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Commercial Eviction and Landlord's Liens

Article

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I. Introduction

The relationship between a commercial landlord and tenant is governed primarily by the terms of the lease. The lease defines each party's rights and obligations with regard to the subject property and the other party. More importantly, the lease affords each party a degree of protection should the relationship fail. While neither party enters into a lease with the expectation that the relationship will fail, and the lease will be terminated, one cannot overemphasize the importance of planning for this contingency at the outset of the relationship. From the landlord's perspective, these preparations should focus on: (1) understanding the process by which the lease will be interpreted and enforced should the tenant breach the lease; and (2) drafting the lease to maximize protection of the landlord's interest in both the property and the funds due under the lease.

With these goals in mind, this paper provides commercial landlords, and their counsel, a comprehensive overview of the commercial eviction process under N.C. law. More importantly, it provides commercial landlords with the necessary tools and resources to properly, and legally, plan for and address any disputes that may arise when a tenant has failed to fulfill its obligations under the lease.

II. Commercial Eviction

In a majority of cases, neither the landlord nor the tenant has reason or cause to consult the terms of the lease after it is signed and the tenant takes possession of the leased premises. However, if either party suspects that the other is failing to fulfill its obligations under the lease, the lease should be consulted to determine if there is, in fact, a breach. If there is a breach, the lease will provide the framework through which the non-breaching may protect its interest. In either case, the first step is to identify the terms of the lease.

Generally, the terms of a lease are contained in a single document signed by both the landlord and the tenant. In these cases, the rights and obligations of each party are readily identifiable. However, leases can also be made up of several writings or instruments and still be enforceable under N.C. law. See *Satterfield v. Pappas,* 67 N.C. App. 28, 35, 312 S.E.2d 511, 516 (1984) ("[A]n enforceable lease or conveyance of land need not be set out in a single instrument, but may arise from a series of separate but related letters or other documents signed by the person to be charged or his authorized agent") (internal citation omitted).

Where a written lease is modified or amended, the parties must consult each and every relevant document when determining their rights and obligations under the lease.[1] This is especially important where one party is claiming the other party is in breach, because a lease, like any other contract, will be interpreted as a whole. See *Wal-Mart Stores, Inc. v. Ingles Markets, Inc.*, 158 N.C. App. 414, 419, 581 S.E.2d 111, 115 (2003). N.C. law does not allow a party to accept benefits arising from certain terms of a contract, while denying the effect of other terms of the same contract. See, *e.g.*, *Advertising, Inc. v. Harper*, 7 N.C. App. 501, 505, 172 S.E.2d 793, 795 (1970); *Cary Crossroads Assocs., L.P. v. Atlanta Bread Co. Intern., Inc.*, 2003 COA02-1178 (unpublished). Therefore, a party should consult the lease to determine what procedures it must follow in identifying any default and enforcing its rights under the lease.

* This article was co-authored by Alesia Balshakova who is not affiliated with Williams Mullen.
1. While the vast majority of commercial leases are written, North Carolina law does recognize oral leases of a duration not to exceed three years. If the term of a lease exceeds three years, it must be in writing under the statute of frauds or the lease is unenforceable. See *Howell v. CSB, LLC*, 164 N.C. App. 715, 718, 596 S.E.2d 899, 902 (2004); N.C. Gen. Stat. § 22-2 (2008).

Questions?

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A. Identifying a Default

Most leases contain specific provisions providing that the landlord may declare the lease in default on the basis of the tenant's failure to abide by any term of the lease. While the most common tenant's default is nonpayment of rent or other sums due under the lease, such as common area maintenance fees, there are a variety of bases on which to declare the tenant in default. Other common tenant defaults include: failure to pay timely rent; failure to operate during specified hours; failure to comply with applicable health codes; failure to properly dispose of waste; failure to comply with the signage requirements; failure to maintain insurance on the leased premises; illegal activity on the leased premises; a change in the permitted use; abandonment; or a tenant's bankruptcy.

B. Cureable / Noncureable Defaults

Once the landlord has identified the default, it must consult the lease to determine how it should proceed. Many leases distinguish between tenant's defaults that are cureable and tenant's defaults that are noncureable.

i. Noncureable Defaults

Where the lease provides that the default is noncureable, the landlord is not obligated to provide notice of the default or to give tenant an opportunity to cure and the tenant is in breach of the lease upon default. For example, the lease may contain the following language:

> Failure or refusal by Tenant to timely pay Minimum Rent or any other sums due following ten (10) days written notice; provided that, in no event shall Landlord be required to give such notice more than two (2) times during any calendar year, and from and after Tenant's third (3rd) such failure or refusal during any calendar year, Landlord shall be entitled to exercise any or all of the remedies set forth herein without prior notice to Tenant.

This provision makes the default cureable the first 2 times, but the third time the default becomes noncureable. Other noncureable defaults may include voluntary or involuntary bankruptcy, abandonment of the leased premises, or the conducting of illegal activities on the premises. In these circumstances, the landlord may simply declare the tenant in breach and enforce its rights under the lease.

However, some leases require that before terminating the lease-or the tenant's right to possession of the leased premises-the landlord should first verify that all the failures occurred within the requisite time period. Where the lease provides that a certain number of failures must occur within "a year," the landlord must determine whether the failures must occur within a 12-month period or within the calendar year. If the lease does not define what constitutes a "year," the courts are likely to interpret it to mean a calendar year. See *Harris v. Latta*, 298 N.C. 555, 558, 259 S.E.2d 239, 241 (1979) ("In construing contracts ordinary words are given their ordinary meaning unless it is apparent that the words were used in a special sense.").

ii. Cureable Defaults

If, however, the lease provides that the tenant must be given notice and an opportunity to cure the default, the tenant will only be in breach of the lease if it fails to cure the default within the time period established by the lease. Where the lease provides for a cure period, the landlord must wait the requisite number of days before taking any further action. Typically, cure periods are five to ten days; however, if the default is nonmonetary, many leases provide the tenant with a longer period in which to cure the default. For example, the lease may provide that:

> Tenant shall be in default hereunder if (a) Tenant fails to pay when due Minimum Annual Rent or any other sums due under this lease and such default shall continue for more than five (5) days after written notice from Landlord to Tenant; or (b) Tenant fails to observe and perform any of the other terms, covenants and/or conditions of this lease and such default shall continue for more than thirty (30) days after written notice from Landlord to Tenant.

Should the landlord fail to provide the requisite notice or the proper time to cure, it may not be able to evict the tenant, even though the tenant is in breach of the lease. As such, the landlord should consult and follow the enforcement provisions set forth in the lease (and any amendments thereto). In particular, the landlord must ensure that: (1) the proper parties are provided notice; (2) notice is sent to the correct address(es); (3) the proper method of serving notice is utilized; and (4) the tenant is afforded the full cure period as provided in the lease.

Proper Parties: The landlord will always be required to provide the tenant, as designated in the lease, with the requisite default notice. However, the lease may also require that notice be sent to other individuals or entities, such as a franchisor or a guarantor. In some instances, the lease will not require that notice be provided to guarantors of the lease, but a prudent landlord will provide such notice to maximize protection of its financial interests under the lease.

Correct Address: Generally, the lease will specify the address or addresses to which default notices must be sent, but the landlord should not rely solely on the lease. While most leases provide that the tenant must send written notice of any address changes to the landlord, the prudent landlord will look to the terms of the lease, all correspondence, and any other documents in its file in determining where to send default notices. To avoid any possible defense of failure to properly notice the tenant of a default, the landlord should send a copy of the default letter to all addresses on file, even if the tenant failed to formally notify the landlord of a change in address.

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Method of Service: Many leases will require that written notice be sent by a particular method, such as certified mail, return receipt requested, or overnight delivery. For example, the lease may provide that:

> Whenever notice shall or may be given to either of the parties by the other, each such notice shall be by registered or certified mail with return receipt requested, at the respective addresses of the parties as contained herein or to such other address as either party may from time to time designate in writing to the other. Any notice under this lease shall be deemed to have been given at the time it is placed in the mails with sufficient postage prepaid.

Overnight delivery is advantageous not only because of the speed at which the letter is delivered but because frequently the defaulting tenants refuse to pick up certified letters from the post office.

Cure Period: If the lease allows a cure period, the days may be counted from the date the letter is sent or from the date the letter is actually received, depending on the terms of the lease. Unless otherwise specified, the "days" refer to calendar days, not business days. *Southpark Mall Ltd. P'ship v. CLT Food Management, Inc.*, 142 N.C. App. 675, 679, 544 S.E.2d 14, 17 (2001). The tenant in *Southpark* argued that the lease provision allowing a five day(s) cure period referred to five business days, not five calendar days. However, the North Carolina Court of Appeals rejected this view and held that "absent any evidence that the parties to a lease intended the word 'days' to mean 'business days' the word 'day' would be given its ordinary meaning." *Id.*

The landlord must also be careful to count the days correctly. In *Harris*, 298 N.C. at 558, 259 S.E.2d at 241, the North Carolina Supreme Court held that in computing time for performance of an act or event which must take place a certain number of days before a known future day, one of the terminal days is included in the count and the other is excluded, unless there is something to show an intention to count only clear or entire days. For example, assume the lease requires that the tenant has five days to cure after written notice of the default and the notice provision states that notice is effective when the letter is mailed. If the letter is mailed on Monday, the tenant will have until Saturday to cure the default. Landlords would be better served if there is a provision in the lease that allows the cure period to begin running on the date the letter is sent versus when it is received.

C. Terminate Possession or Terminate the Lease

If the tenant defaults and fails to cure the default after proper notice from the landlord (if applicable), most leases allow the landlord to either terminate the tenant's right to possession of the leased premises or to terminate the lease. For example, the lease may contain the following language:

Whenever any event of default shall occur, Landlord may, at its option, in addition to all other rights and remedies given hereunder or by law or equity, do any one or more of the following: (a) terminate this lease or tenant's right to possession of the leased premises.

It is important to read the lease carefully to determine what remedies are allowed if the landlord elects to terminate the tenant's right to possession versus if the landlord elects to actually terminate the lease. The lease may provide for different remedies depending on which election the landlord makes. This is especially important if the landlord plans to pursue the tenant for damages due to lost rents going forward. The lease may provide:

> If Tenant defaults, then without further notice or demand, Landlord also may:
> (1) terminate this Lease without any right by Tenant to reinstate its rights by payment of Annual Minimum Rent or other amounts due or other performance of the terms and conditions hereof and upon such termination Tenant shall immediately surrender possession of the Premises to Landlord, and Landlord shall immediately become entitled to receive from Tenant, as liquidated, agreed final damages, an amount equal to the difference between the aggregate of all rentals reserved under this Lease for the balance of the Term, determined as of the date of such termination or (2) without terminating this Lease, re-enter and repossess the Premises, or any part thereof and lease to any other person upon such terms as Landlord shall deem reasonable, for a term within or beyond the Term; provided however, that any such reletting prior to the termination shall be for the account of Tenant and Tenant shall remain liable for Annual Minimum Rent, Percentage Rent, Tenant's Share of CAM, Tenant's Share of Taxes, Tenant's share of Landlord's Insurance Cost and other sums which would be payable hereunder by Tenant.

The landlord's decision to terminate the lease or not terminate the lease may ultimately affect what the landlord is entitled to recover from the tenant.

Some leases do not distinguish between the landlord's remedies if it terminates the lease or if it terminates possession only. Generally, if the landlord decides to terminate possession (and does not terminate the lease), the tenant remains liable for rent each month. If, however, the landlord terminates possession <u>and</u> terminates the lease, the landlord only has a claim against the tenant for damages which will be measured by the lost rents going forward. Technically, once the landlord terminates a lease, it cannot recover future rent because tenant's property rights have been terminated. Property rights include the right to receive unpaid rents and the reversionary right in the leasehold. *Strader v. Sunstates Corp.*, 129 N.C. App. 562, 570, 500 S.E.2d 752, 757 (1998).

If a lease is terminated, any contractual rights remain intact and the landlord can recover damages for breach of contract. *Id.* (citing

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Holly Farms Foods v. Kuykendall, 114 N.C. App. 412, 415, 442 S.E.2d 94, 96 (1994)). "Contract rights include the right to sue for breach of express and implied covenants and the right to sue for consequential damages stemming from a breach of a lease. *Strader*, 129 N.C. App. at 571, 500 S.E.2d at 757. However, the landlord can only recover damages for breach of contract once the lease has been terminated. *Kuykendall*, 114 N.C. App. at 415, 442 S.E.2d at 96. Note: If the landlord obtains a summary ejectment order, the lease is considered terminated regardless of the landlord's intent.

An additional issue for the landlord to consider when deciding whether to terminate the lease versus terminating the tenant's right to possession is bankruptcy. If the landlord does not terminate the lease upon default, and the tenant files for bankruptcy protection, the bankruptcy trustee will have 120 days after the entry of an order for relief or the confirmation of a bankruptcy plan to assume or reject the lease. If the trustee fails to act within the time period, the lease will be deemed rejected. See 11 U.S.C. § 365(d)(4)(A) and (B) (2008). Until that time, the landlord will not be able to reenter the premises. While the landlord can petition the bankruptcy trustee to assume or reject the lease in less than 120 days by filing a motion to compel the trustee to assume or reject the lease, this will take time. Consequently, if the tenant files for bankruptcy and the lease has not been terminated prior to the filing, the premises can remain dark for months. The chance of recouping all of the lost rents and other associated costs is slim. However, if the landlord terminates the lease upon default, the landlord can remove the tenant from the leased premises prior to any bankruptcy filing. If the tenant files for bankruptcy after the lease has been terminated but before the tenant has been removed from the premises, the landlord should be able to remove the tenant fairly quickly. The landlord must be careful with any items remaining on the premises, however, as they are considered part of the bankruptcy estate.

D. Holdover Tenant

Most leases are for a term certain, such as five years. However, many leases contain provisions through which the tenant can extend the term of the lease for some additional period of time (a renewal provision), which may contain the following language:

> Provided Tenant is not then in default of any material terms or provisions hereof, after the lapse of all applicable grace periods, Tenant shall have the option to extend the Term for the number of Extension Periods shown in Section 1.01(D), upon all the terms and conditions contained herein. Each such option is exercisable by Tenant giving notice in writing to Landlord at least four (4) months prior to the expiration of the Initial Lease Term in writing.

If the term of the lease expires and the tenant has not renewed the lease but remains on the premises, the tenant is called a holdover tenant. The landlord can elect to treat a holdover tenant as a trespasser and file a summary ejectment action against the tenant: no other default is required. The landlord can also elect to continue to allow the tenant to remain in the leased premises. The landlord should, however, proceed with caution as a court may determine the lease was renewed.

In cases in which notice to extend term of a lease is required, and none is given, the landlord also has the option to waive notice and treat the tenant as occupying the premises by virtue of an extension of the terms of the lease. *Royer v. Honrine*, 68 N.C. App. 664, 666, 316 S.E.2d 93, 95 (1984); *Realty Co. v. Demetrelis*, 213 N.C. 52, 55, 194 S.E. 897, 898 (1938). When a lease specifies the manner and method by which the tenant may extend the term, compliance with such provisions are conditions precedent to the extension of the term. *Coulter v. Fin. Co.*, 266 N.C. 214, 219, 146 S.E.2d 97, 101 (1966).[2] In *Coulter*, the lease gave the tenant the option of renewing the lease for two years at a higher rent and required that the tenant give written notice to the landlord if it decided to renew the lease. The lease also provided that if the tenant heldover, it would be treated as a month to month tenant. The tenant did not give notice to the landlord but after the initial lease term had expired it tendered the higher rent to the landlord and the landlord accepted it. The North Carolina Supreme Court held that although tenant failed to give notice pursuant to the terms of the lease, the lease was renewed for an additional two years. If the holdover tenant in Coulter had continued to pay the rent specified in the original lease instead of the higher rent specified in the renewal and the landlord had accepted it, the court most likely would have reached a different result.

In *Royer*, 68 N.C. App. at 665, 316 S.E.2d at 94, the lease required the tenant, in order to renew the lease, to give written notice to the landlord and pay a higher rent for the new term. The tenant did not provide written notice to the landlord but remained on the premises for 15 months after the expiration of the original lease term. The tenant tendered the rent specified in the original lease (not the higher amount specified for the renewal) and the landlord accepted it. The landlord then sought to evict the tenant and the tenant argued that the landlord's acceptance of rent waived the written notice requirement. The North Carolina Court of Appeals disagreed stating:

> If the lease provides for an additional term at an increased rent, and after the expiration of the lease the tenant holds over and pays the increased rental, this is affirmative evidence on his part that he has exercised the option to take the lease for an additional term; but where, under such a lease, the tenant holds over after the expiration of the original term and does not pay the increased rental as provided by the lease, but continues to pay the original rental, which is accepted by the lessor, this negates the idea of the acceptance of the privilege of an additional term.

2. In MER Properties-Salisbury v. Golden Palace, 95 N.C. App. 402, 382 S.E.2d 869 (1989) however, the North Carolina Court of Appeals held that the tenant's renewal was effective despite the fact the renewal was required to be sent registered mail and the tenant sent it only by regular mail. There was evidence that the requirement that notice be sent by registered mail was located in the miscellaneous section of the lease, not in the renewal provision. The landlord also actually required the notice. Accordingly, the North Carolina Court of Appeals determined that to hold that notice was not effective solely because the tenant failed to send it by registered mail would be overly harsh.

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Royer, 68 N.C. App. at 666-667, 316 S.E.2d at 95. If the tenant fails to pay the increased rental specified in the renewal provision of the lease, the tenancy is converted to a month to month tenancy and it is terminable by the landlord with seven days notice. *Rushing Constr. Co. v. MCM Ventures, II, Inc.*, 100 N.C. App. 259, 262, 395 S.E.2d 130, 132 (1984).

When the rent for the renewal period is the same as for the initial term and the tenant holds over and continues to pay the rent and the landlord accepts it, it is presumed that the tenant intended to exercise its option. *Id*; see also *First-Citizens Bank & Trust Co., v. Frazelle*, 226 N.C. 724, 726, 40 S.E.2d 367, 369 (1946). A landlord faced with this situation needs to proceed with caution. Acceptance of the rent from the tenant could be construed as a waiver of the tenant's compliance with the renewal provision and the landlord may lose its ability to evict the tenant because of its holdover status.

From the tenant's prospective, it is crucial to keep track of the date required to renew. The landlord may be able to lease the property at a rate that is higher than what is specified in the renewal provision. Therefore, the landlord would have little reason to allow tenant who fails to timely renew to remain on the premises.

E. Self Help Eviction

Self-help remedies are allowed under N.C. law for commercial evictions,[3] so long as carried out without a breach of the peace. Practically any objection or refusal by a tenant to repossession by the landlord will be sufficient to color subsequent actions by the landlord to repossess as "in breach of the peace." Many commercial leases contain a provision which allows the landlord, upon default, to retake possession of the premises through self-help.

> Landlord, with or without terminating the Lease, may immediately or anytime thereafter re-enter the Leased Premises and remove Tenant, including all persons and personal property, from the Leased Premises. In the event of any such re-entry, the Tenant hereby waives all claims for damages which may be caused by the re-entry of the Landlord and will save the Landlord harmless from any loss, cost or damages suffered by the Tenant by reason of such re-entry.

The advantage to self-help eviction is that it is much quicker than going through the summary ejectment process. The disadvantage is that the landlord puts itself at risk of potential claims by the tenant or even by third-parties.

If the tenant agrees to the repossession, the landlord will be within its rights to reenter and take possession of the leased premises. The landlord should be careful to make clear in writing that it is retaking possession of the leased premises because of the tenant's default and that the tenant remains responsible for all future rent accruing under the terms of the lease. "When a tenant abandons premises, and returns the keys to the landlord, the latter may accept the keys as a surrender of possession, thereby determining the tenant's estate, and re-let the premises on his own account, or he may accept the keys and resume possession conditionally by notifying the tenant or other person returning the keys that he will accept the keys but not the leased premises, and re-let them on the tenant's account, in which case the tenant may be held for any loss in rent caused by his abandonment and the subsequent re-letting." *Monger v. Lutterloh*, 195 NC 274, 277, 142 S.E.12, 4 (1928) (internal citations omitted). If, on the other hand, the tenant agrees to the landlord retaking possession of the leased premises, the landlord needs to make it clear that the landlord is not accepting surrender of the leased premises and that the tenant is liable for future rents (or damages caused by the landlord's loss of future rents).

Although N.C. law does not specifically require that the landlord notifies the tenant that the landlord does not accept the tenant's surrender, it would behoove a landlord in such a situation to send the tenant written notice in accordance with the notice provisions of the lease, stating unequivocally the landlord's position regarding the tenant's departure prior to the term's expiration. If the landlord desires to hold the tenant liable for any rent in the future, such a notice should clearly state that the landlord does not accept surrender by the tenant and will further hold the tenant responsible for all future rent accruing under the terms of the lease.

Absent the tenant's agreement that the landlord may retake possession of the leased premises, the landlord who proceeds to retake possession through self-help may lose its rights to damages otherwise available under the lease or even incur liability to the tenant. Despite any provisions in the lease allowing the landlord to retake possession of the leased premises, it is risky for a landlord to retake possession of an operating business. The tenant may have a claim against landlord for lost profits and even unfair trade practices (for which the court can award the tenant treble damages and attorney's fees). Additionally, the tenant may have a claim against the landlord for conversion of its personal property. Even when a lease contains a provision stating that the tenant will not hold the landlord liable for any damages suffered as a result of any self-help eviction, there are no guarantees that a court will enforce such a provision.

It is not uncommon for a third-party to have a perfected security interest in the tenant's inventory, equipment and other property or for the tenant to have leased property in the leased premises (such as cash registers, computers, telephone equipment, and soda machines). The landlord should be aware that changing the locks on the leased premises, even if the lease allows it, also puts the landlord at risk of claims by third-parties. If the landlord does elect to retake possession through self-help, the landlord should carefully go through the leased premises to look for leased items. Additionally, upon changing the locks on the premises the landlord should post contact information somewhere on the leased premises.

The landlord can avoid potential claims by the tenant and third-parties by filing a summary ejectment complaint. Although the

3. Self-help remedies for residential leases are strictly prohibited by N.C.G.S. § 42-25.6.

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summary ejectment procedure may take a month or more, depending on the county, the landlord is able to avoid the risks of a self-help eviction. The process if fairly simple and inexpensive.

F. Summary Ejectment

If the landlord elects to proceed with summary ejectment, after properly noticing the tenant's default and giving the tenant the opportunity to cure the default (if applicable), the landlord must file a summary ejectment complaint with the court in the county where the property is located. Summary ejectment is a simple process but the landlord must be careful to follow the proper procedures. The landlord will be required to attend the summary ejectment hearing. If the landlord prevails, the landlord will be required to wait ten days after obtaining the judgment from the court to see if the tenant appeals the judgment. If the tenant does not appeal, the landlord can get the court to issue a writ of possession and wait for the sheriff to arrange the date and time the landlord can change the locks on the leased premises (usually takes seven to fourteen days).

1. Filing the Complaint

The forms necessary for filing a complaint in summary ejectment are available at the website for the administrative office of the courts www.nccourts.org/Forms. The complaint in summary ejectment (AOC-CVM-201) must be filled out along with the magistrate summons (AOC-CVM-100).[4] The forms must be filled out completely.[5] The landlord should check the forms carefully before filing them as the magistrate may dismiss the case if the forms are not filled out properly.

The complaint must be filed in the county in which the leased premises is located. The landlord needs to check to make sure that it files the complaint in the proper county; the landlord should not rely on the city to determine the county, but should check the street address of the leased premises to determine the county in which the leased premises is located (some cities can be partly located in different counties). The address of the leased premises should be listed on the summons and the complaint along with the tenant's phone number. The sheriff will serve the complaint by posting a copy at the leased premises.

Additionally, the tenant's name also must be listed correctly on both the summons and the complaint. If the tenant is a corporation, the landlord should check the North Carolina Secretary of State's website to make sure that the corporation's name has not changed. The landlord does not want to risk having a judgment on the summary ejectment complaint that does not contain the tenant's proper name.

Before filing the complaint with the court, the landlord should contact the clerk's office to determine whether that office has adopted local policies or procedures. For example, some clerks will require that a stamped envelope addressed to the tenant be included with the summary ejectment complaint and magistrate summons. While some clerks have adopted local policies and procedures, others are uniform across the state. For example, filing fees for summary ejectment proceedings are uniform. Currently, it will cost the landlord $76 to file a summary ejectment complaint and $15 per defendant for a magistrate summons and complaint to be served. However, the courts may increase the filing fees on occasion and the prudent landlord should check with the clerk before filing the complaint. When filing the complaint, the landlord must tender all filing fees and must provide the clerk of court with multiple copies of the summons and complaint. At that time, some counties will allow the landlord to select the hearing date, while others will simply assign hearing dates based on availability. Either way, the hearing date is typically within two weeks from the date of filing. The landlord will either be notified of the assigned hearing date at the time of filing or will receive notification from the clerk of court at a later date.

The jurisdictional limit of small claims court is currently $5 thousand and therefore, if the landlord is owed more than $5 thousand, the landlord must bring a separate action for the amounts owed in either district court or superior court. Our courts have held that all of a party's damages resulting from a single wrong must be recovered in one action. *Mangum v. Nationwide Mut. Fire Ins. Co.*, 61 N.C. App. 721, 724-25, 301 S.E.2d 517, 519 (1983). It is important not to try to recover a portion of the past due rents in the summary ejectment action with the idea that a separate action can be filed in superior or district court for the remaining amount. In *Chrisalis Props., Inc. v. Separate Quarters, Inc.*, 101 N.C. App. 81, 87, 398 S.E.2d 628, 633 (1990), the magistrate awarded plaintiff landlord possession of the leased premises and additionally awarded the landlord the maximum jurisdictional amount ($1,500 at that time). Because landlord was owed more than $1,500, the landlord then filed suit in superior court to collect the additional amounts owed. The trial court granted tenant's motion for summary judgment concluding that the summary ejectment order was res judicata to the breach of contract action filed in superior court. The North Carolina Court of Appeals agreed and held that despite the fact that the summary ejectment statute specifically allows a lessor to bring an action to regain possession of the leased premises separate from an action for damages does not create an exception to the general rule that all damages must be recovered in one action. *Id.* Therefore, if a landlord tries to recover any of the past due amounts (or damages for lost future rents) in the summary ejectment action, the landlord will be barred from pursuing additional damages at a later time. To avoid this problem, the landlord must seek possession only in the summary ejectment action. To ensure landlord is able to pursue an action for damages in superior or district court make sure somewhere on the summary ejectment complaint must contain the statement "[p]laintiff expressly reserves its right pursuant to G.S. § 42 28 to bring a separate action to recover its money damages." The landlord should also reiterate to the magistrate during the hearing that it is only seeking possession.

4. The magistrate summons is the document that gives the sheriff authority to serve the tenant with the complaint. The magistrate summons also provides the sheriff with the contact information for the tenant.
5. Copies of the forms are attached as Appendix. A.

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The day before the scheduled hearing date, the landlord must call to confirm with the clerk of court that the tenant has actually been served. If the tenant has not been served, the magistrate will postpone the hearing until service has been obtained and it is better to learn about it in advance and save a trip to the courthouse.

2. The Summary Ejectment Hearing

Many small claims courts do not give a time certain for the summary ejectment hearing so the landlord should be prepared to sit through other small claim hearings. All documents should be brought to the hearing such as the lease, any amendments, and any correspondence sent to the tenant, such as the demand letters and/or default notices. Some magistrate judges will want little or no information but it is better to be prepared with all documents. Furthermore, a summary ejectment hearing cannot be done without the client or by affidavit. An attorney must bring a representative of the landlord to testify as to the details of the default, the terms of the lease, the tenant's failure to cure, and the tenant's failure to vacate the leased premises.

The most common defense presented by the tenant is the failure of the landlord to follow the terms of the lease when defaulting the tenant. It is crucial that the landlord gives the tenant proper notice of default, pursuant to the provisions in the lease and that, if applicable, the tenant be given the requisite time to cure. If the tenant attends the hearing to contest the summary ejectment, the tenant may try to explain to the magistrate why it has not paid rent, such as the business has not been doing well. Occasionally, a tenant may try to argue that it has withheld rent as a result of landlord's default, such as the landlord failed to repair or blocked the parking lot. If tenant raises this defense, the landlord should check the lease carefully to determine what constitutes a landlord's default and whether the tenant can offset rent. Most leases require that if the landlord defaults, the tenant must give the landlord proper notice and the opportunity to cure:

> If landlord shall default in the observance of any material covenant or agreement herein contained and landlord does not cure such default within thirty days after notice thereof by Tenant . . .

Further, many leases provide that if the landlord defaults, the tenant may not set off rent. For example, the lease may provide:

> In the event of any default by Landlord, Tenant's exclusive remedy shall be an action for damages.

After hearing from both the landlord and the tenant, the magistrate will decide whether to award possession to the landlord.

3. Appeal Period

Once the magistrate awards possession of the leased premises to the landlord, the tenant has ten days from the date the judgment is filed to appeal to the district court the magistrate's ruling. N.C. Gen. Stat. § 7A-225 (2008). Because the appeal period runs from the date the judgment is actually filed, it is important to follow-up with the clerk to make sure the judgment is filed promptly. If is not unheard of for a judgment not to be filed for a week.

If the judgment is mailed to the parties by the court, then the time computations for appeal of such judgment is calculated pursuant to N.C. Gen. Stat. § 1A-1, Rule 6 (which provides for 3 extra days for the mail). If the magistrate announces his judgment in open court, the time for appeal starts running at that time even if the judgment is not actually filed with the clerk on the same day. *Provident Fin. Co. v. Locklear*, 89 N.C. App. 535, 536, 366 S.E.2d 599 (1988).

To stay the execution and remain in the leased premises, the tenant must pay to the clerk of court any back rent that the magistrate found due and timely pay rent going forward to the clerk of court. If the judgment is entered more than five working days before the day when the next rent will be due under the lease, the tenant must also pay the prorated rent for the days between the day that the judgment was entered and the next day when the rent will be due under the lease. N.C. Gen. Stat. § 42-34 (2008). Additionally, the tenant must also sign "an undertaking that he or she will pay into the office of the clerk of superior court the amount of the tenant's share of the contract rent as it becomes due periodically after the judgment was entered." *Id.* If the magistrate judge makes a finding in the record that based on the evidence "presented in court, that there is an actual dispute as to the amount of rent in arrears that is due and the magistrate specifies the specific amount of rent in arrears in dispute, to stay execution of a judgment for ejectment, the appealing tenant shall not be required to pay to the clerk of superior court the amount of rent in arrears found by the magistrate to be in dispute." *Id.*

If the tenant subsequently fails to pay rent going forward, the stay of execution will be dissolved and the landlord can then obtain a writ of possession on the subject property.

4. Writ of Possession

If the tenant fails to appeal within ten days, the landlord must file a Writ of Possession (AOC-CV-401) with the clerk of court in the county where the summary ejectment action was heard. The current fee for a Writ of Possession is $40 plus $15 for the sheriff's fee to serve it. The Clerk of Court will execute the Writ of Possession and forward it to the sheriff. The sheriff will contact the landlord and schedule a time to lockout the tenant. It is imperative that landlord include its phone number on the Writ of Possession so that the sheriff can contact the proper party to schedule the lockout. Under N.C. Gen. Stat. § 42-36.2, the sheriff is required to execute on the Writ of Possession no more than seven days from the sheriff's receipt thereof. Despite this statutory requirement, it is not uncommon for the sheriff in some counties to take up to two weeks to execute on a writ of possession. The landlord must keep in mind in

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dealing with the sheriff that it will not advance its interest by being rude.

The sheriff will require that a landlord's representative be present at the lockout. In most counties, the sheriff will give the landlord a time certain to be at the property for the lockout. The landlord will not have to do anything at the lock out, it only has to be present. The landlord should arrange to have a locksmith present to change the locks. If a landlord has any reason to believe that tenant may react violently, the landlord should inform the sheriff.

G. Suit for Damages

If the landlord's damages due to tenant's breach of the lease are $5 thousand or less, the landlord can ask for these damages in the summary ejectment complaint and potentially be awarded the amount at the summary ejectment hearing. If, however, the landlord's damages are greater than $5 thousand, the landlord will have to file suit for damages in district court (amount in controversy must be less than $10 thousand) or superior court.

The tenant, of course, will be liable for all rent that accrued prior to the time it vacated the leased premises. The landlord should read the lease to determine the tenant's additional liabilities for breaching the lease. If the landlord only terminates possession of the leased premises (not through a summary ejectment proceeding), the landlord can generally sue the tenant for lost future rent (the landlord should check the lease to make sure that collection of future rents is not precluded after possession is terminated). As discussed more fully above, if the landlord terminates the lease through summary ejectment or otherwise, the landlord can sue the tenant for damages caused by the tenant's breach of the lease. These damages will generally be measured by the value of the future rents discounted to a present value and reduced by any rent received by any new tenant.

1. Mitigation

Whether the landlord terminates possession or terminates the lease, the landlord will be required to mitigate its damages unless the lease specifically provides otherwise. The duty to mitigate means that a landlord must use reasonable efforts to relet the leased premises to a new tenant. *Isbey v. Crews*, 55 N.C. App. 47, 51, 284 S.E.2d 534, 537 (1981). If the landlord fails to use reasonable efforts to mitigate its damages, the landlord's recovery will be limited to "the difference between what he would have received had the lease agreement been performed, and the fair market value of what he could have received had he used reasonable diligence to mitigate." *Crews*, 55 N.C. App. at 51, 284 S.E.2d at 537. What constitutes reasonable efforts to mitigate will be determined on a case by case basis.

Recent case law has held that a commercial lease provision which states that a landlord has no duty to mitigate its damages is valid. In *Sylva Shops Ltd. P'ship v. Hibbard*, 175 N.C. App. 423, 432, 623 S.E.2d 785, 792 (2006), the landlord sued tenant bagel shop for breach of lease, seeking unpaid rent and other amounts owed pursuant to the terms of the lease. The lease agreement contained a provision which relieved the landlord of its duty to mitigate. The North Carolina Court of Appeals held that the parties, in an arms length commercial transaction, could contract to avoid the duty to mitigate. "We can perceive of no basis for precluding a party from contracting to relieve itself from a duty of due care to minimize its damages." Sylva, 175 N.C. App. at 429, 623 S.E.2d at 790. The North Carolina Court of Appeals reasoned that commercial real estate lease transactions generally involve relatively equal bargaining power. *Id.* Therefore, the landlord can relieve itself of the power to mitigate by a provision in the lease. See also *Kotis Props., Inc. v. Casey's Inc.*, __ N.C. App. __, 645 S.E.2d 138 (2007).

2. Additional Damages

The lease may also permit the landlord to sue for other damages caused by the tenant's breach of the lease. These damages often include the cost to relet the leased premises, the cost to repair the leased premises and any other costs incurred by the landlord as a result of the tenant's breach. For example, the lease may contain the following language allowing the landlord to recover additional damages:

> In case of a default, tenant shall be liable to landlord for broker's fees incurred by landlord in connection with reletting, the costs of removing and storing tenant's property, the costs of repairing, altering, and the costs of remodeling or otherwise putting the leased premises into a condition that is acceptable to a new tenant.

Many leases also allow the landlord to recover attorney's fees. The North Carolina Supreme Court in *Stillwell Enters., Inc. v. Interstate Equip. Co.*, 300 N.C. 286, 291, 266 S.E.2d 812, 815 (1980) held that a lease is evidence of indebtedness and therefore falls under N.C. Gen. Stat. § 6-21.2, the statute which authorizes the award of attorney's fees. *Id.* In order to recover attorney's fees, however, the landlord must comply with the requirements of the statute by providing written notice to the tenant of the amounts due and owing. *Id.* The notice must state that tenant has five days to pay the amount owed. Attorney's fees are limited by N.C. Gen. Stat. § 6-21.2 to 15 percent of the outstanding balance. If the lease doesn't specify the amount of attorney's fees recoverable, it is construed to mean 15 percent of the outstanding balance. *Devereaux Props., Inc. v. BBM & W, Inc.*, 114 N.C. App. 621, 626, 442 S.E.2d 555, 558 (1994).

III. Landlord's Liens

As demonstrated above, landlords have a variety of options when faced with the prospect of a breaching tenant. Each of these options, however, is fraught with the risk that the landlord will be unable to recover the full amount due and owing under the terms of the lease, let alone for any incidental or consequential damages arising from the breach. Yet, the landlord can obtain additional security through a landlord's lien, whereby the landlord obtains,

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either by contract or through operation of law, an interest in all of the tenant's personal property located within the leased premises.

A. Contracting for a Lien

Under N.C. law, a landlord may contract for a lien on a tenant's property by virtue of the lease agreement or a deed of trust. See *Dunham's Music House, Inc. v. Asheville Theaters, Inc.*, 10 N.C. App. 242, 245, 178 S.E.2d 124, 126 (1970) (holding that a lease provision stating that "all items not removed…shall become Lessor's property" was sufficient to create a security interest in the tenant's property); see also *Faison v. Hicks*, 127 N.C. 371, 372, 37 S.E. 511, 512 (1900). Therefore, many leases contain a provision which explicitly grants the landlord a lien on the tenant's personal property; such as a provision containing the following language:

> To secure the payment of all rent due and to become due hereunder and the faithful performance of this Lease by Tenant and to secure all other indebtedness and liabilities of tenant to landlord now existing but hereafter incurred, tenant hereby gives to landlord an express first and prior contract lien and security interest on all property which may be placed in the leased premises….

While contractually based, the validity and efficacy of a landlord's lien is governed by Article 9 of the Uniform Commercial Code ("UCC"). See *Dunham's Music House, Inc.*, 10 N.C. App. at 245, 178 S.E.2d at 126 (N.C. law recognizes that "a lien on personal property granted a lessor by contract is not excluded from the provisions of the Uniform Commercial Code.")(emphasis added); RICHARD R. POWELL, POWELL ON REAL PROPERTY, 16A.01 [5][b] (2000)("The contractual landlord's lien generally is considered a chattel mortgage. The lien therefore falls within the definition of 'security interest'..."). Article 9 requires that any security interest in the personal property of another be perfected to establish a valid interest in the property as against the claims of any third party. See N.C. Gen. Stat. § 25-9-308 (2008). "[A] security interest is perfected if it has attached and all of the applicable requirements for perfection in G.S. 25-9-310 through G.S. 25-9-316 have been satisfied." *Id.*

Typically, contractual landlord's liens are perfected by (1) executing a lease which contains provisions explicitly providing for a lien in favor of the landlord ("attachment"); and (2) executing and filing a financing statement with the North Carolina Secretary of State's office as set forth in N.C. Gen. Stat. §§ 25-9-310, 25-9-501 ("perfection"). The financing statement must provide the legal name and address of the tenant (debtor), the name and address of the landlord (creditor), and a description of the property to which the lien will attach. N.C. Gen. Stat. § 25-9-502 (2008); N.C. Gen. Stat. § 9-25-521 (2008) (providing a form financing statement, which, if fully completed, will satisfy the requirements of N.C. Gen. Stat. § 25-9-502). The financing statement will be valid for a period of five years, but must be renewed within 6 months of expiration to maintain the landlord's interest with regard to any third party creditors. See N.C. Gen. Stat. § 25-9-515 (2008).

If the landlord fails to file a financing statement (or fails to timely renew a financing statement), the landlord may still perfect its security interest in the tenant's personal property by taking physical possession of that property. See N.C. Gen. Stat. § 25-9-313 (2008) ("a secured party may perfect a security interest in tangible negotiable documents, goods, instruments, money or tangible chattel paper by taking possession of the collateral"); see also *Dunham's Music House, Inc.*, 10 N.C. App. at 247, 178 S.E.2d at 127. It should be noted, however, that taking possession of the property will not insulate the landlord from claims of third-party creditors who perfected their interest in the property by filing a financing statement prior to the landlord's taking possession of the property. Therefore, the prudent landlord will perfect its interest by filing a financing statement upon execution of the lease.

B. Statutory Lien

If the lease does not provide for or prohibit the creation of a lien on the tenant's personal property, a landlord may still obtain a lien under N.C. Gen. Stat. § 44A-2(e), which provides that:

> Any lessor of nonresidential demised premises has a lien on all furniture, furnishings, trade fixtures, equipment and other personal property to which the tenant has legal title and which remains on the demised premises if (i) the tenant has vacated the premises for 21 or more days after the paid rental period has expired, and (ii) the lessor has a lawful claim for damages against the tenant.

Id. Where these requirements are met, the landlord may enforce its lien by conducting a public sale pursuant to the provisions of N.C. Gen. Stat. § 44A-4(e) (2008). The amount of the lien is limited to: unpaid rent due and owing at the time the tenant vacated the premises; rent "for the time, up to 60 days, from the vacating of the premises to the date of" any sale of the property; expenses relating to any necessary repairs to the premises; and the reasonable costs and expenses of any sale of the property. *Id.* Any additional amount realized by virtue of the sale must be returned to the tenant or any other person legally entitled to the funds. N.C. Gen. Stat. § 44A-5 (2008).

As with contractual landlord's liens, the landlord must perfect its interest in the tenant's personal property to protect it against the claims of third-party creditors. In N.C., statutory liens on tenant's personal property are automatically perfected 21 days after the tenant vacates the premises, so long as the landlord has a valid claim against the tenant for unpaid rent, damage to the property, etc. N.C. Gen. Stat. § 44A-2(e). However, any lien perfected under N.C. Gen. Stat. § 44A-2(e) will not have priority over any security interest in the property which was perfected at the time the landlord acquired its lien. *Id.* Thus, if a tenant vacates the leased premises and leaves behind personal property, the chances are (1) there is nothing of value, or (2) another creditor, such as a bank, has a per-

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fected security interest in the property that trumps any interest the landlord may claim under the statute.

The statutory lien set forth in N.C. Gen. Stat. § 44A-2(e) therefore provides the landlord with a limited security interest in the tenant's (abandoned) personal property that provides less security than is provided in the typical, contractually-based landlord's lien. As such, the prudent landlord should provide for a lien on all of tenant's personal property within the provisions of the lease, and execute and file the requisite UCC financing statement to ensure that its interests are fully secured. A landlord simply should not count on recovering any funds through execution of a statutory lien.

C. Determining the Priority of a Landlord's Lien

The creation of a landlord's lien is just the first step in the process of realizing on a tenant's personal property in satisfaction of any amounts due and owing the landlord. The second step involves determining the rank, or priority, of the landlord's interest *vis a vis* the interests of any third-party creditors in the same property. When making this determination, the landlord must first determine whether its lien is statutory or contractual in nature. If it is statutory, it is subordinate to all prior-perfected security interests. See N.C. Gen. Stat. § 44A-2(e) ("This lien shall not have priority over any security interest in the property which is perfected at the time the lessor acquires this lien."). If it is contractual, Article 9 of the UCC governs priority. See generally, *Dunham's Music House, Inc.*, 10 N.C. App. at 245, 178 S.E.2d at 126; POWELL SUPRA. Where there are conflicting security interests in the same collateral, the requirements set forth in N.C. Gen. Stat. § 25-9-317 and § 25-9-322 generally determine which party has the superior interest in and right to the collateral. Under these provisions, priority is afforded the party which is the first to file a financing statement as set forth in N.C. Gen. Stat. § 25-9-501 or which is the first to perfect its interest under N.C. Gen. Stat. §§ 25-9-301 (2008), *et seq.* Furthermore, "[a] perfected security interest…has priority over a conflicting unperfected security." See N.C. Gen. Stat. § 25-9-322(a)(2) (2008) (emphasis added). However, where there are competing unperfected security interests, the first security agreement to attach to the property (as set forth in N.C. Gen. Stat. § 25-9-203) will have priority. Again, the prudent landlord should provide for a landlord's lien in the lease and file a UCC financing statement immediately upon execution of the lease to ensure a greater chance of having a priority interest in the tenant's personal property should the tenant default on the lease.

<u>1.</u> <u>Tax Liens</u>

Occasionally, a landlord's interest in the personal property of a tenant will conflict with the interests of state and/or federal taxing authorities. Where the property is encumbered by a state or federal tax lien, the validity and priority of the tax lien *vis a vis* the landlord's lien generally will be determined outside the confines of Article 9 of the UCC.

Under N.C. Gen. Stat. § 105-242, the Secretary of the North Carolina Department of Revenue "may file a certificate of tax liability to collect a tax that is owed by a taxpayer and is collectible under G.S. 105-241.22." The certificate must be filed with the clerk of superior court in any county in which the taxpayer resides or has property and must identify the taxpayer, "and the type and amount of tax owed." N.C. Gen. Stat. § 105-242(c) (2008). The clerk of court will record the certificate of tax liability as if it were a judgment and is enforceable in the same manner as other judgments. The priority of state tax liens created under N.C. Gen. Stat. § 105-242 is determined under N.C. Gen. Stat. § 105-356(b), which provides that:

> (1) The tax lien, when it attaches to personal property, shall, insofar as it represents taxes imposed upon the property to which the lien attaches, be superior to all other liens and rights whether such other liens and rights are prior or subsequent to the tax lien in point of time.
> (2) The tax lien, when it attaches to personal property, shall, insofar as it represents taxes imposed upon property other than that to which the lien attaches, be inferior to prior valid liens and perfected security interests and superior to all subsequent liens and security interests.
> (3) As between the tax liens of different taxing units, the tax lien first attaching shall be superior.

In other words, if the tenant has failed to properly pay taxes on inventory, and a tax lien is subsequently filed on that inventory, then the tax lien will be superior to all other security interests-even those that arose prior to the existence of the tax lien. However, it the state files a tax lien against the tenant's property for failing to pay a tax that is unrelated to that property, priority will be governed by the time of perfection. Thus, if a landlord perfects its interest in the tenant's personal property prior to the state's filing of a certificate of tax liability under N.C. Gen. Stat. § 105-242, then the landlord will be entitled to realize on the property.

The Internal Revenue Service may also have a lien on the tenant's personal property under 26 U.S.C. § 6321, which provides that "[i]f any person liable to pay any tax neglects or refuses to pay ... the amount (including any interest, additional amount, addition to tax, or assessable penalty ...) shall be a lien in favor of the U.S. upon all property and rights to property, whether real or personal, belonging to such person." As with state tax liens, a tax lien imposed under 26 U.S.C. § 6321 will be treated like and have the effect of a judgment, see, *e.g.*, *Citizens Nat'l Trust & Sav. Bank v. United States*, 135 F.2d 527 (9th Cir. 1943), and will be effective as against holders of security interests, mechanic's lienors, and judgment lien creditors, upon filing a notice of tax liability as set forth in 26 U.S.C. § 6323(f).

Where there are competing interests in the tenant's property, one of which arises under 26 U.S.C. § 6321, federal law will govern the priority of any security interest arising under state law versus any federal tax lien. See *Wallace Resources v. United States*, 1997 U.S.

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App. LEXIS 24933, *7; 97-2 U.S. Tax Cas. (CCH) P50, 666 (4th Cir. 1997) (unpublished). "The general rule of priority under federal law is that federal tax liens attach to a taxpayer's property and are entitled to absolute priority unless otherwise provided by statute." *Id.* at eight (citing *United States v. City of New Britain, Conn.*, 347 U.S. 81 (1954)).

Section 6323(a) provides exceptions to the general rule where the competing interests include prior perfected security interests, mechanic's liens, and judgment liens. The term "security interest", as used in this statutory provision, includes "any interest in property securing payment of an obligation which has become protected under local law against a subsequent judgment lien arising out of an unsecured obligation." 68A AM. JUR. 2D Secured Transactions § 878 (2008). Thus, Section 6323 encompasses perfected security interests arising under Article 25 of the North Carolina General Statutes, which includes contractually based landlord liens. Under the exception provided in Section 6323(a), any federal tax lien will be subordinate to any prior perfected security interest, mechanic's lien, or judgment lien.

However, in keeping with the UCC's preference for perfected interests, a federal tax lien is superior to any unperfected security interest arising under the Code, even where the government has knowledge of any pre-existing, unperfected interest. See, *e.g.*, *Schnarr v. United States*, 795 F. Supp. 934 (E.D. Mo. 1992) (applying Missouri law). While there is no N.C. case law directly on point, there is case law suggesting that a landlord's lien arising under N.C. Gen. Stat. § 44A-2(e) would not be afforded priority over a federal tax lien unless and until the landlord executed the lien by holding a public sale pursuant to the requirements set forth in N.C. Gen. Stat. § 44A-4(e) or otherwise reduced the lien to a valid judgment. See, *e.g.*, *Thompson v. Cline*, 1994 U.S. Dist. LEXIS 2748, *8 (S.D.Fla. 1994) (holding that a landlord's lien does not qualify for special protection under 26 U.S.C. § 6323(a)) (citing *United States v. Morrison*, 247 F.2d 285 (5th Cir. 1957); *United States v. Scovil*, 348 U.S. 218, 75 S.Ct. 244 (1955)); *United States v. Leventhal*, 316 F.2d 341 (D.C. Cir. 1963).

Thus, with regard to state and federal tax liens, the prudent landlord will again provide for a landlord's lien in the lease and file a UCC financing statement immediately upon execution of the lease to ensure that its interests are protected as against the government.

2. Bankruptcy and Landlord's Liens

When a bankruptcy is filed, the bankruptcy trustee must assume or reject the nonresidential lease by the earlier of (i) 120 days after the date of the order for relief; or (ii) the date of the entry of an order confirming a plan. 11 U.S.C. § 365(d). This period may be extended for one period of 90 days upon a showing of cause. If the trustee rejects the lease, the "rejection will operate as a breach of the lease as of the date of the filing of the petition." Collier on Bankruptcy 503.06[6][c] p. 503-38. In the event the trustee assumes the lease, monthly rents must be paid as they become due and any past due rent must be cured within a reasonable amount of time. Shopping center landlords are provided additional protections under 11 U.S.C. § 365(b)(3). In the event the trustee rejects the lease, the landlord will have a three pronged claim. First, it will have an unsecured claim for all rents and other amounts due prior to the filing of the bankruptcy petition. Second, it may have an administrative priority claim for rents and other amounts due between the date of the filing of the petition and the date the trustee rejected the lease. Under 11 U.S.C. §§ 503(b) and 507, the landlord must show the debtor derived some benefit from the lease and the premises during this time period in order to qualify for administrative expense priority. If the premises were vacant during this period, the landlord is not likely to have an administrative expense priority claim. Third, the landlord will have an unsecured claim for rents and other amounts due under the rejected lease for the remaining term of the lease; however, the amount of rent that a landlord can claim under this third prong is subject to and limited by the formula set forth in 11 U.S.C. § 502(b)(6).

In addition to having the aforementioned claim for prepetition and possibly post petition rents, the landlord may also have a statutory landlord's lien under § 44A-2(e). A statutory landlord's lien can be avoided, however, by the bankruptcy trustee under 11 U.S.C. § 545(3) and therefore, offers little protection for landlords. In *re Harrell*, 55 B.R. 203 (1985). 11 U.S.C. § 545 provides that:

The trustee may avoid the fixing of a statutory lien on property of the debtor to the extent that such lien--

> (1) first becomes effective against the debtor
> (A) when a case under this title concerning the debtor is commenced;
> (B) when an insolvency proceeding other than under this title concerning the debtor is commenced;
> (C) when a custodian is appointed or authorized to take or takes possession;
> (D) when the debtor becomes insolvent;
> (E) when the debtor's financial condition fails to meet a specified standard; or
> (F) at the time of an execution against property of the debtor levied at the instance of an entity other than the holder of such statutory lien;
> (2) is not perfected or enforceable at the time of the commencement of the case against a *bona fide* purchaser that purchases such property at the time of the commencement of the case, whether or not such a purchaser exists, except in any case in which a purchaser is a purchaser described in section 6323 of the Internal Revenue Code of 1986 [26 USCS § 6323], or in any other similar provision of State or local law;
> (3) is for rent; or
> (4) is a lien of distress for rent.

The bankruptcy trustee can avoid a landlord's lien even if the lien has been enforced by sale prior to the filing of the bankruptcy petition. *Donahue v. Gunner, LLC*, 197 Fed. Appx. 579, 2006 U.S. App LEXIS 20417 (9th Cir. 2006).