

The Landlord's Lien: An Often Overlooked Remedy For a Tenant's Default

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The recent slowdown in the economy makes it almost certain that there will be an increase in the number of tenants who default in their rental payments and, hence, there will be a corresponding increase in the number of landlords seeking to recover such payments. Two remedies available to landlords are often neglected or improperly utilized: Both the statutory landlord's lien and a consensual security interest created pursuant to the Uniform Commercial Code (the "UCC") can afford a landlord remedies against a defaulting tenant by giving a landlord liens on the tenant's property.

This article first discusses the local statutes and jurisprudence of Virginia, the District of Columbia and Maryland and explains the processes by which a landlord may enforce the landlord's lien granted by statute or common law. The article then discusses how a landlord can further protect itself by including express language in its lease form in order to create a consensual lien under Article 9 of the UCC. By understanding the creation and enforcement of these liens, a landlord can enhance its potential monetary recovery against a defaulting tenant.

The Statutory or Common Law Landlord's Lien

A landlord's lien is the right, granted by statutory or common law or by agreement of the parties, of a landlord to levy upon the goods of a tenant who has failed to pay its rent. Each of the three local jurisdictions, Virginia, Maryland and the District of Columbia, afford a landlord a

lien, outside the scope of Article 9 of the UCC, on the tenant's tangible personal property.

However, the creation and enforcement of the statutory or common law lien differs slightly in each jurisdiction.

Virginia:

Specifically, Virginia Code Sections 55-227, 231 and 233 automatically grant the landlord a lien on any goods belonging to the tenant, or the tenant's assignee, found on the premises or which may have been removed from the premises no more than thirty days' prior to the landlord's exercise of the lien. The landlord does not need to take any steps to perfect the lien as the landlord is granted the lien by virtue of the lease or contract for rent. Further, the courts have described the lien as one that is "fixed and specific and not one which is merely inchoate." *See, e.g., Virginia Nat'l Bank v. Balistreri*, 8 Bankr. 703 (Bankr. E.D. Va. 1981). That is, the lien relates back to the commencement date of the lease and is superior to any other lien upon the tenant's property located in the premises, except a tax lien of the United States, and liens fixed prior to the commencement of the tenancy. The only other exception to the lien is the "shifting stock" of a retail tenant. *American Exch. Bank v. Goodlee Realty Corp.*, 116 S.E. 505 (Va. 1923).¹

The landlord may enforce the lien by instituting a distress action for rent, which is an *in rem* action against the tangible personal property of a tenant who is delinquent in rental payments. The lien is enforced by obtaining a distress warrant to "distrain" *i.e.*, levy or seize, the

¹ Section 55-231 also limits the lien to not more than six months' rent "if the premises are in a city or town, or in any subdivision of suburban and other lands divided into building lots for residential purposes, or of premises anywhere used for residential purposes, and not for farming, or agriculture, and for not more than twelve months' rent oif the lands or premises are used for farming or agriculture whether it shall have accrued before or after the creation of the lien."

tenant's tangible personal property to pay the rent due. The action must be brought within five (5) years from the time the rent becomes due, whether or not the lease has terminated. Va. Code § 55-230. To institute the distress action, the landlord must first file with the court a sworn petition for the issuance of the distress warrant that states the following: (i) the amount of rent due and owing, (ii) that the petition is for rent due within the last five (5) years, and (iii) whether the landlord wants to either levy or seize of the property. However, the petition must also contain an assertion by the landlord that the tenant intends to flee the state, to conceal himself from creditors or to assign, sell or destroy the property, and this assertion may be difficult to make in each instance. *Id.* at § 8.01-534.

As noted, in the petition, the landlord may request either a pre-trial levy on the property or a pre-trial levy and seizure of the property. If the landlord seeks only pretrial levy on the property, he must post a bond equal to the estimated fair market value of the property before the warrant is issued. The property then remains in the possession of the tenant but may not be removed from the property or sold prior to judgment. If the tenant or another person removes the levied goods, the landlord may maintain an action against the person and recover a personal judgment. *See American Exch. Bank v. Goodlee Realty Corp.*, 135 Va. 505 (1923). However, a lienor with a lien inferior to the landlord's lien may remove the goods from the premises if the lienor pays the rent owed and "secur[es] to [the landlord] so much [rent] as to become due." Va. Code Ann. § 55-233.

In the alternative, if the landlord chooses to seize the property, the landlord must post a bond equal to twice the estimated fair market value of the tenant's property, plus costs and damages, and the sheriff will take possession and hold the property until sale. The tenant may,

nevertheless, prevent the sheriff from seizing the property and may retain possession of the property by (i) posting a bond equal to the value of the property or (ii) providing an affidavit that the tenant has a valid defense to the action for distress and an inability to pay the bond.

If the levy or seizure is not contested by the tenant or if the tenant contests the levy or seizure but the court passes judgment for the landlord, the sheriff will arrange for the sale of the property. The amount of the lien to be recovered by the landlord is then established on the date of the sale if the levy is uncontested or on the date of judgment if contested. *See United States v. Melchiorre*, 292 F. Supp. 305 (E.D. Va. 1968).

The District of Columbia:

Pursuant to Section 45-1413 of the District of Columbia Code, landlords in the District of Columbia have an automatic statutory lien on a tenant's tangible personal property which is located on the leased premises and is subject to execution for debt. Like its Virginia counterpart, the District of Columbia Code provides that the lien is in effect upon the commencement of the tenancy. However, in contrast to Virginia, the landlord's lien in the District of Columbia continues only until three months after rent is due or until the termination of any action for such rent brought within the three-month period. As a result, landlords in the District of Columbia must be vigilant in policing their leases and take immediate action upon a default or risk losing one of their remedies for nonpayment of rent. As in Virginia, the landlord's lien is not superior to federal tax liens.

A landlord in the District of Columbia must follow a procedure similar in part to the procedure in Virginia. The landlord's lien may be enforced by attachment, by judgment and execution, or by action against any purchaser of tenant's personal property that had notice of the

lien. To enforce the lien by attachment, the landlord must provide the court an affidavit stating that rent is due and unpaid or that the tenant is about to remove or sell property that is subject to the lien, even if the rent is not due. D.C. Code Ann. § 45-1414(1). A judgment may be enforced by levy against the “chattels”, and may be done so in “whosoever hands they may be found.” *Id.* at § 45-1414(2). When commencing legal action against a third party purchaser of tenant’s property subject to a landlord’s lien, the plaintiff/landlord may obtain judgment for the value of the chattels purchased by the defendant, not to exceed the rent owed. *Id.* at § 45-1414(3). The District of Columbia Code even provides that any officer to whom a writ of attachment is delivered to be executed may “break open an outer or inner door when necessary to the execution of the same.” *Id.* at § 45-1415. A tenant fraudulently removing or conveying its personal property as well as any person willfully and knowingly assisting a tenant in doing so or concealing the same, may be liable in damages to the landlord in an amount equal to double the value of the personal property removed or concealed. *Id.* at § 45-1418.

Maryland:

In Maryland, there is no automatic statutory lien. Rather, the Maryland Code provides a landlord an action for distress for rent. Md. Code Ann. § 8-302. The landlord’s success in this cause of action can give rise to a lien on a tenant’s personal property, which can then be levied upon.

Once the landlord has created a lien, the procedure to enforce it is much like the procedures in Virginia and the District of Columbia. To create the lien, the landlord must bring an action in court for distress, specifically, for “unpaid rent under a written lease for term of more than three months, or under a tenancy at will or periodic tenancy that has continued more

than three months.” *Id.* at § 8-302. The court will issue an order directing the tenant to appear at a hearing to present evidence on his behalf, and the tenant may file an answer to the distress action setting forth any defenses, including the defense that the landlord has charged excess rent. In the event that the tenant fails to appear, all goods on the premises may be levied upon and removed by the sheriff. If the landlord shows the court that the property needs to be protected, the court will order removal of the goods prior to the sale. *Id.* at § 8-310. The court may, however, require the landlord to post a bond before the goods are removed. *Id.* In making a final determination, the court has the power to increase the amount requested by the landlord to include the amount of any rent accruing after the filing of the petition up to the date of sale. *Id.* at § 8-314. If the court orders a sale of the goods at auction, only those goods necessary to satisfy the claim for rent may be sold. Any unsold goods must be returned to the tenant, although another judgment creditor may petition the court for satisfaction of its judgment from the sale of any excess proceeds or goods. *Id.* at § 8-320. In the event that the proceeds are insufficient to satisfy the landlord's claim for unpaid rent, the landlord may petition the court for a deficiency money judgment against the tenant. *Id.* at § 8-325. The sale of any goods belonging to third parties is permitted only after the sale of all of the tenant's goods and only in the event that the proceeds are necessary to satisfy the claim. The third party then has a claim for damages against the tenant.

Upon a “determination of reasonable probability” that a landlord is owed the past rent claimed, a court will issue an order directing that all goods² on the leased premises not exempted

² Section 8-301(e) of the Maryland Code defines “goods” as “goods, chattels, grain, growing crops, produce, unborn young of animals, inventory, and equipment” regardless of where found or located, and includes cash money found on the leased premises. Section 8-301(e) of the Maryland Code goes on to state that “goods” does not include

by law³ shall be levied on. *Id.* at § 8-305(a). Goods located on the premises, which are not property of the tenant, may be subject to levy as well. Where a third party has a perfected security interest in goods prior to levy under the distraint by landlord, the landlord must either release the property from the distraint proceedings or pay the holder of the security interest the balance of the debt owing which gives rise to such security interest. *Id.* The landlord must certify to the court as to the existence of a prior security interest in any levied upon goods of the tenant. *Id.* at § 8-307.

If the levy has been made on goods owned by a third party, the third party may file a petition with the court within seven days after the levy for an order to exclude the goods not owned by the tenant. *Id.* at § 8-311. If no petition to determine ownership of goods is filed by any third party within such seven day period, all of the goods on the leased premises and included in the inventory are conclusively presumed to be the goods of the tenant. *Id.*

Summary

The statutory landlord's lien is useful but its use is limited in several respects. The landlord may only collect for unpaid rent and may only seize the tenant's tangible personal property that is located on the premises, in many instances, within a specific timeframe.

Although it has been suggested that a landlord could define "rent" broadly in the lease, so that

“choses in action, other forms of intangible property, written contracts, securities, bonds, notes, or other instruments for the payment of money”.

³ Section 8-307(a) of the Maryland Code exempts the following items from levy:

- 1) hand powered and operated tools used by the tenant in his occupational livelihood,
- 2) law books of an attorney;
- 3) hand operated instruments of a physician;
- 4) medical books of a physician;
- 5) files and professional records of an attorney or physician; and
- 6) the prior perfected security interest and all goods in which the tenant has an interest.

the statute would apply to more than a monetary default, there is no current case law to support this creative solution. Furthermore, if a tenant that has defaulted on its rent files a petition for bankruptcy, the landlord may be barred from enforcing the lien by the automatic stay or the trustee may avoid completely the landlord's lien pursuant to 11 U.S.C. § 545 (3) or (4). Finally, many sophisticated tenants request a waiver of the statutory or common law lien or seek to have a landlord's lien rights subordinated to those of a purchase money or other lender party. While a subordination of a lien is preferable to a complete waiver, the practical result may be that nominal or insufficient unencumbered value exists thereby undercutting the effectiveness of the statutory lien.

The Consensual Security Interest

As the statutory or common law landlord's lien is somewhat limited, a landlord may further protect itself by including express language in the lease to create a consensual security interest in the tenant's property under Article 9 of the UCC. Attached hereto in Appendix I is suggested language that may be included in lease agreements to establish a consensual lien and to provide enforcement remedies pursuant to the UCC.

Article 9 of the UCC governs security interests in personal property and fixtures, including, but not limited to, goods, instruments, general intangibles, chattel paper or accounts. A written security agreement is needed to create the security interest and hence, the landlord must include express language in the lease regarding the security interest and describing the collateral. The landlord could and should describe the collateral broadly such that it encompasses all categories of property, personal, intangible and otherwise, used by the tenant in the conduct of its business, inclusive of after-acquired collateral. The security interest attaches

when the debtor has signed the security agreement, *i.e.*, the lease, value has been given, and the debtor has rights in the collateral or, according to revised Article 9, the power to transfer rights in the collateral to the secured party.

The inclusion of the language in the lease is insufficient to give the landlord priority over other security interests. Rather, the landlord must also perfect the security interest by filing a financing statement in the proper recording office. If the landlord fails to do so, the landlord's interest will be subordinate to a creditor whose security interest is perfected. While a conscientious landlord may remember to include the security interest language in the lease, he may forget the necessity of filing the financing statement. The revised Article 9 has made the filing easier as the financing statement may now be filed without the debtor's, *i.e.*, tenant's, signature so long as the filing is "authorized."⁴ Nevertheless, not only must the landlord remember to file the financing statement in the proper recording office as required by the revised Article 9, the landlord must also maintain a system of tracking the statements prior to their expiration so that the landlord will timely file a continuation statement. Similarly, the landlord should file a termination statement in the same recording office once the security interest is released or is no longer effective.

In the event that the tenant defaults, the landlord, pursuant to the UCC procedures, may take possession of the collateral without judicial process, if doing so will not involve a breach of the peace, and may then sell the collateral. The landlord may wish to include language in the lease which requires the tenant, upon an event of default, to gather the property for sale by

⁴ According to the revised Article 9, a financing statement may be authorized by (1) authentication, *i.e.*, signature; (2) the granting of an agricultural lien; or (3) the creditor's acquisition of the collateral itself. U.C.C. § 9-509 (2000).

landlord within a specific time frame. Further, the lease should provide that the tenant will agree to execute all additional documents, if any, to permit landlord to perfect and levy upon the lien. Once the collateral is sold, the proceeds must be applied to the expenses of the sale and attorneys' fees, if provided in the lease, satisfaction of the unpaid rent and finally, to the satisfaction of any subordinate debt. Any surplus is returned to the tenant and the tenant is responsible for any deficiency.

If the tenant is in bankruptcy, the landlord with a perfected secured interest is treated as any other secured creditor. That means, however, that the landlord may be barred by the automatic stay from seeking to enforce its security interest until such time as it is able to obtain relief from the stay.

While the Article 9 lien requires additional administrative work on the part of landlord, greater flexibility inherent in enforcing the lien and the ability to exercise immediate control over a tenant's collateral without the need for judicial action makes it quite attractive. Provided that the tenant is not in bankruptcy, the landlord may more quickly enforce its lien without judicial intervention and may afford more comprehensive lien rights as to a tenant's personal property, *i.e.*, the filing of a financing statement, in accordance with the UCC and lease provisions.

Conclusion

Both the statutory landlord's lien and a consensual lien created under Article 9 of the UCC are additional remedies available to a landlord in Maryland, Virginia or the District of Columbia to collect unpaid rent. Generally, landlords should seek to ensure that their lease documents are comprehensive and include broad lien rights, with clear-cut remedies pursuant to the UCC. Landlords should resist efforts to waive and/or subordinate such rights as the inclusion

of such liens may provide additional sources of recovery and/or may provide leverage in a default context. Clearly, landlords should exercise vigilance in administering their leases, identifying potential sources of financial recovery, including lien rights, and moving quickly to seek recovery against a tenant once a default occurs.

APPENDIX I

SUGGESTED LEASE LANGUAGE

In consideration of the mutual benefits arising under this Lease and in addition to any statutory lien for rent in Landlord's favor, Landlord (the secured party for purposes hereof) shall have and Tenant (the debtor for purposes hereof) hereby grants to Landlord, an express contract lien and a continuing security interest to secure the payment of all Rent due under the Lease from Tenant, upon all goods, wares, equipment, fixtures, furniture, inventory, accounts, contract rights, chattel paper and other personal property of Tenant (and any transferees or other occupants of the Premises) presently or hereafter situated on the Premises and upon all proceeds of any insurance which may accrue to Tenant by reason of damage or destruction of any such property. Except upon expiration of the Term where no default exists in the payment of Rent or other sums due from Tenant hereunder, and except for reasonable replacements from time to time, Tenant shall not remove any of Tenant's property from the Premises, other than pursuant to sale thereof in the regular course of its business, without the prior written consent of Landlord, and Landlord shall have the right and privilege, at its sole option and discretion, to take possession of all property of Tenant in the Premises, to store the same in the Premises, or to remove it therefrom and store it in such place as may be selected by Landlord, at Tenant's risk and expense, in accordance with such lien and of any rights of distraint it may possess against Tenant's property. In the event of a default under this Lease, Landlord shall have, in addition to any other remedies provided herein or by law, all rights and remedies under the Uniform Commercial Code of the state in which the Premises is located, including without limitation the right to sell the property described in this paragraph at public or private sale upon 10 days' notice to Tenant, which notice Tenant hereby agrees is adequate and reasonable. Within five (5) days after request by Landlord, Tenant hereby agrees to execute such other instruments necessary or desirable in Landlord's discretion to perfect or continue the security interest hereby created. Any statutory lien for rent is not hereby waived, the express contractual lien herein granted being in addition and supplementary thereto. Landlord and Tenant agree that this Lease and the security interest granted herein serve as a financing statement, and a copy or photographic or other reproduction of this paragraph of this Exhibit may be filed of record by Landlord and have the same force and effect as the original. Tenant warrants and represents that the collateral subject to the security interest granted herein is not purchased or used by Tenant for personal, family or household purposes. Tenant further warrants and represents to Landlord that the lien granted herein constitutes a first and superior lien and that Tenant will not allow the placing of any other lien upon any of the property described in this paragraph without the prior written consent of Landlord. The exercise of the foregoing remedy by Landlord shall not relieve or discharge Tenant from any deficiency owed to Landlord which Landlord has the right to enforce pursuant to any other provision of this Lease.