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Yes, Virginia, Leases for More than 5 Years Really Do Need to be in the Form of a Deed

Virginia Supreme Court allows Early Termination of Lease not in Compliance with Statute of Conveyances

By Diane Shapiro Richer and Blake L. Daniels

Tenants (as well as landlords) seeking an early exit from a Virginia lease of more than 5 years have been given an assist by the Virginia Supreme Court in a recent case causing consternation among commercial real property owners and their mortgage lenders. The decision in *The Game Place, L.L.C. v. Fredericksburg 35, LLC*, 813 S.E.2d 312 (Va. 2018), allowed a tenant that wished to get out of its 15-year lease to terminate early on the basis of form over substance. Notwithstanding the clear intent of the parties to create a lease of 15 years, the failure of the lease to be in the form of a deed, as prescribed by the Virginia Statute of Conveyances, rendered it a month-to-month lease, thus, terminable by the tenant when the lease no longer served its business needs.

While those familiar with Virginia leasing practice have long known to draft Virginia leases of more than 5 years in the form of a deed – typically accomplished by calling it a *Deed of Lease* and reciting that it is a deed of lease within the body of the agreement – the *Game Place* case provides new guidance as to the potentially serious consequences of failing to comply with this formality. While this is important legal news to anyone with an interest in leased real property in Virginia, it may be particularly noteworthy for those acquiring, or providing mortgage financing secured by, Virginia commercial real estate.

Deed of Lease and Seal Requirements in Virginia

First, a quick primer on applicable Virginia law. The Statute of Conveyances, VA Code Ann. § 55-2, requires conveyances of estates in lands of more than 5 years to be by deed (or will). Leases of more than 5 years have been held to fall within this requirement.¹ So, what does it mean to be in the form of a deed? Common law requires deeds to have certain attributes, which historically included being sealed with wax.² But the seal requirement has been relaxed by VA Code Ann. § 11-3, which prescribes seal substitutes:

¹ See *Humble Oil & Refining Co. v. Cox*, 148 S.E.2d 756, 760 (Va. 1966).

² See *Smith v. Plaster*, 144 S.E. 417, 419 (Va. 1928).



(1) a scroll by way of seal, (2) an imprint or stamp of an official seal, (3) use of the words “this deed,” “this indenture,” or other words importing or recognizing a sealed instrument within the text; or (4) acknowledgment before a notary, provided the document complies with VA Code Ann. § 55-48 (which sets out minimal requirements for the form of a deed, including use of the words “this deed”). Common practice today is to call Virginia leases *Deed of Lease* and otherwise comply with the requisites of seal substitute (3) above.

The Court’s Decision

The lease in the *Game Place* case met none of these formal requirements. In *Game Place*, Fredericksburg 35, LLC, as landlord, brought an action against Game Place, L.L.C., its tenant, seeking unpaid rent after the retail tenant encountered business difficulties, vacated its premises, and attempted to terminate its lease before the expiration of the 15-year term. At trial, the tenant contended that the lease, which did not include a seal or any of the seal substitutes available under VA Code Ann. §11-3, was not properly in the form of a deed as required by the Statute of Conveyances, and, therefore, was unenforceable. The Circuit Court of the City of Fredericksburg rejected the tenant’s arguments, looking to the lease’s substance over its form, and finding that the lease was enforceable.³ The tenant appealed.

On appeal, the Virginia Supreme Court overruled the Circuit Court, giving great deference to the form requirements of the Statute of Conveyances and related statutes.⁴ The Court determined that failure to comply with the Statute of Conveyances, by incorporating either the common law seal requirement or any of the statutory seal substitutes, rendered the lease unenforceable as a lease of more than 5 years. Instead, the lease was found to be a month-to-month lease which was terminated when the tenant vacated the rental property and paid its rental obligations through its last month of occupancy.⁵

³ The Fredericksburg Circuit Court held that despite failure of the lease to include the common law requirement of a seal or any of the statutory substitutes, the lease was a 17-page document and could just as easily be titled “Deed of Lease” or “Lease Indenture.” See *Game Place, L.L.C.*, 813 S.E.2d at 313.

⁴ The Virginia Supreme Court reasoned that “the relative ease with which a party can comply with a statute is hardly a basis for excusing him,” and further, that favoring substance over form is a slippery slope in which “courts would simply replace categorical, predictable, bright lines with ad hoc, unpredictable, blurry lines.” See *Game Place, L.L.C.*, 813 S.E.2d at 318. The Court further reasoned that the General Assembly had specifically modified the common law in a number of ways without abolishing the seal requirement. *Id.* at 319.

⁵ The Court relied on precedent established in *Granva Corp. v. Heyder*, 139 S.E.2d 77, 81 (Va. 1964), in which the court adopted the New York approach that even where a tenant takes possession under a defective instrument, a tenancy is still created. See *Game Place, L.L.C.*, 813 S.E.2d at 321. In such cases, the law imposes a new lease on the parties which incorporates the terms of the original agreement so far as they are not in conflict with statutes. *Id.* Subsequently, the court looked towards the period of rental payments, which were received on a monthly basis, to interpret the new tenancy as a month-to-month lease. *Id.*

Takeaways

Unless and until the Virginia General Assembly takes corrective legislative action on this issue, landlords, tenants, buyers, and mortgage lenders with an interest in Virginia leases of more than 5 years are advised to take note of this Virginia Supreme Court decision.

So, what are best practices, in the wake of *Game Place*?

New Leases: Leases of more than 5 years should satisfy at least one of the seal requirements of VA Code Ann. § 11-3 in order to comply with the Statute of Conveyances. We recommend the following: (1) title the lease “Deed of Lease”; (2) recite in the opening text of the document “[T]his Deed of Lease,” and (3) recite in the closing that the parties “have executed this Deed of Lease, intending the same to be an instrument under seal,” while also typing or printing “SEAL” beside each signature. Notarizing the Deed of Lease is not necessary, but may serve as an alternate means of compliance.

Existing Owners/Secured Lenders – Review Leases for Compliance. Those who already own, or have provided mortgage financing secured by, Virginia real estate subject to leases of more than 5 years may want to review leases for compliance with the Statute of Conveyances and related statutory requirements, and consider possible corrective action for leases that may be vulnerable.

New Acquisitions and Mortgage Loans – Checklist/Due Diligence. When buying or financing Virginia real estate, include as part of the lease due diligence: (1) analyze whether leases of more than 5 years comply with Virginia law, as interpreted by the *Game Place* case, and, if not, (2) consider amending any non-compliant leases as a condition to closing.

Any decision to pursue correction of a potentially vulnerable lease, of course, should be considered on a case-by-case basis, taking into account the form of the particular lease, timing/risk/leverage factors, and other legal and strategic considerations. For further information, or assistance in reviewing Virginia leases for compliance with the law discussed in this Alert, please contact **Diane Shapiro Richer** or **Blake Daniels**.

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