

# RETAIL PROPERTIES

## Quarterly

### Legal

## A guide to Colorado-specific laws in retail leases

**B**ehind every successful retail relationship is a carefully negotiated lease. I am not saying this just because I'm a leasing attorney (OK, maybe partly). A lease agreement inherently guides the operation of a retail space. When negotiating leases, retail landlords and tenants will need to consider various local, state and federal laws, along with applicable market considerations and deal-specific terms. In Colorado, there is not a single set of state laws or regulations that govern commercial leases; a majority of the landlord-tenant statutes apply only to residential leases. For the most part, the lease terms will govern the rights and obligations of the parties, and Colorado courts will enforce them accordingly. However, out-of-state landlords and tenants should be familiar with the following Colorado-specific laws that may affect their retail leases.

• **Mechanic's liens.** In Colorado, the mechanic's lien statutes (C.R.S. § 38-22-101 et seq.) provide very strong protection for construction professionals. This includes contractors, subcontractors, materialmen, builders, architects, engineers, draftsmen, artisans – pretty much anyone who provides services or materials to a construction project. A mechanic's lien can be filed after providing plans, drawings or cost estimates for such work, even before construction has commenced. The priority of the mechanic's lien will relate back to the very start of the work, so even a contractor who performs no work until the end of a project will have the same priority as the architect who drew the initial plans. Due to the simple, straightforward process, mechanic's liens are frequently filed when there is a legitimate dispute regarding the sufficiency of the work or the amounts owed. Therefore, both landlords and tenants should promptly and diligently seek lien waivers during the construction process. A lien waiver is an acknowledgement of payment and waiver of future lien rights from the construction professional. Because the lease will likely



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require a tenant to promptly pay any contractor with lien rights, the tenant should reserve its right to bond over mechanic's liens pursuant to C.R.S. § 38-22-131. This removes the lien from the premises while allowing the tenant to dispute the contractor's claim. If the tenant is handling the construction work, the landlord should post notices of nonresponsibility at the leased premises prior to the commencement of the work. If such a notice is properly posted, liens attach only to the tenant's leasehold interest, which will protect the overall retail center against mechanic's liens.

• **Landlord liens.** Unlike some states, Colorado does not provide landlords with an automatic lien against tenant's personal property in the leased premises. A landlord may want to have a claim on furniture, fixtures, equipment, goods and other trade items that add value to the retail space, particularly if the landlord helped pay for them. In order to obtain a security interest on tenant's personal property, the lease agreement should include the grant of a security interest or landlord lien in favor of the landlord, securing the tenant's obligations. The landlord will have to then perfect its security interest by filing a UCC-1 with the secretary of state in which the tenant entity was formed (for personal property) and a fixture filing in the county real property records (for fixtures). If the landlord does not obtain and perfect a security interest at the outset and subsequently pursues litigation and a judgment lien instead, the landlord will not have priority over the tenant's other creditors. On the other hand, the tenant may not want to provide a landlord lien. If the tenant is seeking outside financing for its business, the tenant's lender likely will want a first-priority security inter-

est on the tenant's business-related property. As a compromise, the landlord may be willing to subordinate its rights to the tenant's lender and maintain a second-priority security interest.

• **Eviction procedures.** Regardless of the default provisions in the lease agreement, the landlord will be required to comply with Colorado's eviction procedures. The Forcible Entry and Detainer statutes (C.R.S. §§ 13-40-101 et seq.) provide a streamlined court process for evicting commercial and residential tenants. Generally, the landlord will deliver a notice to quit, upon which the tenant will have three days to cure the default or vacate the leased premises. If the tenant fails to do so, the landlord will file a complaint and schedule a FED hearing. So long as the tenant does not file an answer to the complaint, the court likely will issue a writ of restitution within a couple of weeks. The sheriff's office will execute the writ by supervising the physical removal of the tenant's belongings from the leased premises. Unlike many other states, Colorado does not require the landlord to store or maintain the tenant's personal property removed from the premises after an eviction. The landlord cannot change the locks or exercise other self-help remedies to remove a tenant without following the FED procedures.

• **Duty to mitigate.** Similar to the eviction process, regardless of the lease language, the landlord has a common-law duty to mitigate damages. After a tenant defaults and no longer occupies the leased premises, the landlord will only be able to recover damages from a tenant in an amount that would put the landlord in the same position as if the breach had not occurred, less the amount received (or what would have been received) by the landlord's reasonable mitigation efforts. Although the landlord's duty to mitigate is well established, it is not clear what efforts actually are required. From the landlord's perspective, the lease should state that the landlord is not obligated to re-let the premises before leas-

ing other vacant space in the retail center. In addition, the landlord should only be required to accept a replacement tenant if such tenant meets the landlord's financial criteria, agrees to market lease terms and contributes to the tenant mix of the retail center, as determined in the landlord's discretion. From the tenant's perspective, the tenant should require the landlord to use reasonable efforts to market the premises in the same manner that the landlord markets other available space in the retail center.

• **Post-termination damages.** If a tenant defaults, the landlord typically has the right to terminate the lease or to terminate the tenant's right of possession of the premises, with or without terminating the lease. If the lease is not terminated, the landlord will continue to collect rent as it becomes due under the lease, less the amount received from the landlord's mitigation efforts (as discussed above). The landlord should not terminate the lease unless the lease expressly provides for the right to seek damages after the lease termination. The landlord will want an acceleration clause for damages, which allows the landlord to collect all unpaid rent amounts for the remainder of the lease term as a lump sum payment. Since the landlord's full recovery of the remaining rent amounts would provide a benefit to the landlord that is not bargained for, the tenant will want to adjust the lump sum payment by its present value or the fair rental value of the premises (since the landlord should be able to recover the fair rent value from a new tenant).

• **Conclusion.** As new landlords and tenants navigate Colorado's retail landscape, the Colorado-specific issues in this article are just some of the legal issues to consider in a commercial lease. Consult an attorney when negotiating a commercial lease or dealing with a specific leasing matter. This article is for general information only and does not constitute legal advice.▲