



Legislation Text

File #: CB 120643, Version: 3

CITY OF SEATTLE

ORDINANCE _____

COUNCIL BILL _____

AN ORDINANCE relating to commercial tenancies; establishing limits on the maximum personal guaranty that may be included in or as a condition of commercial leases; and establishing limits on the value of a commercial lease's required security deposit and/or letters of credit; and adding a new Chapter 6.104 to the Seattle Municipal Code.

WHEREAS, the Washington Constitution provides in Article XI, Section 11 that “[a]ny city, county, town or township may make and enforce within its limits all such local police, sanitary and other regulations as are not in conflict with general laws”; and

WHEREAS, it is the goal of the City's Commercial Affordability Initiative, as a component element of the Equitable Development Initiative, to create new policies and steps to support commercial affordability to address the rising cost of commercial space for small businesses, which are key anchors for vulnerable communities; and

WHEREAS, owners of small businesses are less likely than owners of large businesses to own the properties from which those businesses are conducted, thus any requirements that affect tenant commercial businesses will impact small businesses to a greater extent than they will impact large businesses; and

WHEREAS, the Office of Economic Development's 2023 “Future of the Seattle Economy” report reflects a community-informed investment agenda that will promote inclusive economic growth, especially for communities that have systematically been excluded from such opportunities, and its findings identified the need to help Women and Minority Owned Business Enterprises (WMBE) and Small Business Enterprises (SBEs) avoid predatory practices that prevent them from building wealth through their

businesses in an already inequitable system while enabling them to grow and remain in their communities; and

WHEREAS, standard commercial lease agreements generally require a personal guaranty as a condition or an element of the lease agreement, which makes an individual, usually but not always the business owner, personally liable to the lessor for specified expenses during a specified time period in the event that the business cannot pay; and

WHEREAS, this personal liability persists even if the business ceases to operate before the conclusion of the specified time period; and

WHEREAS, this personal liability typically includes rent and utility costs for a period of up to ten years; and

WHEREAS, commercial leases often also require a security deposit as a condition or element of the lease agreement, which requires that a business or an individual, usually but not always the business owner, make a payment to the lessor to fund the costs of addressing any property damages incurred by the tenant during the lease term, and/or other costs as described in the lease; and

WHEREAS, commercial leases may also or alternatively require a letter or letters of credit as a condition or element of the lease agreement. Letters of credit support the mitigation of risk for a lessor if a tenant were to fail to pay rent or other financial obligations under the lease either by (a) issuing a line of credit to an individual, usually but not always the business owner, or to a business, or (b) providing access to money held at a bank by an individual, usually but not always the business owner, or by a business for those financial obligations; and

WHEREAS, an individual who must secure letters of credit, execute a personal guaranty, and/or provide a security deposit as a condition or element of a commercial lease must commit financial resources and/or credit capacity to their maintenance rather than being able to invest those resources and capacity in positive business opportunities, and the ongoing annual charges associated with maintaining letters of credit impose an additional financial burden; and

WHEREAS, the aggregate liability of a personal guaranty, letters of credit, and/or a security deposit imposes a burden on the individual who is responsible for bearing it, usually but not always the business owner, either to possess, have access to, or gain access to a certain level of financial resources, with this burden being supplemental to other business startup or relocation costs, such as custom buildouts, permitting and inspection fees, inventory acquisition, marketing, and those associated with the training and onboarding of personnel; and

WHEREAS, the current absence of regulations limiting this aggregate liability that commercial tenants must assume has been reported to inhibit the establishment of new businesses, particularly when would-be entrepreneurs do not already possess or have access to ample financial resources to start new businesses; and

WHEREAS, in order to limit the aggregate liability that commercial tenants must assume, it is necessary to limit both the personal-guaranty liability and the letter-of-credit requirements that may be included as a condition or element of a commercial lease; and

WHEREAS, most small businesses will not become profitable for two to three years, during which time the owners of those businesses may have to spend from their personal assets and/or on credit to sustain those businesses; and

WHEREAS, lessors of commercial premises assume risk and opportunity costs in leasing or renting a commercial property to a business; and

WHEREAS, it is in the public's interest to foster local businesses and support their contributions to neighborhood vibrancy; NOW, THEREFORE,

BE IT ORDAINED BY THE CITY OF SEATTLE AS FOLLOWS:

Section 1. The City Council finds and declares that:

A. In the exercise of The City of Seattle's (City's) police powers, the City is granted authority to pass regulations designed to protect and promote public health, safety, and welfare.

B. This ordinance protects and promotes public health, safety, and welfare by establishing limits on both the maximum personal guaranty that may be included in or as a condition of commercial leases and the value of a commercial lease's required security deposit and/or letters of credit.

C. Small businesses are vital to the character and community fabric of Seattle, reflecting and nurturing the cultural diversity of the community and serving as important engines of the local economy by providing jobs and operating as commercial anchors in neighborhoods across Seattle.

D. Many small business owners do not own the property from which they conduct their business, requiring them to execute a lease with a lessor.

E. It is typical for lessors to require a personal guaranty as a condition or element of a commercial lease. A personal guaranty commits an individual, who is usually but not always the small business owner, to the payment of certain costs associated with the leased commercial property, such as rent and utilities, for a prescribed length of time, and the obligation to pay these costs persists even if the business ceases to operate.

F. As a condition or element of a commercial lease some lessors require tenants to provide a security deposit, which is a non-rent payment made by a business or an individual, who is usually but not always the business owner, that the lessor retains to fund the costs of addressing any property damages incurred by the tenant during the lease term.

G. As a condition or element of a commercial lease some lessors require tenants to obtain a letter or letters of credit, which is a guarantee from a bank or other institution to pay rent or other financial obligations under the commercial lease in the event that the tenant fails to pay, and which is secured either by the bank holding the amount of assets to be guaranteed for the duration of the instrument or by issuing a line of credit. The letter or letters of credit may be obtained by an individual, who is usually but not always the business owner, or by a business.

H. Personal-guaranty, security-deposit, and letter-of-credit requirements as conditions or elements of a commercial lease agreement impose a financial burden on the business and/or individual, usually the business

owner, who are subject to them. This burden is incremental to the various other costs associated with starting or maintaining a small business and it may disincentivize individuals from starting new small businesses, particularly when they have fewer personal assets.

I. Twenty percent of small businesses fail in their first year and approximately half of small businesses fail within the first five years of operation. Among the operators of these businesses, the second most commonly cited reason for failure is lack of capital.

J. Studies have found that where commitments of personal capital assets are prerequisites for small businesses to obtain credit, the small business owner's existing wealth largely determines whether the business survives; that individuals with more assets are more likely to be self-employed; and that would-be small business owners are more likely to obtain external funding when they have higher levels of education and net worth.

K. Access to capital for small business owners also generally requires a personal guaranty, in addition to any such commitment made as a requirement for a commercial lease agreement. The vast majority of small business loans, including those funded through the U.S. Small Business Association, require a personal guaranty that applies to anyone who owns 20 percent or more of the business.

L. It is in the public's interest to take actions consistent with the goal of expanding and sustaining small business ownership, reducing barriers to access to capital for those businesses, and sustaining a diverse and vibrant workforce.

M. It is in the public's interest to take actions consistent with the goals of expanding economic mobility for those who wish to start a business in Seattle and promoting inclusive economic growth, especially for communities that have systematically been excluded from such opportunities.

N. Analysis of data collected by the Small Business Administration Office of Advocacy showed that 13 percent of surveyed incorporated small businesses had decided not to undertake a positive investment opportunity because the lender required a personal guaranty to obtain a loan for the project and 11 percent of

them had been denied a loan because of their inability to meet the lender's personal guaranty requirements.

O. Research for a 2016 doctoral dissertation analyzing personal guaranties across five types of loans found that, of respondents who had not met requirements for a personal guaranty or who declined to provide one, 53 percent had to seek funding elsewhere, 36 percent could not pursue products or services, 28 percent had to forgo an expansion project, 27 percent could not hire additional staff, and 27 percent had to lay off staff.

P. Nationally, 70 percent of small businesses have outstanding loan debt. The average amount of a small business's total debt is \$195,000. This debt liability is in addition to any liability associated with a personal guaranty on a commercial lease.

Q. To the extent that a business owner incurs less personal-guaranty liability, commits fewer assets to a security deposit, and/or uses less credit capacity to maintain a letter or letters of credit in or as a condition of a commercial lease, that business owner will have greater flexibility to participate in positive investment opportunities for their business.

R. Establishing a framework that limits the personal-guaranty liability and security deposit and/or letter-of-credit liability that may be included in or as a condition of commercial leases is consistent with City's Commercial Affordability Initiative.

S. The harm that business owners have experienced due to the current lack of limitations on personal-guaranty liability and security deposit and/or letter-of-credit liability is based on the standards of leases for commercially owned and/or managed properties. Business owners report that standard lease terms for properties that are owned and/or managed by Federal, state, or local governments, or by Tribal governments, do not cause this harm.

T. It is in the public's interest to limit the exposure of individuals, who are usually but not always the business owners, to personal-guaranty liability in order to help these businesses survive, preserve the livelihoods of those they employ, and continue contributing to the vitality of the community.

U. It is in the public's interest to limit the value of the security deposit and the letters of credit that

businesses or individuals, who are usually but not always the business owners, may be subject to providing in order to help these businesses survive, preserve the livelihoods of those they employ, and continue contributing to the vitality of the community.

V. This ordinance protects and promotes public health, safety, and welfare by limiting certain financial obligations to which tenant commercial retail businesses are subject, which will have the effect of reducing barriers to economic participation for those business owners and their future generations.

Section 2. A new Chapter 6.104 of the Seattle Municipal Code is added to Subtitle III of Title 6 as follows:

Chapter 6.104 COMMERCIAL LEASES AND RENTAL AGREEMENTS

6.104.010 Scope

This Chapter 6.104 applies to all lessors of commercial property located within Seattle city limits. This Chapter 6.104 is an exercise of the City’s police power to regulate commercial contracts.

6.104.020 Definitions

For the purposes of this Chapter 6.104:

“Base rent” means the agreed-upon cost that a commercial tenant regularly pays to a lessor for the right to possess and use a property.

“Commercial property” means real estate that is intended to generate a profit and is used for: commercial or retail activities other than (a) rental as residence or for lodging; as office space; as research and development laboratory space; or as a medical practice, clinic, or dispensary; and (b) farming or cultivation.

“Commercial lease” means a lease that has commercial property as its subject.

“Department” means the Department of Finance and Administrative Services, or successor entity.

“Director” means the Director of Finance and Administrative Services, or successor entity, or the Director’s designee.

“Lease” means any agreement between a lessor and a tenant that establishes or modifies the terms,

conditions, rules, regulations, or any other provisions concerning the use and occupancy of a commercial property.

“Lessor” means the owner, or agent of the owner, of a commercial property that is leased to a business entity or person, called the tenant. For the purposes of this Chapter 6.104, “lessor” does not include:

1. The United States government;
2. The government of any Indigenous Tribe;
3. The State of Washington, including any office, department, agency, authority, institution, society, or other body of the state, including the legislature and the judiciary; or
4. Any county or local government.

“Letter of credit” means any guarantee from a bank or other institution to pay rent or other financial obligations associated with the assumption of a commercial lease if the tenant fails to pay, and which is secured either by the bank or other institution holding the amount of assets so guaranteed for the duration of the instrument or by the issuance of a line of credit. Letters of credit may be issued by a bank or other institution on behalf of an individual, who is usually but not always the business owner, or a business.

“Personal guaranty” means a specific and time-limited contractual agreement either as an element of a commercial lease or rental agreement or as a separate, freestanding agreement which establishes an individual’s agreement to pay, with their own money, certain expenses that a commercial tenant owes the lessor under the terms of the lease if the tenant is unable to pay. These expenses typically include base rent and tenant improvement costs and may include taxes, insurance, common area maintenance, and utility charges, and they may include additional expenses.

“Security deposit” means a payment other than base rent or additional rent that a tenant makes to a lessor prior to the commencement of the lease term, which the lessor retains as a security for the duration of the lease term for performance of the tenant's obligations under their lease agreement and/or to fund the cost of addressing any property damages incurred by the tenant during the lease term. This payment may be made by

an individual, who is usually but not always the business owner, or a business.

“Tenant” means a business entity or person who is entitled to occupy or possess commercial real estate that belongs to another business entity or person, in accordance with the terms of a lease agreement.

“Tenant improvement allowance” means a pre-negotiated sum of money that a lessor may optionally make available to a commercial tenant to support the making of tenant improvements to a leased space.

“Tenant improvement costs borne by the tenant” means costs that support the making of improvements to a leased space that are borne by that space’s tenant rather than by its lessor. If a tenant improvement allowance is insufficient to fund the full configuration needs of a tenant, the incremental costs of the configuration are considered tenant improvement costs borne by the tenant.

“Tenant improvements” means customized alterations to a leased commercial space as mutually agreed to as a condition or an element of a lease agreement, in order to configure the space for the needs of that particular tenant, which may include changes to walls, floors, ceilings, and lighting, among other construction and design elements. Tenant improvements are exclusive of the following lessor-provided items and features of a leased commercial space: heating, ventilation, and air conditioning units and ductwork; exhaust fans, hoods, and fireproofed ductwork approved by a fire marshal to allow for commercial kitchen exhaust; sprinkler and fire alarm/fire suppression systems, electrical panels and main electrical line connections, main plumbing and sewage line connections, bathrooms, and any other base building systems that are necessary to support commercial business or retail activity.

6.104.030 General provisions

All lessors of commercial premises involved in promoting or executing lease agreements for commercial properties within Seattle shall comply with the following:

A. For any new lease executed after the effective date of this ordinance, the total value of any required security deposit and/or letters of credit shall not exceed the total value of the first month and last month of base rent.

B. For any new lease executed after the effective date of this ordinance, the maximum personal guaranty that may be included in a commercial lease or in a separate agreement upon which a commercial lease is conditioned is the sum of (1) the first two years of base rent payments and (2) the total cost of tenant improvements made to the leased space, inclusive of tenant improvement allowance, if any; and exclusive of tenant improvement costs borne by the tenant, if any.

6.104.040 Summary of provisions in commercial leases that limit personal guaranties and the value of security deposits and/or letters of credit

A. The Director shall, as soon as is practicable, and as the Director shall deem necessary from time to time, prepare a summary of this Chapter 6.104 and any other applicable regulations that pertain to commercial leases.

B. The Department shall make the summary described in subsection 6.104.040.A available to lessors and to commercial tenants at no cost.

C. Nothing in the summary described in subsection 6.104.040.A shall be construed as binding on or affecting any judicial determination of the rights and responsibilities of landlords and tenants, nor is the Department liable for any misstatement or misinterpretation of the applicable laws.

6.104.050 Distribution of summary by lessor required

A. A copy of the summary described in subsection 6.104.040.A shall be provided by the lessor of commercial property to any commercial tenant or prospective commercial tenant when such new property lease is offered.

B. Lessors shall, within 90 days after the Director prepares the summary described in subsection 6.104.040.A, distribute the summary to their existing commercial tenants.

6.104.060 Enforcement and rulemaking powers and duties

A. The Director shall adopt rules pursuant to Chapter 3.02 to implement the provisions of this Chapter 6.104. The Director may promulgate, revise, or rescind rules deemed necessary, appropriate, or convenient to

administer the provisions of this Chapter 6.104, providing affected entities with due process of law and in conformity with the intent and purpose of this Chapter 6.104.

B. The Director is authorized to investigate any potential violation of this Chapter 6.104.

C. Any violations of this Chapter 6.104 shall be enforced under the citation provisions set forth in Section 6.104.080.

6.104.070 Violations

It is a violation of this Chapter 6.104 for any commercial lessor to:

A. Enter into, or require another party to enter into, any commercial lease in which the total value of any required security deposit and/or letters of credit exceeds the total value of the first month and last month of base rent.

B. Enter into, or require another party to enter into, any commercial lease agreement that includes or is conditional upon personal guaranty that exceeds the sum of: (1) the first two years of base rent payments; and (2) the total cost of tenant improvements made to the leased space, inclusive of tenant improvement allowance, if any; and exclusive of tenant improvement costs borne by the tenant, if any.

6.104.080 Citation

A. If, after investigation, the Director determines that a lessor has committed a violation of this Chapter 6.104, the Director may issue a citation to the person responsible for the violation. The citation shall include the following information:

1. The name and address of the responsible person to whom the citation is issued;
2. The complete address of the commercial property subject to the commercial lease violation;
3. A separate statement of each violation;
4. The date of the violation;
5. A statement that the person cited must respond to the citation within 15 business days after the

date of service;

6. A space for entry of the applicable penalty;
7. A statement that the response must be sent to the Hearing Examiner and received not later than 5 p.m. on the day the response is due;
8. The name, address, and phone number of the Hearing Examiner where the citation is to filed;
9. A statement that the citation represents a determination that a violation has been committed by the responsible person named in the citation and that the determination shall be final unless contested as provided in subsection 6.104.080.C; and
10. A certified statement of the inspector issuing the citation, authorized by RCW 5.50.050, setting forth facts supporting issuance of the citation.

B. The citation may be served in person or sent by first class mail, addressed to the last known address of such person(s). Service shall be complete at the time of personal service, or, if mailed, three days after the date of mailing. If a citation sent by first class mail is returned as undeliverable, service may be made by posting the citation at a conspicuous place on the property.

C. Response to citations

1. A citation must be responded to in one of the following ways:
 - a. Payment of the monetary penalty specified in the citation, in which case the record shall show a finding that the person committed the violation; or
 - b. A written request for a mitigation hearing to explain the circumstances surrounding the commission of the violation and providing an address to which notice of such hearing may be sent; or
 - c. A written request for a contested hearing specifying the reasons(s) why the cited violation did not occur or why the person cited is not responsible for the violation, and providing an address to which notice of such hearing may be sent.
2. A response to a citation must be received by the Office of the Hearing Examiner no later than 15 business days after the date the citation is served.

D. If the Office of the Hearing Examiner does not receive a response within 15 business days of service of the citation, the Hearing Examiner shall enter an order finding that the person cited committed the violation stated in the citation, and assessing the penalty specified in the citation.

E. Hearings

1. Mitigation hearings

a. If a mitigation hearing is requested, the mitigation hearing shall be held within 30 days after written response to the citation requesting such hearing is requested by the Hearing Examiner. Notice of the time, place, and date of the hearing shall be sent to the address specified in the request for hearing not less than ten days prior to the start of the hearing.

b. The Hearing Examiner shall hold an informal hearing that shall not be governed by the Rules of Evidence. The person cited may present witnesses, but witnesses may not be compelled to attend. A representative of the Department may also be present and may present additional information, but attendance by a representative of the Department is not required.

c. The Hearing Examiner shall determine whether the cited person's explanation justifies reduction of the monetary penalty; however, the monetary penalty may not be reduced unless the Department affirms or certifies that the violation has been corrected prior to the mitigation hearing. Factors that may be considered in whether to reduce the penalty include whether the violation was caused by the act, neglect, or abuse of another; or whether correction of the violation was commenced promptly prior to citation but that full compliance was prevented by a condition or circumstance beyond the control of the person cited.

2. Contested hearing

a. If a person requests a contested hearing, the hearing shall be held within 60 days after the written response to the citation requesting such hearing is received.

b. Contested hearings shall be conducted pursuant to the procedures for hearing contested cases contained in Section 3.02.090 the rules adopted by the Hearing Examiner for hearing contested

cases, except as modified by this subsection 6.104.080.E.2 The issues heard at the hearing shall be limited to those that were raised in writing in response to the citation and that are within the jurisdiction of the Hearing Examiner. The Hearing Examiner may issue subpoenas for the attendance of witnesses and the production of documents.

c. No citation shall be deemed insufficient for failure to contain a detailed statement of facts constituting the specific violation which the person cited is alleged to have committed or by reason of defects or imperfections, provided such lack of detail or defects or imperfections do not prejudice substantial rights of the person cited.

d. A citation may be amended prior to the conclusion of the hearing to conform to the evidence presented if substantial rights of the person cited are not thereby prejudiced.

e. The certified statement or declaration authorized by RCW 5.50.050 shall be prima facie evidence that a violation occurred and that the person cited is responsible. The certified statement or declaration authorized under RCW 5.50.050 and any other evidence accompanying the report shall be admissible without further evidentiary foundation. The person cited may rebut the Department's evidence and establish that the cited violation(s) did not occur or that the person contesting the citation is not responsible for the violation.

f. If the citation is sustained at the hearing, the Hearing Examiner shall enter an order finding that the person cited committed the violation. If the violation remains uncorrected, the Hearing Examiner shall impose the applicable penalty. The Hearing Examiner may reduce the monetary penalty in accordance with the mitigation provision in subsection 6.104.080.E.1 if the violation has been corrected. If the Hearing Examiner determines that the violation did not occur, the Hearing Examiner shall enter an order dismissing the citation.

g. The Hearing Examiner's decision is the final decision of the City.

3. Failure to appear for a requested hearing will result in an order being entered finding that the

person cited committed the violation stated in the citation and assessing the penalty specified in the citation. For good cause shown and upon terms the Hearing Examiner deems just, the Hearing Examiner may set aside an order entered upon a failure to appear.

F. Citation penalties

1. The following penalties shall be assessed for any violations of this Chapter 6.104:

- a. \$500 for the first violation; and
- b. \$1000 for each subsequent violation within a five-year period.

2. The Director may, in an exercise of discretion, issue a warning to the person responsible for the violation if that person has not been previously warned or cited for violating this Chapter 6.104.

3. Each party responsible for a violation can be assessed a separate penalty for that violation.

4. If the person cited fails to pay a penalty imposed pursuant to this Section 6.104.080, the penalty may be referred to a collection agency. The cost to the City for the collection services will be assessed as costs, at the rate agreed to between the City and the collection agency, and added to the penalty.

Alternatively, the City may pursue collection in any other manner allowed by law.

5. Each day a person commits a violation under Section 6.104.070 may be considered a separate violation for which a civil citation may be issued.

6.104.090 Private right of action

A. Any person that suffers financial injury as a result of a violation of this Chapter 6.104 may bring a civil action in a court of competent jurisdiction against the lessor violating this Chapter 6.104 and, upon prevailing, may be awarded reasonable attorney costs and such legal or equitable relief as may be appropriate to remedy the violation including, without limitation, any payments made to the lessor by the tenant plus interest due. Interest shall accrue from the date that the payment or payments were made at a rate of 12 percent per annum, or the maximum rate permitted under RCW 19.52.020. To the extent that actual damages are unliquidated or difficult to prove, a court may award liquidated damages of up to \$20,000 instead of actual

damages. Such damages when awarded are to be on a per incident, rather than a per tenant basis.

B. For purposes of this Section 6.104.090, "person" includes any entity a member of which has suffered injury, or any other individual or entity acting on behalf of an aggrieved party that has suffered injury.

Section 3. The Office of Economic Development (OED) and the Department of Finance and Administrative Services (FAS) are requested to convene a stakeholder process to evaluate the impacts and effectiveness of this legislation. The process should include owners and lessors of commercial premises including members of the Building Owners & Managers Association (BOMA) and the Seattle Restaurant Alliance; operators of hotels and restaurants; representatives of the Downtown Seattle Association, the Chamber of Commerce, and the National Association for Industrial and Office Parks (NAIOP); and neighborhood business owners who may be members of independent local affinity groups. OED and FAS should seek to ensure that stakeholders represent a diversity of racial and economic perspectives. Evaluating the effectiveness of this legislation should include an evaluation of the unique needs of businesses with leases of two years or less in duration and whether additional regulation of personal guaranties may be warranted for the tenant parties to such leases. In addition to evaluating the impacts and effectiveness of the legislation, the stakeholder group should provide feedback on the implementation of the legislation and submit any recommendations for amendments to the legislation, including an explanation of the rationale for those recommendations and their anticipated impacts.

The Executive should provide an initial written report including the evaluation, feedback, and recommendations to the Public Assets and Homelessness Committee, or successor committee, and the Central Staff Director by December 31, 2024. The Executive should provide reports annually thereafter.

Section 4. These commercial lease requirements shall be reviewed in 2026.

Section 5. This ordinance shall take effect and be in force 30 days after its approval by the Mayor, but if not approved and returned by the Mayor within ten days after presentation, it shall take effect as provided by Seattle Municipal Code Section 1.04.020.

Passed by the City Council the _____ day of _____, 2023, and signed by
me in open session in authentication of its passage this _____ day of _____, 2023.

President _____ of the City Council

Approved / returned unsigned / vetoed this _____ day of _____, 2023.

Bruce A. Harrell, Mayor

Filed by me this _____ day of _____, 2023.

Scheereen Dedman, City Clerk

(Seal)