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Landlords and restaurant leases by Dennis Serpone

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Dennis Serpone

Seventy-five percent of all small businesses are food and liquor related.

Every business owner, once a location is secured, has to be prepared 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, his leasing agent.

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 bldg. 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 over the last three years, 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.

However, there are landlords that can't resist taking advantage of every opportunity to make money.

I recently had a very successful Boston restaurant sale in place for over \$2 million. The lease which still had nine years left, was "assumable." The landlord, who owns a lot of Boston-area properties, demanded a \$25,000 payment for assigning the lease. When the tenant refused and threatened to sue the landlord for breach of contract, the landlord said, "Sue me. You may eventually win, but I'll drain a lot more than \$25,000 out of you before it's settled." The tenant paid the ransom.

With a recovering economy, the summer will see uncooperative landlords losing tenants, and vast amounts of shopping center and office space will go unoccupied.

Fast food has benefited the most over the last few years, with bars, pubs, and entertainment venues coming back strong. 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. Beyond the summer, this fall will see the growth of the restaurants that have established a competitive advantage.

Over the past 43 years, I have assisted thousands 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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