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Landlords and restaurant leases: Each party should have interest in the success of the business - by Dennis Serpone

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Every business, once a location is secured, has to prepare for dealing with a landlord, a build-out, personnel, and then the customers. At the top of this pyramid is the “landlord”...be it an individual or, in many cases, the landlord’s representative.

Ideally there should be a symbiotic relationship between the landlord and the tenant with each party having an undivided interest in the success of the new business.

If you’re a retail landlord, the tenant’s investment is fairly limited...new décor, shelving, bathrooms, and office area.

In the case of leasing to a restaurateur, the investment is significantly higher with extensive high-capacity plumbing and electrical requirements, handicap bathrooms, kitchen equipment and refrigeration, special walls and flooring in the kitchen, ventilation, and constant scrutiny by local health and building inspectors.

Typically, the landlord wants a “triple net” lease...essentially he wants to own the property with the tenant carrying all his operating expenses. This is not an unreasonable business model...in good times.

However, when the economy stumbles as we’ve seen in the last six months, it’s relatively easy for the retail tenant to close his doors and walk away. In the case of the restaurateur, his investment is so significant that, when his operating numbers fall into the red, he typically seeks the cooperation of the landlord when he’s having trouble paying his rent. The landlord at this point is holding all the cards. Subject to the terms of the lease, the landlord could force the tenant to go out of business, take over the location, and re-lease the, now fully equipped restaurant, to another operator. The problem here is that the operator may have invested his life’s savings in this venture and fights to keep his business going, many times to the point of filing a Chapter 11 bankruptcy. The question

that arises is, “isn’t there a better, less confrontational way of avoiding all this animosity?”

Simply put, both tenant and lessor would benefit from being represented by a restaurant real estate broker. Because restaurant leases are so complicated, it takes years of practical experience and an ongoing education to properly negotiate them. The National Restaurant Exchange is both a restaurant and real estate specialist, well aware of these complexities and is uniquely qualified to address and manage the contingencies contained therein.

There are two very distinct actions that the landlord can do to avoid losing the tenant and that the operator can do to avoid going out of business. Both solutions are a function of the steps taken at the very beginning of this journey that the landlord and tenant are taking.

First and foremost, the tenant should engage the advice of a restaurant real estate specialist who can provide an unbiased opinion of the appropriateness of the location for his concept. All too often serious conditions exist which the optimistic lessee can’t see through his rose-colored glasses...many times risking his life’s savings. Conversely, a restaurant specialist can justify to a landlord a tenant’s background and experience and help negotiate the language of a lease that helps ensure that both parties understand the mutual interest each party has in each other. Success of the tenant ensures a peaceful, uneventful stream of income for the landlord.

The fall will see uncooperative landlords losing tenants, vast amounts of shopping center space will go unoccupied, with some restaurateurs who have the financial reserves are talking about hibernating for the Fall and Winter, hopefully reopening in the Spring. National chains are faced with the same problems, just on a larger, wider scale.

Fast food has benefited the most during this pandemic, with bars, pubs, and entertainment venues hurt the most. Financially sound, growth-oriented operators are experiencing the best of times for them to grow their brand by taking advantage of the distress of those not able to survive. The fall will see the erosion of those hurt most by COVID-19 and the growth of the restaurants that have established a competitive advantage.

Over the years, I have assisted hundreds of buyers and sellers entering and exiting this multifaceted industry and have been called upon as an expert witness in helping solve lease disputes.

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