



Leasing Tips

Every In-House Counsel Should Know

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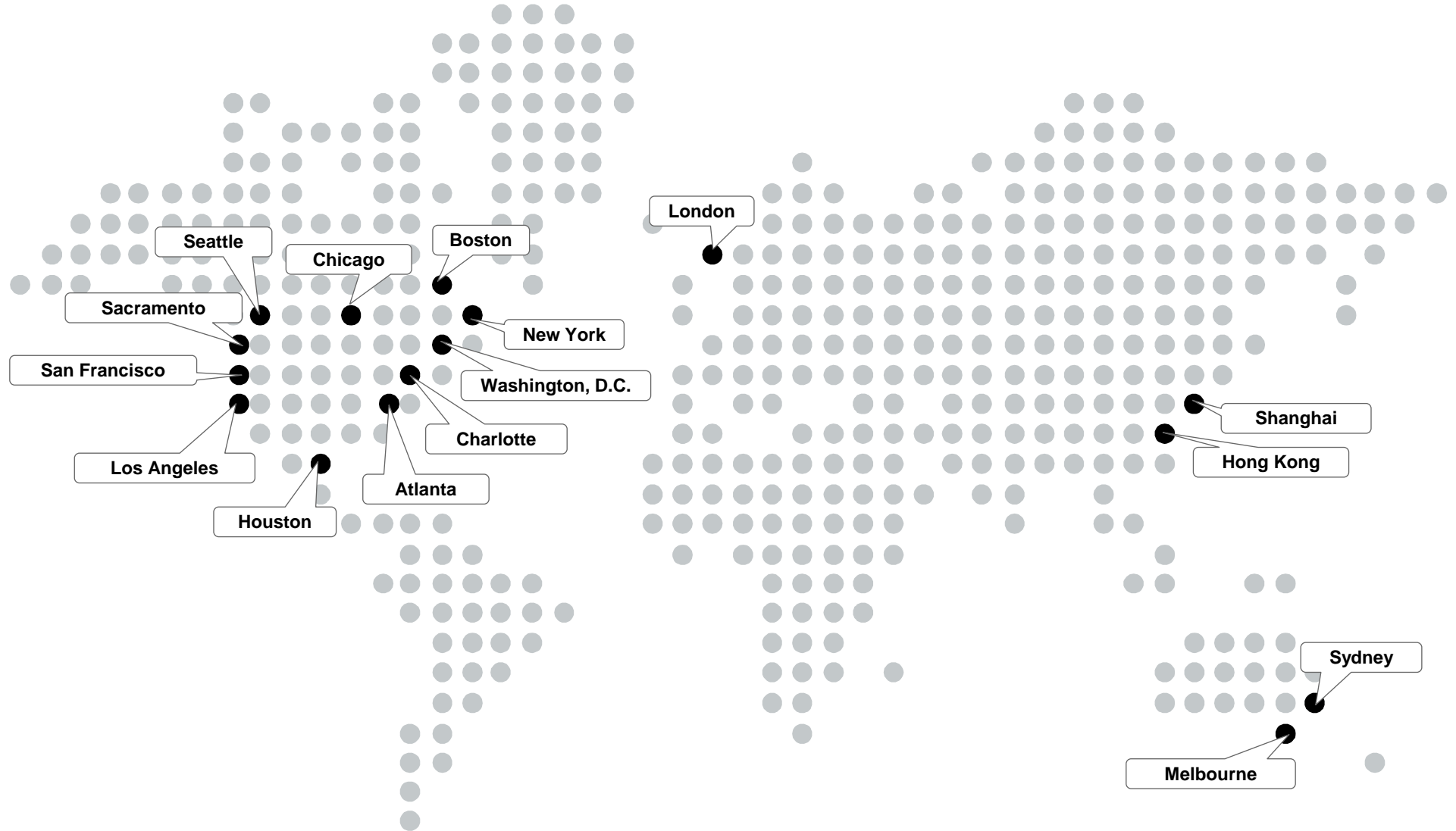
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Agenda

- 1 | Negotiating Your Letters of Intent (LOI)
 - 2 | What May Be Important In One Lease May Not Be In Another
 - 3 | Focusing on Economics
 - 4 | Shortcuts to Addressing Key Lease Terms
 - 5 | Reviewing and Negotiating Levels of Service
 - 6 | Avoiding the Use of Pre-Printed Forms
 - 7 | Don't Forget About End of Term Obligations
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Negotiating Leases in General

Almost everyone in business has at some point leased space.

- Could be for office space to conduct general business operations; retail or industrial space to operate a specific business—restaurant, retail store, manufacturing plant, etc.; a warehouse space to be used to store/distribute goods, etc.
- Most landlords have a form of lease that they use for their properties (provides for consistency in terms of both negotiations and administration) or tend to revert to a pre-printed form (AIR, CAR, etc.).
- Leases vary from a few pages (typically 10 or so, which are usually the pre-printed type) to hundreds of pages (including exhibits and schedules).
- Leases are one of the most complicated agreements as they cover a multitude of concepts including possession, construction, various economics, insurance, maintenance, assignment, insurance, indemnification, condemnation, casualty, title and seniority, and that's just a small part.



Negotiating Letters of Intent (LOIs)

- People tend to gloss over this stage and rush to get to a draft lease.
- Negotiating your LOI can save a lot of time in terms of negotiating the actual lease.
- Parties tend to respect what was agreed to in an LOI, which doesn't mean much if it says "to be addressed in the lease draft" or provides either just a very general agreement on a term or ambiguous/conflicting statements.
- For tenants, negotiating the LOI should reduce your exposure to being presented an unbalanced, landlord biased lease as the initial draft.
- For landlords, negotiating the LOI should reduce your exposure to lengthy lease negotiations as the terms have been agreed to.

What May Be Important In One Lease, May Not Be In Another

As with any contract, various risks, obligations and liabilities may be more or less important to one party than another and will be driven by many factors.

- An office tenant likely won't be concerned with use of hazardous materials, whereas a manufacturing/lab tenant likely will.
- A restaurant tenant might have greater concerns regarding transfer rights in connection with a sale of the business.
- An office tenant in a large office building is likely less concerned that its general office use is permitted by applicable law, whereas an industrial or retail tenant will definitely want to confirm that their use is permitted.



Focusing on Economics

- Economics are important in every lease—each tenant having certain expectations as to what it will be spending under its lease.
- There are numerous potential charges under a lease.
- In addition to base rent, unless the lease is gross (tenant pays only the stated rent), tenants will often pay their share of “operating expenses” and “real estate taxes.”
- Paying operating expenses/taxes may start day one or be based on a “base year” (the year upon which a tenant’s share of costs exceeding such year are based).
- Real estate and rent taxes, tends to be a regional issue, may be an expensive obligation, especially if the property hasn’t been reassessed in decades (in California, a Prop 13 issue).
- Other economic costs may include parking, after-hour service charges, excess use charges, late fees, transfer charges, etc.
- One economic matter that is often overlooked is tenant’s obligation to remove alterations on or prior to the expiration of the term.

Shortcuts to Addressing Key Lease Terms

- With so many provisions to negotiate that can impact your bottom line, it is important to know shortcuts to addressing key lease terms.
 - Fortunately, there are provisions that naturally lend themselves to shortcut solutions can save on negotiation costs as well as long-term lease costs.
- Economics are a key driver in nearly every lease. However, a tenant may not wish, or it may not be efficient to negotiate each and every economic term.
 - Instead of spending the time going through each element of operating expenses, it may be more efficient to simply obtain some form of cap on increases from year to year.
 - Similarly, a tenant may try to negotiate a flat amount for operating expenses and/or taxes.
- If exit options are important and you do not wish to negotiate the entire transfer provision, at least provide for certain “permitted transfers” that are mostly likely to occur—e.g., a sale of the company or division, transfer of ownership interests in tenant amongst existing owners or for estate planning or due to death or divorce.



Reviewing and Negotiating Levels of Service

- Many leases now provide specific levels or caps on services being provided to tenant, which may include levels of HVAC, amount of electricity and other utilities, amount of janitorial, etc.
- Service levels carefully reviewed and confirmed, especially if tenant has special or unique needs.
 - The days and times on which services are to be provided should be carefully reviewed.
 - If a tenant needs a lot of after-hours HVAC or other services (e.g., freight elevator use), should try to negotiate cost upfront (including increases) and consider negotiating for free periods and/or discounted rates.
 - If you have special needs, they should be specifically addressed in the lease.
- Landlords may or may not have an issue providing extra services, but a tenant should expect to pay for them (plus possible mark-up/administration fees) and may not be happy getting hit with additional charges.

Avoiding the Use of Pre-Printed Forms

- For any new lease transaction, be careful if you decide to use a previously negotiated lease form or preprinted local industry form.
 - There are likely business points or property attributes that are unique to your deal which may not be reflected in the pre-printed form.
- The devil is always in the details. The lease form you use should be specifically tailored to the type of property involved and the type of deal.
 - Stuffing square pegs into round holes will generally lead to problems.
- Any company that routinely engages in leasing (whether on the tenant side or the landlord side) should create and maintain its own library of lease forms.



Don't Forget About Your End of Term Obligations

- Leases often require a tenant to remove wiring and cabling installed by or for tenant.
 - Need to make sure you budget for this and coordinate timing to perform at end of term.
- Leases may require that tenant remove alterations made by or for tenant.
 - Can be an expensive and timing consuming obligation and could cut into the period in which you can operate in the lease space.
- Unless you have sophisticated lease administration software, you should calendar important dates immediately following lease execution.
 - Period to exercise an option to extend; to exercise an option to expand (albeit not an end of term issue); date by which landlord must notify you of removal obligations (which obligation you should try to negotiate out), etc.
- Holdover can be expensive.
 - Increased base rent (sometimes 200%).
 - Possible indemnification and consequential damages.



Conclusion

- As you probably noticed, many of the topics discussed today cross into each other.
- Leases are often a complicated and sophisticated agreement that will govern a relationship between parties for many years, and in some cases, decades.
- Negotiating a comprehensive and detailed LOI can save substantial time and money in connection with both negotiating the lease and getting to an execution final.
- Although significant problems are generally less common, which may be one of the reasons people tend to not want to spend the time and money to negotiate leases, and it may not be possible to identify every possible issue that could arise (e.g., not many leases previously addressed pandemic), you will generally be much happier when a major issue arises if you did negotiate your lease.

Thank You

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