

Negotiating an Office Lease; Top Issues to Consider

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When negotiating an office lease as a tenant there are several important issues to be aware of during the negotiation process. The first thing every tenant should keep in mind is to get its attorney involved early in the process, especially prior to signing a letter of intent. While the letter of intent is merely a springboard for drafting the lease and lease negotiations, it will be more difficult for a tenant to re-negotiate an issue that it agreed to with the landlord at the time of signing a letter of intent. An attorney can help identify the important issues at the time of the execution of a letter of intent and save the tenant the aggravation of having to renegotiate issues that have already been put in writing in the letter of intent.

While conducting due diligence is typically associated with the purchase of a property, potential tenants under a lease should conduct a modified investigation of the property they are interested in leasing. Tenants should aim to determine the state of the building – Are its common areas well maintained? Are its systems (i.e. HVAC) in good working order? Is the landlord reputable? Does the landlord own and manage other properties? Is the landlord responsive? Tenants should also confirm that the zoning of the property permits the purpose for which the tenant intends to utilize the property. These are issues that can potentially have a large impact on the tenant's use and enjoyment of the property

Once the letter of intent has been signed and due diligence has been completed, the tenant can focus on the actual negotiation of the lease. The two basic types of leases are gross leases and net leases. In a gross lease the landlord will pay the taxes, insurance and miscellaneous operating expenses and the tenant will know exactly what its rent expenses will be each month. In a net lease, in addition to the "fixed" or "basic" rent, the tenant is responsible for a share of certain additional costs that are associated with the leased property.

The term of the lease also needs to be considered, including any options that the tenant may have to renew and/or cancel the lease. The ability to install signs on the property and the amount of parking spaces allotted to a particular leased property are also terms that need to be negotiated. A tenant may also attempt to obtain a right of first offer. In the event that additional space contiguous to the leased property becomes available, or additional space in the building becomes available, it would be advantageous to the tenant if the tenant had a right of first offer to lease or purchase such additional space. In the event that such space became available, the tenant would have the opportunity to lease the space before any other tenants in the building or any prospective tenants. A tenant may also try to obtain a right of first refusal on the leased property. In the event that a third party approaches the landlord about purchasing the leased property, the tenant would have the ability to purchase the leased property on the same terms as the third party offer.

The tenant will also need to consider the relationship with any existing and potential lenders of the landlord. Lenders require subordination language in leases which provides that the lease is subordinate to any mortgage on the property. As such, tenants will want to make sure that they obtain protection in the event of a default by the landlord on the landlord's loan. Without such protection, the tenant risks termination or modification of its lease by the landlord's lender upon a default by the landlord under its loan. A Subordination, Non-Disturbance and Attornment Agreement, known as an "SNDA", will provide important protections to a tenant in the event a landlord defaults under its loan. An SNDA is a three-party agreement between the landlord, the tenant and the landlord's lender. The SNDA will require the tenant to acknowledge the landlord's lender as its landlord in the event of default by a landlord but will also provide that upon a landlord default, and a lender take-over of the lease, the lease will remain in effect and the terms of the lease will remain the same, so long as the tenant is not in default.

A tenant will also want to consider its relationship with its own lender. Under New Jersey law, a landlord has a right of distraint which enables the landlord, in an event of failure to pay rent by a tenant, to take control of any personal property and equipment of tenant at the leased premises. The lender can then sell the personal property and equipment and use the proceeds to cover the delinquent rent. A lender will often require that when a borrower enters into a lease, the landlord waive its rights of distraint. The landlord should not have an issue agreeing to this waiver. The landlord will have other ways to protect itself in the event of delinquent rent (i.e. guaranty of the lease, security deposit), the right of distraint is not an easy one for the landlord to exercise (i.e. absent extenuating circumstances a landlord must obtain a court order to proceed with its rights) and the tenant will need the landlord's cooperation so that the tenant can obtain financing to operate its business successfully.

These represent a few of the many issues that are involved in negotiating a lease from a tenant's perspective. While these provide a good starting point for the negotiation of any lease, there are numerous other issues and terms that need to be considered by a tenant.