

## News from our Real Estate Group

# In this Market—it is More Important than Ever to Assess Your Lease

For most companies, lease-related costs are the largest expense after payroll. Yet most companies fail to focus time or energy reviewing their leases to assess possible strategies and options until the last year of the lease term. The current economy highlights the importance of reassessing your lease position on a regular basis for possible cost-saving opportunities. Some questions to consider:

- ▶ How does our rent compare to market rents and is there a means of reducing our rent?
- ▶ Is it time to expand or contract our space?
- ▶ Do we want to move to another location or consolidate our operations under one roof?
- ▶ If we are amending our lease, are there any opportunities to correct or update our lease to save us money or reduce our risk?

### Opportunities for Tenants:

**1. Rent Renegotiation.** As a result of the downturn in the market, many tenants are paying above-market lease rates. Landlords are motivated to retain tenants and creative deals are being struck long before lease terms are set to expire.

**2. Expansion and Rent Reduction.** Generally speaking, landlords are sitting on too much empty space in their buildings and are highly motivated to fill that space. If your company needs to expand, many landlords will reduce the rental rate on your

existing space in order to entice you to add square footage to your space. An expanding tenant may even be able to receive the additional space for an initial period of free rent.

**3. Extension and Rent Reduction.** A common lease renegotiation strategy is the so-called “blend and extend.” In these deals, time is added to an existing lease (usually with one to two years remaining on the term, but it could be more) in exchange for a lower rental rate which goes into effect immediately. In some cases, tenants are able to give back unwanted space or receive free rent (which is often—but not always—given in deals when the space is expanded).

**4. Revisiting the “Base Year.”** When a lease is amended, the “base year” for operating expenses and real estate taxes is often reset to a more current year, which may reduce the annual escalations in operating expenses and real estate taxes that are typically passed through to tenants. This could be particularly meaningful for tenants with a base year earlier than 2007. Many buildings were sold before or during 2007, when commercial real estate values were at their peak. In most jurisdictions, those sales triggered increased tax assessments which in turn are producing unusually high annual escalations in real estate taxes. Resetting the base year to a more current year could therefore significantly reduce the real estate tax pass-throughs.

**5. Relocation and Consolidation.** In some cases, landlords will assume a tenant’s

existing lease obligations at a current location (typically if there is no more than a year left on the current lease) in order to lure the tenant to their building—at lower rental rates. This is potentially very attractive if a tenant is looking to consolidate several leases into one location, particularly where the leases have different expiration dates.

### Remember: it is a process

Regardless of your particular leasing goals, always start your lease negotiations as early as possible. The leasing of space is a process which takes time, particularly if tenant improvements must be constructed or there are specific criteria that are important to the tenant (like access to client or customer populations, open floor plans or specific infrastructure requirements). As important, if you run out of time, you run

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out of leverage. With the market in commercial real estate continuing to decline, there is wide disparity among landlords as to the concessions they are willing to offer and how creative they are willing to be. The more time you allow yourself, the more opportunity you will have to find the right landlord, the right location and the right mix of concessions.

### **Purpose**

This *Alert* is intended to provide a snapshot of current leasing trends and give you practical tips for making the best leasing decisions possible. All lease documents, whether new leases or lease amendments should be reviewed by your real estate counsel.

If you would like to discuss these issues further and/or have questions about this *Alert*, please contact one of the attorneys listed above. ■