# LEASE

# MITIGATION

***Counsel's Corner***

Mitchell Rudder Properties, LP sued GKG.Net, Inc. for breach of a commercial lease agreement. The jury awarded judgment to Rudder, and GKG appealed to the Houston Court of Appeals.

GKG had extended its lease until March 31, 2013. In 2006 GKG defaulted and Rudder took possession. At the time of the default GKG was paying $13.56 PSF per year.

Rudder quickly signed a replacement lease with World Savings Bank. World was later acquired by Wachovia. The replacement lease had a term through 2011, but World also reserved for itself a 'kick-out' or 'knockout' clause, where World could buy out of the last two years. Also, World reserved a five-year extension option.

Litigation was asserted by Rudder against GKG in 2006 for past due rents, diminished rents relative to the World lease, future rents for the unexpired original lease term (2011 World lease vs. 2013 GKG lease), and costs. Rudder was awarded damages in all categories requested, in addition to $314,123 for the two-year period of time after expiration of the World Lease.

GKG appealed only the $314k component, claiming that the jury improperly failed to grant an offset for the value of the lease during the two year period. Rudder's property manager had testified in court that ". . . nobody that I know as an investor that would buy that tenth year – or year 11 and the last 3 months of 12 as an income stream for anything when they'd [World Savings] had already vacated the building. So we didn't assign any value to that."

The Houston Court of Appeals reviewed a pivotal 1997 Texas Supreme Court ruling, and more current case authority, and concluded that ". . . the reasonable cash market value of a lease for its unexpired term means the reasonable cash market value of the property – not the reasonable cash market value of the lease that has been breached." Really the Court had little choice, because to do otherwise would mean that breaching tenants would never be entitled a fair market value offset for the balance of the lease term – that the remaining lease term is always worth zero.

In a further erosion of jury decisions, the Houston Court of Appeals therefore held that there is no evidence to support the jury's decision that the reasonable cash market value for the remainder of GKG's term is zero, and that Rudder was entitled to the full rental value of $314,123. The trial court's judgment was reversed and the case returned to court for a new trial.

<u>Lessons learned</u>:

1. A really good lawyer is going to fight really hard for every penny due you.
2. The residual years of a long-term commercial lease have value.
3. It is the non-waivable duty of a Texas landlord to mitigate its losses for the entire duration of the lease term.

I don't know what happened as I was not personally involved, but surely Rudder would have been more pleased to allow GKG some type of rental offset for the two-year gap period at the end of the term, then have to start over with a new trial.

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