

Glissman offers insights on the value of a RE broker in connection with tenant concession negotiations

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Tenants are beginning to feel the pain of business contraction and looking for solutions. The space they don't need and the rents they cannot afford to pay may hinder their continued viability. What services can brokers offer and what services should tenants and landlords ask of their brokers in this environment? This article offers an approach to utilizing the brokers immense market knowledge to find solutions to the dilemma, first from the tenant's perspective and then from the owner's perspective. Consider the following:

Tenants are coming to their landlords seeking rent, space and term relief. Landlords want nothing to do with it given their own problems with loans coming due, rents shrinking and cap rates rising. But, each of these players needs the other and therein lies the crack in the door. When confronted with a tenant's request, the landlord asks itself the following fundamental business questions. Does the tenant and/or its guarantors have sufficient assets to support enforcement of the lease without the need for modification? Does tenant have valid defenses to enforcement? How long will it take to evict tenant and collect or enforce the payment obligations under the lease and at what cost? Assuming there are no meaningful assets to collect from the tenant, how long will it take to lease up the space, at what rate and term, with what concessions and to what type of credit? Finally, what is the net present value of a lease enforcement/relet solution vs. a lease modification with concessions? A real estate broker, acting within the context of its engagement or prospective engagement, can be a powerful resource..

FROM THE TENANT'S PERSPECTIVE

1. Help The Tenant Get Organized. The landlord has no interest in a sob story. It wants hard facts and the smart tenant does its homework before sitting down with its landlord. The tenant should answer all of the above questions before its first words are uttered. As an initial step, tenant and its lawyer need to review the lease file and understand tenant's obligations, eviction defenses, negotiating leverage, eviction and collection timing, litigation costs and asset exposure.
2. Advise The Tenant About The Market. What are the market rents, terms and concessions applicable to this space? If the landlord takes this space back, how long will it take to lease it up, what will the cost in doing that be, and what economic benefit will the landlord obtain from that new deal? Net present value it back to today. What is that deal worth to the landlord in today's dollars?
3. Develop the Concession Strategy. Refer to New England Real Estate Journal Volume 48, Issue 1, January 2-8, 2009 for an article on a number of concession strategies to consider. The essence of a broker's service at this stage is to look at each concession strategy and apply the "can landlord do better than this in the market" test. The analysis must be backed up with hard, independently

verifiable, market facts. If landlord can do better by saying no to the proposal, then the conversation is going to be short. Some concessions to consider include rent abatement or reduction, rent accrual, term reduction, lease termination perhaps with buyout, rent reduction followed by increase later to recoup the loss, improving the lease, improving the collateral behind the lease or behind the rent accrual, equity piece to landlord, draw on security deposit with later replenishment, and others.

4. Consider A Below Market Rate Assignment. What rental terms make this space immediately marketable and attractive? A broker can provide advice on that threshold and define its elements. Under this scenario, broker locates a new tenant at an attractive below market rate (such as an adjoining or nearby user). Tenant assigns the lease to new tenant. Ideally, new tenant assumes the lease as is or with some negotiated rental reduction between landlord and tenant. Then, old tenant executes an agreement behind the scene directly with new tenant pursuant to which old tenant agrees to pay new tenant \$X per month as a rent subsidy. Alternatively, old tenant enters into the same agreement with landlord and pays it directly to landlord and the assigned lease is modified to a reduced rent reflective of the attractive rate. Old tenant ideally is off the hook for the assigned lease, and locked into the rental subsidy amount payable either to the new tenant or directly to the landlord. There are a variety of variations to this approach, many landlord objections, and a good leasing lawyer can provide solutions as the negotiation unfolds.

5. Advocate for the Tenant. Finally, during the early stages of negotiations, before the heat rises and swords are drawn, what better person is there to negotiate a renewal or modification than a deal making broker armed with a well thought out plan representing the tenant backed up by solid market data.

FROM THE LANDLORD'S PERSPECTIVE

1. Owner To Get Organized. Owner, like tenant, needs to do its homework. Owner should obtain an asset search and credit report on the tenant and its guarantors; get owner's attorney to review the lease, guaranty and credit enhancements, and correspondence file; owner to locate eviction counsel to advise on viability of eviction, timing, cost and potential defenses. Owner to set up a checklist and framework for analyzing the viability of enforcing the lease "as is" or negotiating a rent concession and documenting it.

2. Provide landlord with a reality check on market rate tenant availability for that product and marketing time. An owner has to decide what its next best option is. How long will it take to evict the tenant? How long will it take to market and lease up the space and at what rate? Will there be TI, free rent and other concessions required? Owners must know the answer to these questions before they can respond to a tenant's request because at the end of the day, the owner must decide which path provides the better return. Say no and fight or take a hit. A broker can provide the owner with the solid fact based market data it needs to make this decision; information that has great economic value to an owner confronted with these questions. Just framing the analysis for the owner may be of tremendous service. Moreover, under Connecticut law, once an owner serves the notice to quit and starts the eviction, it has a duty to mitigate damages and needs to be going to market asap and documenting a reasonable marketing program. This will require that owner list the property right away and commence marketing.

3. Provide landlord with current rent data for market comparison. A tenant will say "the best you can do if you go to market is X, and therefore, you are better off working with me at that number or less"

and the landlord needs to determine whether that statement is accurate. Working with that tenant on a modification may make sense, and the broker can represent the landlord in those negotiations using market knowledge and an understanding of the tenant's options. "Tenant, we can lease this all day long at X. You are going to have to do better than that before this conversation is going to go anywhere."

4. Provide landlord with a reality check on below market rate tenant availability. When a tenant is in trouble, they may need to reduce their space or walk from it. A landlord faced with a termination request and perhaps a pennies on the dollar buy out offer, may prefer to facilitate a below market sublet or assignment in cooperation with the tenant. This approach is potentially a win win. New user gets a below market rate; departing tenant subsidizes the below market rent bringing it up to the contract or a negotiated rate at a substantial savings to tenant while spreading the cost of that solution over the balance of the term; and landlord keeps the rent stream going at the bargained for rate while expanding the credit on the lease from one troubled tenant to two joint and severally liable credits. A broker has the capacity to put this deal together and can tip the owner off to the viability of this solution.

5. Owners should be reminded that there are other enhancements they can consider in exchange for a rent or space concession. Extend the term; reduce rent now and raise it later to recoup the loss; rewrite the lease to pick up the concessions you made when you put the deal together; collateralize or improve the credit behind the lease; take an equity piece in the tenant; draw the security deposit down and require a phased in replenishment of it; to name a few.

A good broker knows the market, the current rates and concessions and who out there is moving, growing and shrinking. A good broker can take their immense market knowledge and plug it into an analysis matrix that will be invaluable to both parties in finding their way to a solution to a real economic problem. The broker has the skill sets that owners and tenants need to meet the issues confronting them in this market; and that has all the makings of opportunity for everyone involved.

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