A LOOK AT SOME LEGAL IMPLICATIONS OF **COVID-19 ON HEALTHCARE REAL ESTATE**

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Conventional wisdom has held that the healthcare real estate industry is generally recession resistant. While that has historically been the case, the conventional wisdom did not account for a recession caused solely by a public health crisis due to a global pandemic. While the long-term effects of the COVID-19 pandemic on the healthcare real estate market remain to be seen, the short-term effects of the pandemic are already being felt throughout the industry. While some of the legal and economic issues facing healthcare real estate owners and tenants mirror the issues facing owners and tenants of other classes of commercial real estate, other issues are wholly unique to the healthcare industry. This article addresses the issues that owners and tenants alike are addressing in real time as the implications of this unprecedented event continue to unfold.

Rent and/or Mortgage Relief

Landlords have begun to be flooded with requests from tenants for rent relief, ranging from a rent deferral or abatement for a period of time, to a permanent reduction in the rent to be paid under the lease. While the need for such relief may be obvious for hospitality, restaurant and most retail tenants, it is not as readily apparent for healthcare tenants. Nevertheless, some healthcare tenants are undoubtedly feeling the effects of this public health emergency. For example, some healthcare providers are seeing their revenues being severely impacted by the shelter in place restrictions being implemented by the federal, state and local governments as a result of the COVID-19 public health emergency, because these restrictions are preventing them from providing their core services, such as, for example, performing elective surgeries. Depending on the duration of the restrictions preventing them from providing these services, this could certainly impact their ability to stay current on their contractual rent obligations. However, other healthcare tenants are not impacted by the pandemic in the same way and should certainly be able to continue to satisfy their lease obligations. How is a landlord to determine whether rent relief is appropriate?

First, the landlord should request detailed information from each of its tenants that are requesting relief regarding the tenant's finances and current caseload to ensure that the tenant is truly in need of relief. **A proposed checklist for landlords to provide to tenants can be found here.** In addition, prior to entering into rent relief discussions with a tenant, the parties should consider executing a pre-negotiation letter to preserve each party's rights, claims and defenses during such discussions so that no party waives or relinquishes any rights or incurs any obligations unless and until a further written agreement is executed. This protects both the landlord and the tenant and encourages honest and frank discussions between the parties.

Once it is determined that some form of rent relief is merited, the landlord must work closely with its lender and equity/capital partners to ensure that no lease amendment triggers any defaults under its mortgage loan or other financing arrangements. If the rent relief being considered by the landlord (either to the particular tenant in question or in the aggregate to all of the tenants in the building) would cause the breach of a financial or other covenant under the landlord's loan, then a modification of the loan should be negotiated simultaneously with the lease amendment. Of course, if the aggregate effect of the reduced rent results in an inability for the landlord to pay its mortgage payment, then the landlord should attempt to have the loan modification address a reduction in (or waiver of) mortgage payments for a period of time as well. Early indications have shown lenders to be generally agreeable to short-term waivers of covenant defaults and potential

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deferral of mortgage payments resulting from tenant-driven COVID-19 issues. It remains to be seen how long this general mood of cooperation continues.

Regulatory Considerations with Rent Relief

When considering if, or how, to provide rent relief, the primary healthcare fraud and abuse laws must still be considered, namely, the federal Anti-Kickback Statute ("*AKS*") and the Stark Law. In general, Stark and AKS are more of an issue when dealing with hospital systems or when the landlord entity is owned by one or more physicians, but Stark and AKS can be implicated in a number of other circumstances, and both laws contain exceptions or safe harbors for space leases that healthcare landlords are intimately familiar with. The Centers for Medicare & Medicaid Services ("*CMS*") has recently provided some relief through blanket waivers under the Stark Law related to COVID-19, which is within the Secretary of Health & Human Services' discretion during a public health emergency. In addition, the Office of Inspector General for Health & Human Services ("*OIG*") has announced that it will exercise its enforcement discretion not to impose administrative sanctions under the AKS for many payments covered by the Stark Law blanket waivers published last week.

In the most general terms, the AKS prohibits any offer or exchange of a benefit that could be construed to induce or reward referrals or other business involving items or services payable by federal healthcare programs. Since the AKS is an intent-based law, strict compliance with a safe harbor is not necessary to demonstrate compliance. Instead, parties must be able to demonstrate to the OIG that the arrangement does not violate the AKS. This means that parties must document the purposes for any type of rent relief granted as a result of the COVID-19 public health emergency. This should include the underlying problem that has resulted in the need for rent relief, as well as a policy or process for what the parties will do with the remaining rent obligations under the lease when the public emergency ends. The parties should also take reasonable efforts to analyze the impact of any rent relief on the fair market value nature of the arrangement. Absent a clear intent to defraud, OIG enforcement against rent relief efforts is unlikely; however, the burden is on the parties to the lease to demonstrate how relief of any obligations under the lease, rent or otherwise, remains in compliance with AKS. Appropriate documentation maintained by the parties is the key to such demonstration.

The Stark Law is more limited in scope than the AKS. Generally, the Stark Law prohibits a physician from making referrals for certain designated health services ("*DHS*") payable by Medicare to an entity that the physician (or an immediate family member of the physician) has a financial relationship with, unless a Stark Law exception applies. The exception for space leases is the exception healthcare real estate landlord will primarily be working in. As noted above, CMS issued blanket waivers (https://www.cms.gov/files/document/covid-19-blanket-waivers-section-1877g.pdf) on March 30, 2020, in response to the COVID-19 public health emergency. These blanket waivers apply nationwide and are intended to ensure the availability of healthcare services for Medicare and Medicaid beneficiaries and to allow healthcare providers to receive payment for certain claims that would otherwise violate the Stark Law if the waivers were not in place. CMS included examples such as payment of less than fair market value rent, remuneration to a physician tenant in the form of rent abatement, deferral or forgiveness that could result in rent that was no longer fair market value, or remuneration resulting from a loan by a DHS entity to a physician tenant to pay rent that includes a below-market interest rate or terms that are unavailable from a commercial lender that does not receive referrals from the physician. While included as possibly protected arrangements, parties must analyze and structure the arrangements as outlined in the waivers.

To take advantage of the waivers (which does not require any request to CMS), the arrangement must be for a valid "COVID-19 Purpose," which is broadly defined to encompass a variety of situations resulting from the COVID-19 public health emergency, so the waivers are not unlimited. For example, in the case of lease arrangements, the parties will need to demonstrate how the relief—deferral, reduction, or overall abatement—is appropriate as relief because of COVID-19. It is unlikely that abatement of rent for the remainder of a lease, as opposed to limited deferral or reduction, is appropriate relief. Thus, the parties should document the reasons for the arrangement, the specific terms of the arrangement, and how the arrangement qualifies for the waivers. Best practices include (1) establishing a policy or protocol to ensure that all requests are evaluated on the merits of the particular request and that financial assistance is not tied to the value or volume of referrals or other business between the parties; (2) development of a business case, including documentation that without assistance the tenant would no longer be financially viable; and, finally, (3) obtaining a third-party opinion on the commercial reasonableness, as warranted by the facts and circumstances.

Finally, the parties must remember that the blanket waivers will not last forever. They are retroactive to March 1, 2020, and absent extension or grandfathering by CMS, the blanket waivers will remain in place only as long as the public health emergency lasts. When the public health emergency declaration expires, the parties to an arrangement will need to be prepared to terminate the non-compliant arrangement or to restructure it to comply with an appropriate Stark Law exception.

Force Majeure

A big issue in legal circles over the past couple of weeks has been the applicability of force majeure clauses to the COVID-19 pandemic and resulting public health emergency. Typically, a force majeure clause temporarily excuses a party to a contract from performance when circumstances beyond the reasonable control of such party prevent it from timely performing. While the COVID-19 pandemic would qualify as a force majeure event under many force majeure clauses, such clauses often expressly exclude the inability to pay from the application of the force majeure clause. So, while the force majeure clause in the applicable documents may allow for a delay in the performance of an obligation, such as, for instance, the obligation to finish construction by a date certain, it likely will not excuse a party from paying its financial obligations, such as a rent payment or a mortgage payment. Many force majeure clauses require written notice by the party claiming a delay due to force majeure. When drafting such a notice, landlords must be mindful of other loan provisions that may unintentionally be implicated if the notice is not phrased appropriately (such as any material adverse change provision, or admitting in writing the party's inability to pay its debts as they are due – which is also usually a full recourse carve out for the guarantor). In any event,

it is advisable to have your attorney review the applicable documents to determine the scope of the force majeure clause and the procedures which must be followed to avail yourself of its benefits.

Impossibility of Performance

Another doctrine of the law being closely monitored by attorneys is the doctrine of impossibility of performance, which provides that one party may be excused from performance under a contract due to circumstances that render its ability to perform impossible. For example, if a tenant of an ambulatory surgery center is rendered incapable of operating the leased premises for the stated use in the lease (i.e., performing elective surgeries) because of government regulations restricting such surgeries as a result of the current crisis, is the tenant excused from paying rent for the duration of the crisis? The answer will likely vary from state to state and an experienced attorney should be consulted if you are confronted with this issue.

Conclusion

Like the rest of the world, the healthcare real estate industry finds itself in uncharted waters while grappling with the myriad issues created by the COVID-19 pandemic. This crisis will undoubtedly challenge even the most experienced real estate professional. Now, more than ever, it is important for healthcare real estate professionals to have experienced legal counsel who are well equipped to handle both the real estate and the healthcare regulatory issues that the COVID-19 pandemic presents.

About the author: Over the past 20+ years, Andy Dow has developed a reputation as one of the preeminent healthcare real estate attorneys in the United States. Clients from across the country seek his counsel and advice on a variety of transactions and strategies related to the healthcare real estate sector. Whether representing a health system in a monetization transaction or a healthcare investor in a portfolio acquisition, he brings a distinctive blend of real estate excellence and healthcare industry acumen to each engagement. As the Chair of Winstead's Real Estate Industry Group and its Healthcare Real Estate Practice Group, Andy leads a team of seasoned healthcare real estate professionals with an impressive stable of clients, including industry leading healthcare REITs, private equity investors, developers, operators, hospital systems, physician groups and lenders.