Commercial Leasing – Ten Key Issues For Tenants

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In the ever-changing marketplace, tenants now find themselves in the driver’s seat with respect to negotiating commercial leases. Every tenant has different real estate requirements, but certain basic concepts should be addressed and negotiated favorably by tenants in the current climate. Each real estate broker and advisor should be sensitive to several key issues which, if addressed at an early stage, can be favorably negotiated and documented for tenants in their commercial leases.

Ten key issues for tenants are discussed below. However, it must be pointed out that several other issues can and should be negotiated for tenants within commercial leases, depending on the relative leverage of the parties involved.

Ten Key Tenant Issues

1. **Use Clauses** – A tenant should be leery of an over-restrictive use clause that severely limits the activities that can be undertaken within the leased premises. The use clause should build flexibility into the lease for the tenant, instead of being unduly restrictive. For example, should the tenant be required to sublease or assign the premises, it should be permitted to do so for “general office use”, as opposed to a specific industry segment or function. Furthermore, provided that a tenant timely pays rent, the tenant should resist continuous or uninterrupted occupancy requirements as to the leased premises.

2. **Assignment and Subletting** – Tenants should negotiate the assignment and subletting clause with a goal toward a practical operation and predictable result when and if it sublets or assigns the lease. Additionally, tenants should “pre-plan” for a potential acquisition of or by the tenant entity, and avoid any pitfalls that may result regarding landlord approvals and/or notifications. Furthermore, tenants should eliminate any potential “recapture” rights under which a landlord could take back all or part of the leased premises in the event of a proposed assignment or subletting.

3. **Expansion and Contraction Rights** – A tenant making a long-term commitment of over five years in any commercial lease should carefully consider its opportunities for either expansion or contraction at the project. Given the current marketplace, tenants may be in a better position to obtain rights of first refusal, rights of first offer and other advantages that would give an existing building tenant the right to expand or contract prior to new tenants entering the building. These rights of expansion and contraction have real monetary value and “real world implications” given the business and corporate goals of many expanding businesses.

4. **Parking** – It is essential for the tenant to obtain specific parking rights, as the same relate to quantity, cost, location, availability and administration of parking facilities. In a suburban office park, parking rights should be viewed as a significant legal right that is critical to the function of the leased premises. A sizable tenant may insist that no
other tenant in the building or project obtain more favorable parking ratios or parking charges during the lease term.

5. **Utilities and Overtime Services** – While tenants should know and predict the costs of occupancy with respect to any leased premises, additional costs assessed by landlords relating to excessive use and/or overtime heating, ventilation, air-conditioning or electricity may be billed to the tenant over and above regular rental costs. Oftentimes, if a tenant does not promptly pay such bills upon presentation, that tenant can be declared in default of the lease. To the extent possible, all such charges should be predictably determined on a negotiated schedule or otherwise specifically agreed to by the parties in the lease. Furthermore, tenants should address the result and effect of an interruption in major utilities and services at the building and leased premises, and, in most instances, rent should abate during any period of utility interruption. This “interruption of services” is rarely, if ever, included in a landlord form lease and must be carefully negotiated.

6. **Building Management Issues and Vendors** – A tenant leasing commercial office space in an office building for a term of five, seven or ten years must realize that it is committing to “living” in the leased premises for a significant period of time. Depending upon the relative size of the tenant in relation to the building, the tenant may often be able to negotiate rights which amount to either veto powers or, at a minimum, significant input relating to building management, janitorial, landscape, security, telecommunications and other services which may be provided to the building. The tenant and its representatives should identify such key issues at an early stage in the transaction.

7. **Restoration/Improvements** – A few technical provisions in the lease also demand significant attention from the tenant and its representatives. A tenant should clearly address who is responsible for removal or repair of the initial tenant improvements, as well as subsequent alterations made during the lease term. Neither landlords nor tenants appreciate “surprises” as to which party is responsible for the removal or restoration of standard or specialized improvements at the end of the lease term. Additionally, if the premises are subleased for part or all of the lease term, the parties will benefit from a clear description of responsibilities as to restoration and improvements. Typically, a tenant should not agree to restore any of the initial tenant improvements that are left in place at the lease expiration. Landlords will typically agree to accept such improvements at the end of the lease term, unless significant alterations are made and/or such improvements have been damaged by the tenant during the lease term.

8. **Holdover Rights** – Significant monetary penalties can be assessed by a landlord should a tenant holdover beyond its lease term. Tenants should specifically negotiate the exact monetary amounts, timing and scope of damages available if and when a tenant holds over. Tenants engaging in subleasing or assignment transactions during the lease term need to be acutely aware of these issues, since a subtenant or assignee holding over in the leased premises could create unintended consequences for all parties involved.

9. **Landlord Default/Setoff Rights** – An initial review of any landlord lease will note several pages dedicated to the issue of a tenant default and the landlord remedies
thereafter. Very few commercial leases describe any event of landlord default or the subsequent remedies available to a tenant. Within reasonable parameters, a commercial lease should supply notice and cure periods under which a landlord is required to repair, restore and/or remedy any default under the lease. In certain instances, a tenant may be entitled to setoff or deduct all or a portion of its rent until a landlord cure has been effected. The relative leverage of the parties and the duration of the lease term may be critical factors in determining the rights of a tenant with regard to these matters.

10. **Access Cards, Parking Passes and Keys to the Premises** – Although not critical legal issues, tenants benefit by having their advisors identify costs of access cards, parking passes and keys to the premises during the early stages of lease negotiations. It is possible to obtain all of the initial access cards, parking passes and keys at no cost to the tenant, and negotiate a fixed replacement cost for such items during the lease term. Even though these costs may not be significant given the overall value of the transaction, a tenant will appreciate having several thousand dollars in potential landlord “fees” waived at the outset of a lease transaction.

**Conclusion**

These ten key issues will benefit many tenants in most instances. However, each tenant and each landlord has unique and differing requirements and priorities. It is essential for brokers, architects, consultants and lawyers representing both landlords and tenants to identify the key priorities of each party early in the transaction, and to set realistic goals and objectives for all parties. During 2003, however, tenants may enjoy a degree of leverage in the marketplace that has been absent for several years. We urge tenants and their representatives to take advantage of such market conditions when and where they exist.

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