

COLGATE

Real Estate Advisors

Commercial Lease Negotiations, Restructurings, Reviews & Audits

Leasing Trade Secrets & Other Truths

Our “Back to School-Commercial Leasing 101” series focuses on educational video blog seminars regarding the new re-ality we all face!!! The goal is to empower you and our client base with the ability to make informed and knowledgeable real estate decisions in light of the business, professional and/or personal constraints we all face at some level.

Foreword

The Landlord/Tenant relationship is akin to a “partnership” where each must work together to allow the other to enjoy their rights and honor their obligations under their lease. Put another way, landlord’s and tenant’s need to work together to help each other lead the way out from the abyss many of them currently reside in. It is time to share the pain, take our medicine and recognize that price capitulation in many circumstances is a good thing for all concerned.

Lease Restructurings, Modifications & Workouts

Introduction

“Don’t sit back waiting for the storm to pass, learn how to dance in the rain” (Vivian Greene).

CHAPTER 1

Negotiating Mindset, Landscape & Philosophy

Simply put, the restructuring of a lease generally occurs when a tenant is proactive and approaches it’s landlord for a reduction in rent or some other type of concession relative to the terms contained in its lease. The process thereafter is one of give & take on both sides...and if all goes as planned, one where the perfect negotiation occurs...namely where both parties give and take and consequently walk away from the negotiations both a little happy & a little sad!

Landlords & tenants need to work together to get thru what we all hope are these temporary challenging times. To paraphrase the mission of the Torch Foundation—a small army of volunteers from the NY real estate industry trying to make a difference for those not as fortunate—landlords & tenants need to work together to help each other build a foundation for a better today & tomorrow!

When dealing with a request for rental relief, one needs to put his or herself in the shoes of the person sitting on the other side of the bargaining table. There are some tenants who simply feel that because they perceive the world & their business as going to hell in a bucket, that the landlord should unequivocally grant them rental relief. Regrettably for them, that isn’t & shouldn’t be the way it works! Tenants can’t lose sight of the fact that the landlord possesses a signed lease wherein tenant has agreed for a term of years to numerous monetary & non-monetary obligations. Conversely, landlords need rent paying tenants more than many can recall in recent memory, and consequently, many landlords recognize that they need to “play nice in the sandbox” with their tenants when confronted with a request for a rent concession.

In that context, when asking for a short term or long term “lifeline” from a landlord, tenants need to be armed and ready with not only a convincing “tale of woe” and a sensible solution to get them thru their challenging times, but with clear & written authoritative documentation in support of their request to landlord. Put another way, tenants need to empower their landlord to make an informed & knowledgeable decision as to the granting of their requested lease concession.

CHAPTER 2 Help Me ... Help You ... Help Us: Documentation to Provide a Landlord in Support of Tenant’s Request for Rental Relief

What authoritative documents should a tenant have ready to not only formulate its rental relief game plan but also to help the tenant “tell the story” to its landlord when in fact it does broach the subject? Stay tuned for the answer!

There are some in our industry when it comes to negotiating leases, workouts and modifications who approach it as if we are creating world peace or splitting an atom—but it’s really not that complicated and much simpler. Our team of professionals approaches lease modifications with the mindset of if “you want a little you gotta give a little”.

Having received numerous requests over the past 25 years in our respective roles as attorneys, CPA’s, commercial real estate owners, brokers, property/asset managers and/or general counsels, we always gave greater respect and priority to those tenants and their representatives who along with their request for a lease concession, delivered documents in support of their position. **The Landlord’s Mindset:** Prop me up, convince me and give me the ammunition to help me help you and simultaneously help each other given in the context of our respective “boxes of constraints” we both bring to the bargaining table!

A landlord needs as much information as possible to properly evaluate when a tenant is entitled to a short term or long term rent reduction or deferral or whatever other relief they may be requesting. **Examples of documents that need to be supplied and thereafter reviewed include:**

- tax returns (past few years) • historic financial statements • year to date & comparative profit/loss statements • future projections of income/expense • in the case of retail stores, daily sales logs (current year and the past 2 years) • payroll tax returns (current year/past 2 years)
- any other writings in support of a tenant’s request for relief **Examples** • industry wide problems germane to tenant’s business • a dearth of potential subtenants • loss of major clients • loss of credit facilities

The “Silver Lining”: As a tenant, if you have declining sales, layoffs of employees, rising utility costs, loss of credit facilities and in general a somewhat dire yet hopefully short term situation, you have a story to tell that most landlords will at least listen to. When the foregoing documents are presented to a landlord along with a term sheet outlining the relief requested and the corresponding tradeoffs you might be willing to give to your landlord, we firmly believe that a tenant has laid the proper foundation to negotiate some sort of relief from its landlord. Put another way, when authoritative in nature, the declining numbers you present to your landlord don’t lie... and as strange as it may sound, they are actually your ally in your request for rental relief!

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Leasing Trade Secrets & Other Truths > Lease Restructurings, Modifications & Workouts (Continued)

CHAPTER 3>What's So Funny 'Bout Peace, Love & Rent Restructurings? aka Factors Owners Consider If Confronted With a Rental Relief Request

Many landlords recognize that secure and stable cash flow-although quite possibly in an amount less than they might otherwise prefer-is truly a good thing. In the context of the times we now live in, it is our belief that a large percentage of something is better than 100% of the nothing that comes with a soon to be vacant space courtesy of a tenant in distress.

The following 10 or so items are but a few of some the ingredients that a landlord throws into its analytical blender when evaluating whether to drink, stir, sip, gulp, choke on or merely spit out the rental relief cocktail their tenant is now serving them:

- The devil you know is better than the devil you don't know
 - ~ (the point-if you have a tenant who you generally never hear from but for when their timely rent payment arrives in the mail, treat them like gold.
- Is the rental relief requested short term or for the remaining lease term?
 - ~ Needless to say, a request for a short term rent concession is much simpler to digest.
- Is the landlord constrained by the terms of its mortgage to even grant a rent reduction or other lease modification?
- Given the landlord's rent roll & expenses for the building, is it in danger or in a comfort zone as to complying with it's debt service coverage ratio?
- What is the near & longer term tenant rollover for the bldg?
- Rising vacancies and declining rents in virtually all markets
- Increased competition from tenants trying to sublet their space at lower costs with potential use of furniture, phone systems & sufficient existing build-outs.
- Is the named tenant merely a shell corporation? What "skin" does the tenant have in the "game" (e.g., a parent, personal, or good guy guaranty)?
- In the long term, is the tenant someone the landlord would like to renew its lease-if so, among many reasons, potentially not having to pay an outside broker, not do a new build-out or provide an improvement allowance which go hand in hand with a new tenant are also factors landlords consider.

Bottom Line-Do (a) the documents, (b) the tenant's "tale of woe" and (c) tenant's game plan for recovery-when evaluated by a landlord in the context of the foregoing factors-support the claimed level of distress and provide the landlord hope that the tenant will weather the storm and prosper in the long run?

CHAPTER 4

The "Proposal"

Tell the tale, back it up with supporting documentation, provide the recovery game plan & propose what the tenant will give up in return for rental relief!

The proposal to landlord to throw tenant a lifeline should contain 7 honest & concise chapters-what we like to refer to as our very own **MAGNIFICENT 7!**

Part 1: Basic intro and a meaningful quick pat of itself on the back by the tenant to remind the landlord I that until the recent past, historically your tenancy has been a mutually beneficial one ...just be careful not to sprain yourself on the shoulder while doing so!

Part 2: "The Tale of Woe". Tell your story to the landlord-and don't be afraid to convey it from a personal, business & professional perspective.

Part 3: The authoritative written backup in support of the tenant's temporary short term distress.

Part 4: Tenant's game plan for recovery. Tenants walk a fine line here: a landlord needs to be seduced by a tenant with substance, and with quite a bit more than a "well-if there is life there is hope" proposition. Ideally, the game plan will give your landlord comfort that you as the tenant will ultimately weather the storm and live up to its lease obligations once that storm has passed.

Part 5: The "Plea for Rental Relief". The request needs to be rooted in reality... the tenant needs to be realistic in the context of not only it's own box of financial constraints but those of it's landlord as well. Now is the time to step up and tell your landlord exactly what you are looking for! **Examples: • a free month or 3 of free rent? • a 25% reduction in rent in the form of a deferral or for an outright forgiveness of rent?**

- is it an offer to extend your lease in exchange for a reduction in the current higher rent to that of what is now market?
- a request to take back a portion of your space or move you to a smaller/less desirable location in the building that now fits your downsized business?

Part 6: "Life is a Tradeoff": The time to "pony up" and give what you got to give to get what you want and need to survive! **Examples include:**

- surrender of a tenant's security deposit
- going personal for the rent reduction if you don't live up to the terms of your restructuring agreement
- paying interest on the reduction if it is merely a deferral
- giving the landlord a good guy guaranty if one doesn't currently exist
- signing a Confession of Judgment for arrears
- moving your retail store to a different part of a strip mall to allow the landlord to combine your space with an existing vacant space to make it more attractive to lease
- staying open for a period of time beyond that which you as the tenant would otherwise prefer if your landlord doesn't want your high traffic location to "go dark" prior to it potentially securing a replacement tenant

Part 7: The "Up Close & Personal": The time for the tenant to convey the message that, in the words of McCartney and Lennon, "we can work it out" and "take a sad song and make it better"! We strongly prefer that prior to forwarding the proposal to the landlord and requesting a meeting, the tenant &/or his representative call and give the landlord a "head's up" as to what the tenant is delivering.

Bottom Line: More than most of us can recall in the last 20 years or would like to acknowledge, the times dictate that a significant number of landlords and tenants not only need each other more than ever but also need to work together for their mutual survival.

CHAPTER 5: Concluding Rants and Raves on Lease Restructurings, Modifications and Workouts

Imagine if you will the 1970's hit song "Why Can't We Be Friends" playing in the background. With the mood now set, to landlords and tenants contemplating whether to "play nice in the sandbox" with each other for the greater good of each party's respective interests, or alternatively, to kick sand in each other's face and sit back and wait for the fallout from doing so-among other factors-please ponder the following Jerry Garcia lyrics when considering whether to continue your partnership ... **"The Grass Ain't Greener, The Wine Ain't Sweeter, Either Side of the Hill"**

Many out there don't necessarily agree that landlords and tenants need one another, nor do they believe that at a certain level, landlords and tenants are truly partners-and for better or for worse, just like a married couple-they need to continually cultivate and work on their relationship. Many factors are taken into account when considering whether to continue the "bond" between a landlord and tenant-including the myriad of constraints coupled with the costs associated with relocating (from a tenant's perspective) or having and thereafter leasing vacant space (from a landlord's perspective). Accordingly, simultaneously "channeling" the Beatles and Crosby, Stills & Nash, many landlord's and tenant's should adopt the dual mantras of "We Can Work It Out" and "If You Can't Be With The One You Love, Then Love The One You're With".

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