



Negotiating Three Pesky Provisions in a Retail Lease: Assignment, Rent Acceleration, and Exclusive Uses

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As a relatively new real estate attorney, I often interact with other relatively new brokers, property managers, and asset managers. Broadly speaking, these professionals certainly understand that many transactions warrant, or even require, the involvement of a commercial real estate attorney, but I often find myself discussing how an attorney can add value to a transaction. For these real estate professionals, the crux of the transaction is usually the financial terms. And the ultimate goal of the deal is getting it across the finish line. For an attorney, the crux of the transaction is usually the language of the contract or lease; the language which contemplates all the “what if’s” that may pop up along the way. This article will highlight three heavily negotiated provisions in a retail lease transaction and explain how the involvement of an attorney can add value for the client.

Assignment and Subletting

In a retail lease, there should always be a section regarding the process for the tenant to request and complete an assignment of its lease. This is a hot button section for both landlords and tenants: the landlord wants the tenant and any guarantors to remain bound by the lease after a transfer, while the tenant usually wants to be released free and clear. Understandably, from an increased financial security perspective, the landlord wants as many people and entities as possible bound by the lease and guaranty, while the tenant does not want to be responsible for a default it did not cause post-assignment.

When representing a tenant, attorneys often try to build in potential escapes from the lease contract. One way this is accomplished is to include an automatic release if the new tenant and guarantor have a specific (often tangible) net worth, or if the new tenant and guarantor have a net worth *equal to or greater than* the original tenant and guarantor. From the landlord’s perspective, this is not necessarily an unreasonable request, but landlords must be careful to set a high bar for release so as not to be exposed to greater risk in accommodating a tenant request. While this proviso may not assure the landlord of any minimum operational experience of a potential assignee (which is often an important consideration too), it provides to the landlord certain assurances of financial strength.

Default: Rent Acceleration

The second lease provision that can often remain open until the very end of the negotiation is the rent acceleration provision as a landlord remedy following a tenant default. Generally, a tenant is very much against rent acceleration because a tenant may potentially owe hundreds of thousands of dollars immediately, but, more importantly, if there is a personal guaranty, the individual guarantor could owe the same amount. Landlords, on the other hand, do not want to rely on an already unreliable tenant to pay rent monthly after default, thus the need to declare all future rent to be immediately due and payable.

At times, landlords are willing to remove the rent acceleration provision from the lease if there is a personal guaranty. But, if landlords are still uncomfortable with the risk, another option is to provide for rent acceleration of the rent coming due for the balance of the term reduced by the then-fair market rental value of the premises. To make the provision even more tenant-friendly (and perhaps more likely to be enforced by a court), the rent can be further reduced to its net present value

in performing the aforementioned calculation. While the enforceability of rent acceleration provisions remains highly dependent upon the applicable jurisdiction, courts generally favor a present value reduction calculation over the onerous burdens of straight acceleration.

Exclusive Use

Though all landlords want maximum control of their shopping center or mall, letters of intent often grant tenants an exclusive or protected uses to offer a particular good or service. The letter of intent, however, will often contain just a short blurb providing the tenant the exclusive right to sell or provide a particular good or service such as, for example, the sale of hamburgers. The generic blurb in the LOI, however, often doesn't contain a remedy. While there are strategic considerations as to whether the inclusion of a remedy is in the best interest of a landlord or a tenant, generally speaking, setting forth a specific remedy often favors a tenant.

An attorney effectively representing a tenant will generally, at a minimum, add a remedy if the landlord leases a space to another tenant that will sell hamburgers – say, a 50% rent abatement and a termination right if the violation is not cured within twelve months. While the specifics of such a remedy (or the inclusion of a remedy at all) are certainly subject to negotiation, a seasoned attorney on the landlord's end will also add a remedy for a "rogue tenant violation." That is, if a tenant, without the landlord's permission, begins selling hamburgers, the landlord is entitled to additional time to cure the violation. From the perspective of the landlord, it can solidly argue that if it did not intentionally lease space in violation of the exclusive use, it should not be subject to a penalty for a tenant acting outside of the scope of its permitted use. The tenant's attorney should note, however, that the landlord is the only party that can prevent the rogue tenant violation, as the landlord owns the shopping center and it is the only party with a contractual relationship with the offending exclusive use violator. In this instance, many times a compromise is reached requiring the landlord to diligently attempt to cure the rogue tenant violation and, so long as it does, it will not suffer a penalty for some stated period of time while it pursues corrective action.

Conclusion

Though thoroughly negotiating a lease (or any contract for that matter) may slow the pace of a transaction, it is important to realize the attorney's goals of achieving clarity and, more importantly, the value that an experienced attorney can add to answer those "what if's" that often go un contemplated. The three above examples are just a few of the hotly negotiated legal issues that I've encountered thus far in my early years of practice, and I have no doubt that the list will continue to grow throughout the years.

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