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Retail roulette: The risks and rewards of relocation clauses in commercial leasing by Adam Barnosky

May 26, 2023 - Spotlights



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Given changing economic conditions and shifting consumer trends in the commercial real estate market, developers require flexibility when expanding or modifying retail centers, while tenants seek stability and often invest heavily in a specific location with unique visibility and benefits. This tension has led to more focus and negotiation over relocation clauses in commercial leases in recent years. Despite inherent tensions, well informed parties are usually able to find a reasonable compromise over competing interests implicated by relocation clauses.

A “relocation clause” refers to a lease provision which allows the landlord to relocate the tenant to another location within the building or development in the event of various triggering circumstances, such as building renovations or reconfiguration of the space.

The terms of the lease agreement will govern the parties’ rights and obligations in a relocation scenario. A landlord’s right to relocation, including the rights and responsibilities of both parties, is material and therefore customarily discussed early in negotiation of material lease terms, ideally at the letter of intent stage. Common tenant rights in a relocation clause may include the right to receive compensation for relocation expenses, the right to approve the new location, rent abatement and, less often, the right to terminate the lease

Relocation Benefits and Downsides: There are many reasons why a relocation clause can be of benefit to both the landlord and tenant, including flexibility, cost savings, and mitigation of risk. A relocation clause can provide both parties with the flexibility to adapt to changing circumstances. If the landlord needs to undertake renovations or repairs in the tenant’s current space, a relocation clause can provide a solution that minimizes disruption to the tenant’s business. Relocating to a different space within the same building or complex can be more cost-effective than terminating a lease early and searching for new space elsewhere. Further, a relocation clause can help both parties mitigate risk, by ensuring the parties have some control over how their property is used and can prevent a tenant from occupying a space that does not fit with their overall plans for the property.

While a relocation clause can benefit both parties in certain circumstances, it can also have potential downsides where it does not include mutually agreeable and reasonable terms. For example, a hastily vetted relocation clause can result in a strain on the landlord-tenant relationship, particularly if the relocation disrupts the tenant’s business or creates additional unforeseen expenses for the tenant. The tenant may not want to move to a new location, particularly if they have built up a loyal customer base or if the new location is less visible or less convenient for their customers. Additionally, the cost of relocating a business can be substantial, particularly if the tenant has invested in custom fixtures or improvements to the space. This scenario can have negative consequences for the landlord as well, as developments thrive on stable and profitable tenancies.

Relocation Terms: There are certain terms within a relocation clause which will ensure a balance between flexibility of the landlord and stability for the tenant.

(1) Comparable Space: With a requirement that relocation be to a comparable space (i.e. size, configuration, and location within the building or development), the parties can minimize potential negative impacts as a result of the relocation.

(2) Financial Compensation: A relocation clause can be more palatable where the landlord provides the tenant with compensation to offset the costs of moving and other miscellaneous expenses incurred directly as a result of the relocation;

(3) Advance Notice, Timing and Limitations: A provision can be included which provides a window for relocation within the lease term, a reasonable runway for both parties to plan for the move, a limitation on the number of relocations allowed within the term, and timing to ensure the tenant can continuously operate; and

(4) Improvements and Rent Abatement: A landlord can incentivize relocation options by paying for improvements to the new space and allowing for rent abatement during any down period.

The prevalence of relocation clauses in commercial leases reflects the need for a delicate balance between the flexibility desired by developers and the stability sought by tenants. These clauses provide a means of compromise in an ever-changing market landscape. While relocation clauses offer benefits such as adaptability, cost savings, and risk mitigation, they can also pose challenges if not carefully negotiated.

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