard that the landlord's consent may not be unreasonably withheld. Whether the landlord unreasonably withheld consent is a question of fact that the tenant has the burden to prove. (Cal. Civ. Code § 1995.260.) Failure to act reasonably or delayed response gives the tenant the right to seek damages or injunctive relief or terminate the lease (Cal. Civ. Code § 1995.310).

Defaults and Preservation of Rights

14. If a commercial tenant is evicted from its premises, can the landlord still collect the rent until the lease term expires?

In California, when a landlord terminates a commercial tenant's right to possession of the premises, a landlord may not continue to collect rent. However, if provided under the lease, a landlord may recover a lump sum award for future rent owing through the balance of the lease term, less any amount that the tenant proves may be reasonably mitigated, discounted to present value. (Cal. Civ. Code § 1951.2.)

For more information on eviction in California and the landlord's right to sue for damages, see Practice Note, Landlord's Rights and Remedies (Commercial Lease) (CA).

For information on protections afforded certain small businesses and nonprofits under the Commercial Tenant Protection Act (also referred to as SB1103), see Practice Note, Qualified Commercial Tenant Requirements for Landlords (Commercial Lease) (CA).