

## Commercial leases in today's landlord-slanted market

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Many New York commercial leasing brokers have been waiting to see how the mortgage fallout would affect the market. While many believe that transaction volume may drop, they do not anticipate a decrease in office rents.

Demand for office space is still extremely high throughout Manhattan and there is not enough supply to meet that demand. As a result, landlords are able to maintain an obvious bargaining advantage when it comes to drafting commercial leases.

A commercial lease is simply a contract between two or more parties. When drafting a lease, a landlord's focus should be to obtain the fullest benefit of this agreement under any default scenario. Because of ongoing incredible demand for commercial space in Manhattan, landlords have the opportunity to create a contract from which they can derive maximum monetary returns, and other nonmonetary benefits.

When drafting a lease, the first priority of the landlord's counsel is to fully protect the landlord. A landlord that fails to ensure its interests are protected can easily be saddled with an undesirable tenant. In the event of default, the focus should be to facilitate the expedient reclamation of the leasehold, with as little delay as possible.

For example, commercial lease forms should contain a clause prohibiting counterclaims by a tenant when the landlord has already commenced a summary proceeding to evict.

However, it is also important that landlords not implement excessive penalties and late fees. Any damages imposed upon the tenant must bear a relation to the harm that may have been caused.

Another important guideline is to avoid ambiguity, leaving no room for interpretation. Today's leases should use plain language with concrete terms and should not contain clauses that a court would have any difficulty interpreting. This can lead to conflict, which can ultimately erode the advantages that a landlord has already obtained by way of superior bargaining power.

For example, we recently encountered a case where the lease provision relating to common area maintenance (CAM) detailed each item that was to be allocated to CAM and each item that was to be charged to the tenant. Despite this attempt at all-inclusiveness, this clause was poorly drafted because it left too much room for the tenant to challenge the landlord's calculation.

It is also more difficult to prove the validity of a dollar amount derived from multiple sources outside of the lease. Landlords can avoid such a pitfall by incorporating a flat rate for CAM, as



stated in the lease.

With demand remaining high for commercial space throughout the city, landlords are also able to negotiate substantial rents.

These rates, of course, are detailed in rent schedules that cover the lease

term, and the landlord should attempt to forecast market rates accordingly.

The lease will also include "additional rent," or fees that are collectible within the framework of a summary nonpayment proceeding.

Additional rent items can include common charges, late fees, utilities, and real estate tax escalation charges, which permit a landlord to pass along a prorated share of annual taxes assessed on the building. With regard to utilities, it is generally advisable that landlords have tenants billed directly for electric, water, and the like, to prevent delinquencies from the tenant.

This, like the CAM issue mentioned earlier, relates to provability because

utility charges are harder to confirm in court than numbers that are derived from the lease itself.

Provisions in the lease should explicitly state when the landlord has the right to terminate the tenant's lease prior to the expiration of its term.

The governing principles should be clarity and expedient reclamation of the leasehold.

A good default provision provides a mechanism that will permit the landlord to quickly and conclusively prove that the tenant has violated the terms of the lease and is subject to eviction. As a final recourse, the landlord should be able to pursue the commercial tenant's principal for any monies due.

Guarantors are commonplace in commercial leases and give the landlord "teeth" in the collection of arrears or damages arising from a lease violation.

A common and valuable lease clause with New York landlords relates to demolition. Demolition clauses offer landlords the ability to reclaim the leasehold upon reasonable notice, which is typically six months, in order to engage in the substantial renovation or demolition of a building.

Properly drafted clauses are extremely attractive to developers that can purchase the building and serve termination notices rather than resorting to

expensive buyouts of tenants with long lease terms.

Overall, landlords are finding themselves in a very good position in today's market.

But many are concerned that changes in the credit market or a shift in economic confidence could affect their ability to dictate leasing terms.

Experts are saying that finance entities will continue to sit tight with current office spaces until the subprime crisis cools — demand may have peaked in this premium sector.

However, a credit crunch could, in

fact, benefit some landlords if developers find it difficult to secure loans and development slows. In this scenario, potential lessees would be forced to make due with the existing space, while demand for the existing space will increase.

Consequently, increases in lending rates could help preserve the status quo for New York landlords.

So long as there is limited supply of commercial space in New York, landlords can expect to find tenants that will grant them favorable lease terms on all accounts. ■

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