

## WHAT ABOUT THE LITTLE GUYS?

### THE TOP ISSUES FOR A SMALLER TENANT TO NEGOTIATE IN ITS LEASE

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#### A. Introduction

Statistics tell us that small businesses create more new jobs each year than big corporations. Yet, when reviewing the great questions in leasing, commentators often overlook the needs of smaller tenants, even though the vast majority of leases involve them. This article will focus on the essential concerns a small tenant will have when executing a lease, how the landlord will respond and how the lease can address the tenant's concerns while still providing the landlord the rights and remedies it needs.

The main issues for the smaller tenant revolve around the performance of its business. The tenant will want protections in the lease ensuring that the landlord's operation of the property will not impair the tenant's business. Next, the tenant will want to protect its bottom line. It will want to know in advance what the lease is going to cost, to be able to budget this expense, and to avoid surprise costs that can be fatal to a small business. Lastly, the tenant will want an exit strategy, either in order to sell its business, or in the unfortunate circumstance when the business fails, to reduce its exposure.

#### B. Protection of Business

A small tenant must consider the nature of its business. Often, a nearby tenant with a competing use can cut into the small tenant's revenue stream. Understandably then, small tenants will look to the landlord for a certain amount of protection, since the landlord ultimately controls the type of tenants on the property and the mix of uses that the tenants, collectively, provide to the public or other tenants of the property.

##### 1. Use

The nature of the tenant's use, however, will govern how flexible the landlord is willing to be. Of course, no neighborhood coffee shop wants to operate next to Starbucks. On the other hand, if a tenant opens up a sundries shop in an office building, it is unlikely the landlord would want or need another similar use on the property. The tenant should analyze the critical aspects of its business before asking the landlord for an exclusive use clause. The tenant must be able to explain why the request is important in the context of the particular property. While an office building might not be able to support more than one sundries shop, a strip mall might be able to support a sundries shop and a stationery store, even though both operations may involve the sale of greeting cards. A landlord will not welcome a request for an exclusive use, since it restricts the landlord's ability to lease space, and can lead to tenant conflicts in the future. As a practical matter, the landlord will not want to waste much time and effort negotiating a business protection provision with a tenant who pays a modest sum of rent and who, in the landlord's opinion, may go out of business in the next economic downturn, regardless of what the other tenants in the property are doing. Landlords typically save business protection provisions such as radius clauses and tenant exclusive use clauses for the high-rent tenants who can create a draw to the

landlord's property. But, if the tenant knows a direct competitor will toll the death knell for its business, it should insist on an exclusive tailored to its critical area of income.

Early on in the tenant's investigation of a multi-tenant location, the tenant should ask the leasing broker to find out from the landlord what exclusive use rights the landlord would be willing to grant, and then review the response in light of the current and likely future other tenants of the property. If the landlord refuses to grant an exclusive use clause, the tenant could consider requesting a right to terminate if the landlord leases to a competing use, but this is usually not very helpful to a retail tenant because (a) it is extremely expensive to close down and move; and (b) when it moves, the tenant often loses much of its customer base, which it may not be able to rebuild in the new location.

Smaller tenants may want to change use during the lease term in order to maximize profitability. For example, one business idea (e.g. buggy whips) may be less profitable than another (e.g. video arcade). Also, consumer product demands morph with increasing speed (skis move to snow boards which move to snow skates; video tape moves to DVD, muffins are hot but change to croissants and then to bagels). As a result, tenants need the flexibility to change with the market. Similarly, a retail tenant who is trying out a new location for the first time can never be absolutely sure it will be a success in that location. For example, what if an auto parts chain wants to open a new store on the landlord's property? The landlord will want to limit the use clause only to the sale of auto parts and accessories, to protect against other uses that do not fulfill its ideal tenant mix. But such a limited use may not work for the auto parts tenant. If the tenant is a successful retailer of auto parts elsewhere, it will know that if its store fails in this location, it will be because of the location, not the tenant's operation. The tenant will find it impossible to assign or sublet because of the overly restrictive use, since another auto parts seller will have the same problem. Thus, the use clause must allow the tenant to change to another use that is reasonably compatible with the rest of the uses on the landlord's property, as long as this does not violate any of the landlord's existing exclusives.

While landlords want profitable tenants who can pay the rent, to maximize overall profitability landlords (especially in the retail context) need to orchestrate a harmonious tenant-mix, consistent with the character of the property and compatible with parking demands, and other operational details. As a result, the landlord may prefer certain types of profitable businesses (e.g. high-end hair salon and spa) to others (e.g. barber shop, tattoo parlor or blue video outlet). Often, some profitable uses that may seem particularly attractive to the tenant are unacceptable to the landlord in certain parts of the city. For example, the landlord of a Class A building in an urban core may not want its soup and lunch counter tenant to sell cigarettes, lottery tickets or 40-ounce malt liquor. Often, when a tenant sells these kinds of items, it attracts a clientele that the landlord may deem undesirable. In addition, the landlord's other tenants may find such clientele undesirable if they feel that the advent of a new demographic materially alters the atmosphere of the landlord's property. Accordingly, the landlord will want to limit strictly the tenant's use and may even want to add boilerplate to its lease form stating that, apart from the allowed uses set forth in the lease, no other uses are allowed and expressly exclude certain uses. The lease would then set forth the allowable uses with particularity. It is also worth noting that in some geographical areas, a change in a tenant's use may never attract a change in that tenant's clientele and the landlord may be less sensitive to a use change.

## 2. Non-disturbance

A smaller tenant may also seek a non-disturbance agreement (“NDA”) from the landlord’s lender if the premises are integral to the tenant’s operation, or the tenant will invest in significant tenant improvements. As a practical matter, the landlord usually does not care if the tenant receives an NDA or not. It is more a question of the time and effort it will take to run this issue by the lender providing financing for the property. The landlord’s response to a request for an NDA will be governed by the loan documents and its experience with its lender. The landlord and tenant may elect to make the receipt of an acceptable NDA a contingency of the lease, so long as the landlord is under no obligation to obtain the NDA. The tenant making the request should be prepared to pay all of the lender’s costs incurred in delivering the NDA. A further alternative may be for the tenant to waive receipt of the NDA from the existing lender, but make subordination of its lease to any future mortgage conditional upon receipt of an NDA. Landlords will almost always grant this concession.

## 3. Financing

Smaller tenants will very likely need financing for portions of their business. The tenant’s lender will usually require a first priority lien on all of the tenant’s assets, including its leasehold interest. The smaller tenant should therefore request that the landlord prospectively agree to waive or at least subordinate any lien the landlord may have to the lien of the tenant’s lender, and to enter into a “landlord’s consent” with respect to the lease. Such documents include a range of terms, but at the core the landlord agrees that the personal property of the tenant is not subject to any claims of the landlord, allows a collateral assignment of the tenant’s lease to the tenant’s lender, and grants the tenant’s lender certain rights, such as (a) notice and opportunity to cure tenant defaults; and (b) the right to enter and remove the personal property following a loan default or termination of the lease. Here, the landlord’s chief concern lies in potentially losing control over the type of business in the tenant’s space. If the tenant should default under its loan, the tenant’s lender may have the ability under its collateral lease assignment to assume the tenant’s leasehold interest and operate any type of business that the lender sees fit. In such an event, the tenant’s lender can deprive the landlord of control over the tenant mix on the property, which is of special concern in the retail context. However, if the use clause in the lease strictly limits the permitted uses of the premises, the tenant’s lender will be bound by all of those restrictions. Alternatively, the landlord may consent to a lien on the tenant’s personal property, but refuse the tenant’s lender the right to have a lien on the tenant’s leasehold. Unless the tenant’s location is pivotal to the residual value of its business, the tenant’s lender may well consent to this arrangement, since assumption of the lease carries with it an obligation to pay the rent, lowering the likelihood that the lease will be an asset.

It is critical for the tenant to obtain the concurrence of the landlord and the tenant’s lender before the tenant signs the lease and while the tenant maintains its bargaining power. If the tenant waits and requests the a landlord’s consent AFTER signing the lease, generally the landlord will have no obligation even to negotiate in good faith with regard to the document. The tenant may then be in the impossible position of being bound by the lease, but not able to obtain the financing it needs to operate the premises.

#### 4. Franchises

Often, smaller tenants are franchisees who operate a particular business under a franchise agreement. Many of the same issues arise with franchisors as with tenant lenders. Often the franchise agreement requires that the franchisor have the right to take over the business in the event of the tenant's/franchisee's default, and the right to re-assign the lease to a new franchisee for operation of any one of the franchisor's current concepts. In these cases the landlord's concerns are no different than in a collateral assignment of the tenant's lease, as discussed above. Namely, the landlord may have bargained for a specific business on its property; i.e., a particular restaurant or a specialty retail operation. If the use changes as a result of the franchisor taking over the lease and modifying the business, the landlord may be stuck with a use that is incompatible with the other uses on the landlord's property, and or which may not contribute to the landlord's ideal tenant mix. If the lease limits the permitted uses to those that will be workable for the landlord, the landlord can reduce or eliminate this risk. The bottom line with franchise tenants is that the landlord, tenant and franchisor will need to work through the franchise requirements prior to execution of the lease.

#### 5. Expansion

Often, smaller tenants hit the market at the right time, under the right circumstances, and suddenly the 300 square foot storefront space is too small. The tenant needs to expand – and fast – preferably into an adjacent space. These types of scenarios are best negotiated prior to signing the lease. The landlord's position on this type of request will depend on a variety of factors, including among other things, the vacancy rate in and around the property in question, the lease terms of the tenants surrounding the new tenant making the request, and whether the request is in the form of a right to expand or a right of first offer or first refusal on available space. In any event, the landlord will want to document how the rent will be determined for the expansion space to ensure the tenant pays as close to market rent as possible, unless some other factor makes a rent concession to the tenant reasonable. Alternatively, if the landlord cannot accommodate the tenant's expansion needs, the tenant may request a right to terminate so it can move to larger premises. For example, the tenant may request that if its annual sales exceed \$X and the landlord does not make acceptable larger space available, the tenant would be able to terminate the lease.

### **C. Tenant Operations**

#### 1. Maintenance

Smaller tenants often have maintenance issues. By the nature of their business, smaller tenants will not have large budgets for maintenance and will want to shift that burden to the landlord as much as possible. However, the landlord will not be willing to deviate from its regularly building maintenance allocation at the smaller tenant's request. In fact, if the smaller tenant has storefront premises or has any kind of business that uses outdoor seating, the landlord may want the smaller tenant to bear additional maintenance responsibilities, such as keeping a portion of the street clean as well. At minimum, the small tenant will want to ensure that the lease is not overreaching. Often landlord forms will provide that the tenant bears all responsibility for maintenance, including structure and compliance with laws. The small tenant

should at least ensure that the landlord has a duty to maintain the building structure, exterior, common areas and any shared building systems, such as HVAC and plumbing.

## 2. Disruption of Services and Casualty

Smaller tenants need the right to terminate in the event of a disruption in services or casualty damage. For example, if a shopping center landlord fails to adequately maintain and repair the common areas, provide power, etc., unlike many larger tenants with multiple locations, the smaller tenant's business will suffer and ultimately fail unless the problem is fixed in short order or the tenant can move elsewhere (although relocation is often not optimum for the tenant, as discussed above). From the landlord's perspective, all tenant termination rights are undesirable, and in fact may be directly contrary to provisions in the landlord's financing documents. A prudent landlord will review its loan documents for these issues before granting any concessions in this regard. In addition, the landlord may have an administrative reason for having all leases state the same terms and conditions in the event of casualty or disruption of services. Especially in the event of casualty, when the landlord may have a duty to repair in a stated timeframe, it is easier for the landlord if every tenant's lease has the same stated timeframe (e.g. repair within 120 days after the damage). To protect against the failure of the tenant's business during a disruption of service or casualty, many landlords correctly insist on the tenant carrying business interruption insurance. While large tenants often negotiate this provision out of the lease, for the small tenant, business interruption insurance may be the only thing that keeps the business alive. Thus, the landlord should insist that the smaller tenant carry this insurance.

## 3. Parking

Smaller tenants may request special parking commitments, especially if the tenant's business is dependent on accessible parking for clientele near the tenant's premises. For example, a restaurant may require that the parking garage be available for customers at a reduced rate in the evening. But, if the landlord leases the parking garage to a parking services provider, the landlord may have no control over the rates and concessions available to the tenant. Similarly, an office tenant may request that the landlord provide a certain number of reserved parking spaces for free for the length of the lease term. The landlord's ability to grant this will depend on the overall parking situation for the project. Where parking is tight, the small tenant will be the last to obtain reserved spaces. In the case of the office building tenant, the landlord may even want the tenant to lease a guaranteed number of spaces each month at a specified price. The tenant may not know how many employees its will have from time to time or whether they will wish to pay for such parking. Therefore, such a parking arrangement will likely be unattractive to the tenant. If parking is critical to the tenant, this needs to be discussed early on, preferable at the time of the letter of intent. As a practical matter, landlords want their tenants to succeed and will try to accommodate reasonable requests, if they are forced to address the issue as part of the overall lease proposal.

## 4. Signage

Smaller tenants may also need specialty signage, for example, to meet the requirements of their franchise agreement. Depending on the relative leverage of the parties, the landlord may not be willing to grant signage concessions to the smaller tenant that are inconsistent with

building standard signage. With respect to street level premises, the landlord will be especially sensitive to its other tenants' needs for visibility on the street, and may be unlikely to grant the tenant's request for an awning or other exterior markings or signage. If, for whatever reason, the tenant's request for signage is compelling, at the very least the landlord will want to pre-approve the tenant's signage specifications in advance of lease signing, to ensure that any proposed signage will be consistent with the landlord's property. The tenant should be prepared to pay for any extra costs caused by a deviation from the building standard signage. As with parking, if signage is critical to the tenant, this needs to be discussed at the time of the letter of intent.

#### **D. Unanticipated Costs**

Unanticipated costs are the hobgoblin of any tenant, and smaller tenants are especially sensitive to this issue.

##### **1. Build-out**

With respect to tenant improvements, smaller tenants will be sensitive to cost overruns during the build-out process and will want to quantify their risk and perhaps even shift some of the risk of tenant improvements to the landlord. A turnkey build-out from the landlord may be ideal for the smaller tenant. Smaller tenants in particular often have a very limited budget for the construction of tenant improvements to the premises. Further, if the tenant is a franchisee, the tenant must comply with the detailed construction specifications referenced in the franchise agreement – often quite a challenge given the smaller tenant's budget. Correspondingly, the landlord will have a budget for the tenant build-outs and have an equal interest in making sure that there are no costly surprises on the landlord's end. The very nature of the smaller tenant may mean it is leasing Class B premises, which may need extensive improvements prior to occupancy. Unless the tenant has some particular leverage, the landlord will likely not be able to offer the smaller tenant any tenant improvement allowance and may only be willing to do basic building-standard tenant improvements.

To avoid downstream difficulties, the lease should (a) clearly distinguish between those elements of the build-out that are the landlord's responsibility and the tenant's responsibility; and (b) clearly state the standard for each party's level of work, if any. For example, the lease should address who is responsible for the bathrooms, for distributing the HVAC within the space, for making entry points for data and communications lines, for preparing the surface of the floor so it is ready to accept the tenant's flooring, etc. The standard of work will typically be in compliance with applicable codes and regulations, but the landlord may only be responsible to the level of building standard finishes whereas the tenant may be required to construct finishes in accordance with its franchise agreement or in a "first-class condition." In this vein, the landlord often requires pre-approval of all plans and specifications for any tenant improvements prior to lease signing, so that all parties can budget accordingly. Often landlord's standard build-out will not work for an idiosyncratic use, such as a small retail space in an office building. In this instance, the parties will need to place special focus on the build-out terms.

##### **2. Compliance with Law**

Depending on the tenant's use, the tenant may need to comply with the Americans with Disabilities Act (ADA) or other codes and regulations. Leases will vary in allocation of

responsibility for compliance with laws but as with the build-out situation, the smaller tenant's budget is often tight, and the tenant will need to make sure that the lease is clear on who is responsible for compliance with applicable laws. It should place special emphasis with regard to (a) making sure the landlord delivers the premises in compliance with applicable law (or at least knowing the deficiencies and what it will cost to remedy them); (b) changes in laws occurring after delivery; and (c) required changes to the premises as a direct result of the tenant's particular use. For the landlord's part, it will require the tenant to build all of its improvements in compliance with applicable law. Moreover, the landlord will want the tenant to be responsible for compliance with all future laws and regulations with respect to the tenant's premises. Accordingly, smaller tenants should understand what costs are involved in code compliance given their business and budget for these expenditures. The landlord will usually warrant that the premises, if new construction, when delivered to the tenant, will comply with all applicable laws, including ADA and hazardous materials laws. In older buildings, however, the landlord may take the position that the tenant takes the premises AS-IS, with no warranties as to compliance. Before the tenant considers accepting this, it must perform a thorough inspection. Even then it will be taking a risk (magnitude unknown) that it will later encounter undiscovered problems that could be extremely expensive to remedy (hazardous materials removal, structural instability, etc.). Similarly, in older buildings, the tenant must be cautious about taking on responsibility for compliance with future laws, and consider excluding laws relating to change in the structure or building systems (upgrades to HVAC system to remove CFC's, seismic upgrades, etc.). Another possible protection is for the tenant to negotiate for a cap on costs it must bear for unanticipated problems; providing that if the problem were too expensive to remedy, either the landlord would bear the cost or the tenant could at terminate the lease.

In addition to ADA compliance, there may be compliance issues with respect to laws relating to hazardous substances. The landlord will want the tenant to comply with all laws and regulations regarding hazardous materials and to indemnify the landlord from any damage or loss caused by the tenant's violation of such laws. The landlord will usually not offer smaller tenants a reciprocal covenant and indemnification regarding hazardous materials, resulting in a one-sided provision. At minimum, the tenant should limit its compliance obligations to matters arising directly as a result of the tenant's activities in the premises.

### 3. Utilities

Utilities can also result in unanticipated costs. Smaller tenants need electricity, HVAC and garbage services, just like any other tenant. However, the ever-fluctuating costs of electricity and other utilities can be especially burdensome on smaller tenants. A small tenant may have unusually high consumption, such as a restaurant, hair salon or spa, which consumes more water than other uses. Landlords often ask tenants with excess consumption to bear the cost of separately metering their premises, but this may be too great a burden for a smaller tenant given the budget constraints previously discussed. The landlord will likely be unwilling to bear the costs of separately metering the smaller tenant's premises, but more often than not, the landlord will have a mechanism for allocating the operating costs of the property to each tenant based on the tenant's pro-rata share of the property. From the landlord's perspective, if it already has a procedure in place where each tenant is charged for its pro-rata share of operating costs, it is simpler to add the new tenant into the system.

#### 4. Operating Costs

While the smaller tenant can take some comfort in knowing it is only paying for its pro-rata share of operating expenses (even if it has high consumption), the tenant may still be subject to unanticipated costs. Especially harsh winters may subject the tenant to snow removal costs; upgrades to the parking lot pavement and lighting systems may cause a rise in operating expenses for the tenant; and the ever-popular roof maintenance can cause an unanticipated increase in the smaller tenant's pro-rata share of operating costs. Additionally, if the smaller tenant will generate special additional or increased costs (e.g. a start-up biotech operation or a veterinary practice with special maintenance needs), the landlord may require that the tenant pay for or provide for those special needs or expenses. While a small tenant is most in need of extensive exclusion and limitations on what the landlord can charge as part of operating costs, landlords generally will not spend the time to negotiate these provisions on a small lease, or to grant the tenant the right to audit the landlord's books. The small tenant's best approach is to negotiate for a cap on its share of operating expenses. The landlord will be unwilling to cap expenses over which it has no control (e.g. utility expenses, real estate taxes and insurance premiums). However, there may be other expenses over which the landlord has more control and would be willing to consider a cap. For example, the landlord may be confident that the repair and maintenance budget won't increase more than five percent (5%) per year and therefore be willing to agree to a corresponding cap on the repair and maintenance expenses that will be passed through to the tenant.

Of course, the 300-pound gorilla in this whole equation is the cost of insurance. The landlord's insurance premiums are often passed through to its tenants. The landlord's lender may require the landlord to carry certain types of coverages at certain limits and these coverages may include the always-feared terrorism insurance. In addition, the landlord's lender may need to approve the landlord's lease form, which will contain the insurance requirements for each tenant. Generally speaking, the landlord will also realize an administrative benefit from having a standard insurance provision in all of its leases. Experienced landlords will make sure that their leases (a) require the tenants to comply with any insurance requirements imposed by the landlord's lenders; and (b) pass through to the tenants all of the costs of the landlord's insurance as required by its lenders. This can result in problems and unexpected costs for the tenant. For example, in the last three (3) years, more and more lenders have required that landlords carry earthquake and terrorism insurance, and the cost can be astronomical. The landlord may have no choice if the deed of trust for its loan requires the landlord to carry "such other coverages as lender requires from time to time." Even standard insurance clauses can cause problems for smaller tenants. In some limited cases, the tenant's insurer may be suddenly downgraded by A.M. Best and no longer meet the rating standard required by the lease, causing the tenant to go to the market to seek a new insurer. In addition, many tenants do not carry business interruption coverage (discussed above) because the cost may be out of scale with the benefit. All of these create potential pitfalls for the smaller tenant, but the landlord's ability to work with the tenant may be limited by the requirements of the landlord's lender, the location of the landlord's property or the insurance market in general. As a result, the tenant's goal will be for the insurance provisions in the lease to be as specific as possible. The tenant should check with its insurance agent, before it signs the lease, to verify that all required coverages are likely to continue to be available at a commercially reasonable cost.

## 5. Surrender of the Premises

The tenant often incurs another unanticipated cost when it vacates the premises. The landlord will want the tenant to remove all of its trade fixtures and restore the premises to a good condition, wear and tear excepted. The landlord will likely want the tenant to patch and repair all holes left in the walls, the ceiling or the floor as a result of the removal of the tenant's equipment. In the case of flooring, such a provision may a substantial cost to the tenant. Naturally, at the time of the lease expiration, the tenant will not want to incur unexpected costs, and, as discussed above, a small tenant simply may not have the budget required for such work. As with the construction of tenant improvements, the tenant's obligations with respect to the removal of tenant improvements should be documented as much as possible prior to lease signing so that each party can allocate its risk accordingly.

### **E. Exit Strategies**

#### 1. Transfer of Lease

Every tenant, small or large, needs to have some right to assign the lease or sublet the premises as part of an overall exit strategy for the lease. The right to assign the lease or sublet the premises can be critical for the smaller tenant, because it will allow for the natural evolution of the tenant's business (e.g. sale of the business, merger with another business, expansion, consolidation of multiple locations, etc.). Typically, the landlord's lease form will prohibit assignments of the lease without the landlord's prior written consent. Moreover, the lease will usually characterize a sale of the business, a merger, or a transfer of more than fifty percent (50%) of the stock as an assignment requiring the landlord's consent. The lease will also provide that the transfer of the lease does not release the original tenant or any guarantors from their responsibility under the lease or any guaranty thereof. Also, the lease will often provide that landlord receive any consideration paid in connection with a transfer of the lease. Finally, the lease may require that the new tenant have at least the same net worth or financial stability as the original tenant, and may require the assigning tenant to pay a processing fee to defray the costs of the landlord's underwriting of the new tenant and the landlord's attorney's fees in documenting the assignment.

From the tenant's perspective, the assignment and subletting provisions must be reviewed carefully and negotiated thoroughly. For example, in the case of an assignment, the tenant should retain all of the profit from the sale of its business and any improvements it may have made to the space. Similarly, even if there is profit attributable to the value of the lease (as opposed to the business), the tenant should recoup all of the commissions and other costs related to the transfer before the landlord gets its share. With regard to a sublease, the tenant may be providing additional services to the subtenant (use of a conference room, receptionist services, etc.) so the consideration for those additional services should be segregated. Importantly, if the tenant sells its business to a creditworthy successor, the principals of the business will want a release from liability under the lease. The landlord has absolutely no incentive to grant this release if the business is sold after the lease is signed, so the tenant must ask for this on the front end.

## 2. Termination of Lease

The ultimate exit strategy is a right of the tenant to terminate the lease in the event certain circumstances occur. The landlord is typically unwilling to consider such a provision since the landlord wants a quantifiable income stream over the long term. In addition, the landlord's lender may not allow it to consent to early termination clauses without the lender's prior approval. A small tenant should note that even though there may be valid business reasons for an early termination clause, landlords grant termination rights sparingly. In cases where landlords do grant such rights, landlords often require payment of a termination fee and reimbursement for all unamortized costs related to the lease (free rent, commissions, tenant improvements, etc.). Further, the termination right it will usually be a one time right, at a fixed point in the lease term, such as after the third year. This way the landlord can book the lease as a three-year lease, and if the termination right is not exercised, it can then book the balance of the lease term.

## 3. Guaranties

Landlords often require that the principals of, or other individual of sufficient net worth related to, the smaller tenant guaranty the lease. Tenants who have the leverage to do so should try to include various limitations or sunset clauses in the guaranty. For example, the guaranty might only cover the unamortized tenant improvements and commissions, or, so long as the tenant is not in default, it might be capped at a certain number of months of rent, with the number of months declining over the lease term. Each landlord will have to evaluate this type of request based on the perceived financial stability of the tenant. A guarantor may also negotiate for a release of liability upon the sale of the business to a successor with some minimum net worth.

## 4. Relocation and Transition

Transition issues can be critical for the smaller tenant. If the tenant is moving its business out of one leased premises and into another or otherwise is counting on a specific date or timeframe for the move and opening in the new space, the lease needs to contain a commitment by the landlord to deliver the space on the required date. If the landlord fails to do so, the lease needs to specify the consequences. For example, the tenant might have a right to receive two (2) days of free rent for each day of delay. If the delay extends beyond a specified date, the tenant must have the right to terminate the lease, as it cannot not have an indefinite obligation for space that prevents it from committing to another location. Typically, the landlord will not consent to be held liable for any delay in the delivery of possession of the premises and will want a definite carve-out for force majeure events. On the other hand, depending on the amount of work that must be completed prior to delivery, and assuming that all parties are clear on who has the responsibility for each component of the build-out, the landlord may be able to make an estimate on the delivery date that is acceptable to all parties, giving the landlord the leeway it needs and giving the tenant the certainty it needs.

## 5. Disputes

Disputes between a smaller tenant and its landlord can be "David v. Goliath" contests. As a result, the lease should always include a prevailing party attorney's fee clause, which can

help to level the playing field. Attorney's fees provisions are often overlooked in a lease until a potential dispute arises, when each party reads the lease to see if it can recover its attorney's fees from the other party. A smaller tenant may not have the wherewithal to commence litigation against the landlord (even if it is justified in doing so) without the possibility of recovering its expenses. Accordingly, it will be important for the attorney's fees clause to state that attorney's fees are recoverable by the substantially prevailing party whether or not a lawsuit is actually commenced and attorney's fees will be recoverable on appeal. The landlord will want to go a step further, however, and insert a provision that if the tenant goes bankrupt, the landlord can appear in any bankruptcy or insolvency proceeding affecting the premises. The tenant shall pay the landlord's reasonable attorney's fees in that proceeding as well as on appeal. Even if the tenant can recover its attorney fees, a smaller tenant may not be able to outwait the course of normal litigation, if the dispute involves something essential to its business. In such cases, it may be advisable to incorporate alternative dispute resolution provisions incorporated into the lease, allowing the parties to bring disputes to designated mediation or arbitration providers.

## **F. Conclusion**

By nature, Landlord lease forms are biased. Unlike the big tenants, smaller tenants have no hope of using their own lease form. They must ferret out the provisions of the landlord's form that run to the heart of their business and convince the landlord to accommodate their needs. Obviously, the smaller tenant cannot obtain the same lease concessions available to a larger, more creditworthy user. However, by keeping their essential business concerns in the forefront of the lease negotiations, small tenants should be able to achieve leases that meet most of their needs. Landlords benefit from tenants with successful businesses, and will usually agree to lease concessions that are reasonably designed to achieve this mutual goal.