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TO RENEW OR NOT TO RENEW, VOLUME II - THE MAGNUM LEASE

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PREFACE

This article has been written as a follow up to our original article "To Renew or Not to Renew". The first article specifically addressed a hypothetical lease of 10,000 RSF. This article has been prepared to address many of the additional complexities that arise in a much larger transaction.

The authors of this article debated whether or not this article should be a series (i.e., requiring the reader to read the original "To Renew or Not to Renew" in order for this article to be complete) or independent (i.e., can it stand on its own

merits). We finally concluded that the two articles should have the ability to stand on their own. As a result, many of the concepts set forth in the original "To Renew or Not to Renew" are set forth in this article because they apply equally to a 10,000 RSF or a 100,000 RSF lease. We apologize for this redundancy but in the final analysis we believed this to be the best approach.

INTRODUCTION

Each and every executive responsible for decisions concerning real estate will at some point face the decision of whether to renew an existing lease or to consider a new lease

and location. As a general rule, the larger the transaction the more complex. When the transaction is a Magnum Lease it is by its very nature complex. What do we mean by a Magnum Lease? A Magnum Lease is a lease that is very important to you and your organization notwithstanding the size of your organization. This importance could be based on location, image, or economics. In some circumstances, a Magnum Lease could be a 5,000 RSF transaction but in most circumstances a Magnum Lease will be substantially larger. We have assumed that for most companies a lease of 100,000 RSF would be considered a Magnum Lease. The 100,000 RSF lease transaction is in fact rare; however, many of you will be called upon to one-day handle a transaction of substantially similar size or its equivalent to your organization.

In some situations the decision is simple. You enjoy a great location; your employees are attracted to your organization in part because of your location and its amenities; your relationship with the Landlord is good; truly viable alternative sites are limited and the rent is reasonable. Is there any good reason why you should do anything but renew? All that needs to be worked out is this pesky little thing called rent. In other circumstances the decision to relocate is simple, since the current building no longer meets the needs of your organization nor does it fit the activity to be conducted from the Building. In still other situations, the path to the Promised Land is more troubled and not as clear as we would prefer. Your current building meets your requirements but superior product is available, the location is good but so is the location of other viable alternatives, the rent is reasonable but perhaps superior economic terms are available.

This article has been written to provide some guidance in the event the “*stay in place*” scenario is indeed a viable option and the primary obstacle to renewal is agreement on *rent*. This decision will involve an analysis of your leverage with your current Landlord and your leverage in the market.

To a substantial degree the tenant’s leverage will vary with: (a) the real estate market; (b) your organization’s needs; and (c) its approach to the renewal process. This article has been prepared to assist the sophisticated businessmen in the analysis of the age-old question: "To Renew or Not to Renew, - **The Magnum Lease?**"

For your ease of review we have defined some terms. "Landlord" is your current landlord; "landlord" means any landlord which may include your Landlord; "Tenant" means you; "tenant" means any tenant which may include you; "Building" means the current building that you occupy and "building" means any alternative but suitable building; "Windfall" means the financial difference by and between Tenant staying in place and Landlord obtaining a new tenant.

Good News, Bad News

As a 100,000 RSF Tenant there is some good news and bad news. First, the good news is that you will have significant leverage in most marketplaces. Secondly, the bad news is that your available options will decrease significantly in most marketplaces. Third, moving a 100,000 RSF business operation requires professional assistance and can rarely be accomplished exclusively with your current in-house resources. Fourth, a relocation of this nature will have a significant impact on the productivity of the organization located at this site.

Assumptions

In the immortal words of the famous real estate philosopher Hacking Henry Hardpan "**it appears that some real estate leases are more equal than others**". Since none of us would ever dare question the inscrutable logic of handsome Hardpan we have assumed certain parameters for this hypothetical lease of a 100,000 RSF.

Since each real estate transaction is unique, in order to provide any useful discussion we have attempted to set some parameters that will address many of the issues where execution of a lease transaction –renewal or new lease– is the ultimate goal/solution (i.e., purchase or other alternatives are not desired). Even with this finite scenario the variables are limitless but for the purpose of this discussion we have intentionally limited the variables.

Preliminary Facts -- to this 100,000 RSF Leases

In General:

- (a) There exist viable market alternatives although some of the alternatives will be viewed unfavorably by some of your employees and management (e.g., location and image);
- (b) The organization is in fact willing to relocate;
- (c) You are a good tenant and the Landlord desires to keep you in place;
- (d) You are a sophisticated executive but your department has its hands full with current day to day requirements;
- (e) You have the support of your senior management;
- (f) The market is a semi-hot market (that is, if you were to vacate the Landlord will have to look for a replacement tenant but should be able to locate another viable tenant without unacceptable downtime for the space);
- (g) The vacancy factor in acceptable alternative locations is about 12% and we anticipate that the Tenant will have a minimum of six (6) options, all in acceptable buildings and locations;
- (h) Historically, if you stay in place you can expect very few requests for upgrades to many of your existing systems like telecommunications, information systems, furniture, fixtures and equipment. On the other hand, when a move

does take place the requests for upgrades in all these areas have averaged \$25.00 RSF. Since whether or not these costs are actually expended is not directly tied to relocation we have assumed a cost of \$25.00 RSF in both circumstances;

- (i) Your current space is in a Class A Building that contains 275,000 RSF of office space;
- (j) You have engaged a top of the line broker that exclusively represents the end users of real estate on a preliminary basis. This preliminary retention is currently limited to the sole purpose of providing you a preliminary market survey and financial analysis; and
- (k) You have engaged an experienced real estate leasing lawyer.

In Specific:

- (a) Employee parking is plentiful and not an issue, visitor parking is less than desirable;
- (b) Senior management and the property manager have a very good relationship and on occasion play golf together;
- (c) The Building has changed hands twice in the last ten (10) years, most recently one (1) year ago;
- (d) Your current Landlord is a large real estate firm that represents both landlords and tenants alike;
- (e) The current lease document was negotiated more than ten (10) years ago and the lease has been amended five (5) times by the preeminent real estate leasing guru Emmett Eye Maidauhmistake, Esq.; you have signed three estoppel certificates but you noticed that your predecessor has been somewhat negligent in obtaining non-disturbance, subordination and attornment agreements from the new owners/lenders. Emmett is currently on medical leave and is at home recovering from a quadruple lobotomy, which is rumored to have improved his IQ 20 points. Although Emmett is available for comment you have determined to forego his input and seek other representation;
- (f) Your organization restructured about three (3) years ago and although such reorganization did not require the Landlord's consent the Lease does require written notification to the Landlord. Upon review of the files you are unable to find any record of this notice. Additionally, as part of this reorganization your company changed its name, all invoices from Landlord are submitted in the old corporations name but paid for under the new name;
- (g) You are currently paying \$2.00/RSF per month;
- (h) You are the largest tenant in the Building and expansion space is limited;
- (i) The Lease contains a hold over provision, which provides that in the event you hold over, your rent increases to 200% of the then current rent –your lawyer and broker were asleep during this part of the negotiation–[we will ignore my recent article on this subject];
- (j) The Lease does contain a renewal option (see “Existing Lease - Option” below);
- (k) You have thirty (30) months left on the current term of this Lease;
- (l) When the original lease was executed you were a

60,000 RSF Tenant but during the initial term you have taken additional space three times and you now lease approximately 100,000 RSF; and

- (m) The expansion options in the Lease contain a fair market rental rate formula that provides credit for all market tenant concessions and although one expansion was accomplished per an option the other two expansions were negotiated by your steadfast loyal and erudite broker, Honest Ernest. Unfortunately Honest is also in the hospital. As with most brokers his personal generosity knows no bounds and Honest has donated 70% of his brain to science (IQ went up 35 points after the removal operation). Alas, he is currently unavailable as he has determined to forego his real estate career and seek political office. He has hired Baghdad Bob as his campaign manager and things are looking very good for Senator Honest Ernest—is that an oxymoron—?

Recent Developments:

You have requested a proposal for renewal from the Landlord but he has yet to put anything in writing. The Landlord has also questioned why are you commencing this process so early? He has stated: “We have thirty (30) months left on our term, what is the rush”? However, he has verbally discussed the following terms for a renewal:

- Base Rent of \$2.40/RSF;
- \$10.00/USF improvement allowance;
- Expansion option is available but non-contiguous in the Building; and
- Although you have requested a hold over of ninety (90) days without increase in rent the Landlord has refused this request however he has promised to be flexible: “If we are making good progress and negotiating in good faith I am sure something can be worked out –trust me–”.

Existing Lease - Option

The Lease contains two, five-year options to extend the term of the Lease;

The basic terms of the option are as follows:

- Must be exercised in writing;
- It cannot be exercised earlier than eighteen (18) months but no later than twelve (12) months prior to the expiration of the then current term. Once exercised it is a must take, the fair market rental rate is the only unresolved matter and it is subject to arbitration. The Base Rent during the option term is to be the fair market rental rate, which includes all market concessions then available for like space in the market. Note, although often these market concessions are diluted by limiting the tenant improvement dollars and sans of brokerage fees, we have assumed that market concessions have not been diluted –your broker Honest and attorney Emmett were awake during this part of the

negotiation-. Once the option is exercised the Landlord and the Tenant are bound and any dispute as to fair market rental rate will be resolved via a fair and detailed arbitration provision under the auspices of the American Arbitration Association.

The Current Market Rates for Like Type Space

Your Broker's initial market survey has produced the initial non-negotiated results:

- ❑ \$2.20-2.40/RSF; and
- ❑ The Tenant Improvement Allowances available in the market average from \$30.00 - 35.00 per USF/RSF (includes all allowances). Other potential landlords have proposed "turnkey" tenant improvements.

Preliminary Facts in the Tenant's Favor

Time. Probably the single most important factor! Without the time necessary to find, negotiate and make the new space ready for occupancy the Tenant will be at a significant disadvantage in any renewal or new lease negotiations. The Landlord knows that an alternative lease of this magnitude could take anywhere from 6 to 24 months to locate, negotiate, memorialize and make ready for occupancy. The time variance is dependent upon the condition of the alternative space and the usefulness of its current configuration for your use. This hypothetical scenario has time on your side. The Tenant has exactly twelve (12) months to determine whether or not the Tenant desires to negotiate with his/her current Landlord, negotiate a new lease with another landlord or exercise the option as stated in the Lease.

Size. 100,000 RSF tenants are not a plethora; leases of this magnitude are rare.

Preliminary Facts in Landlord's Favor

- The locating, negotiating and moving of a 100,000 RSF tenant is very complex;
- Any relocation will be very expensive to Tenant in time, energy and money;
- Remodeling to your existing space can as a general rule be accomplished more economically than preparing new space for your use; and
- You are already in his Building and you will have to take some affirmative action to relocate.

I Have an Option, Why Not Exercise it?

Our personal experience is that renewal options are very seldom exercised as stated in leases. The larger the lease transaction the less likely the renewal option will be exercised. During the term of the lease most tenants discover things that need to be addressed in a renewal. Extension

options by their very nature assume that all other terms, covenants and conditions of the existing lease and the building are just fine as - is. As a result, although lawyers and brokers spend a lot of time negotiating extension options and expansion options, they are seldom actually exercised as set forth in the lease. There is generally some give and take during the renewal or expansion process. The older the lease form the more likely many of the terms, covenants and conditions of the options need to be revisited. In this case, our Lease is seasoned by not ancient. The level of sophistication during its creation will dictate its current viability. You might ask why is this the case; I hired the best leasing lawyer and broker on the entire planet? The answer is simple; seldom do things stay static. What was true and good ten (10) years ago may not be so true and good today. The options to extend and expand as a general rule leave the Lease in its initial, undisturbed position which may not be desirable from the Landlord's or the Tenant's perspective.

When are options most likely to be exercised? Our experience has shown that most of the time renewal options are exercised when: (a) the rent is specifically stated in the lease and it is perceived to be below or very close to market by the tenant; (b) there are very few viable alternatives in the market—you have to be in a location and there are only one or two buildings that can possibly meet your needs—; (c) the tenant fails to timely commence the renewal process and must make a decision as to the renewal option before he has had a fair opportunity to test the market; (d) the renewal process was botched and the tenant has lost its leverage early in the process. Although we have no scientific evidence, it is our opinion that (c) and (d) above; are the primary reasons renewals are accomplished per the pre-existing provisions of a lease.

As stated earlier we have assumed that your lawyer did an excellent job of negotiating a well thought out, very detailed and apparently fair arbitration provision. The sole purpose of this arbitration provision is to determine the rent that would apply during the renewal term. The best of the arbitration agreements or provisions contain a very detailed formula, setting forth exactly what is to be considered and what is not to be considered in determining the fair market rental rate.

We respectfully submit for your consideration the question: whom do you want determining your rent? In this case you have a choice to make. You can choose to utilize the inherent economic forces available in a free enterprise system or you can choose to exercise the renewal option in the Lease.

Renewal options in leases generally contain a mechanism for determining the fair market rental rate. This mechanism is generally set forth in an arbitration agreement or provision.

What is arbitration? When all is said and done arbitration is nothing more and nothing less than an alternative form of

dispute resolution. Although many very erudite, sophisticated real estate professionals would opine that arbitration is not litigation, I would submit to you a slightly different view. What is litigation, other than a fight, a civilized method to resolve a disagreement by and between parties? Is not arbitration, just another form of fight with slightly different rules? To further illustrate my point, I am an advocate of arbitration in lieu of litigation, mediation in lieu of arbitration and a stronger advocate of negotiation in lieu of mediation.

In the objective sense you must ask yourself what rent do you want to pay? The best rent available or the fair market rental rate? In either case what is the best mechanism for determining the most accurate fair market or best rental rate: (a) a cadre of lawyers, appraisers and brokers debating amongst each other, trying to compare apples to apples and oranges to apples and apples to kiwi's; or (b) the competitive market forces of the free enterprise system?

To further illustrate this point let's take a minute to discuss some of the most common fair market rental rate mechanisms set forth in leases.

First, the baseball type mechanism, which somewhat mirror images the process used in determining the salary of a baseball player –we all know how well that has worked–. This process basically consists of the landlord and the tenant submitting their individual best estimates of fair market rental rate to the arbitrator and or the arbitration panel. The arbitrator/arbitration panel has one task, that is to select either the landlord's or the tenant's submittal as the closest to fair market rental rate. Another common approach is the averaging approach. In this approach landlord and the tenant each submit their individual best estimates of fair market rental rate to the arbitrator/arbitration panel and the arbitrator/arbitration panel takes the rates and performs an averaging exercise within certain specified guidelines. Still another common approach is for arbitrator/arbitration panel to actually determine the fair market rental rate. In this approach landlord and the tenant submit their individual best estimates of fair market rental rate to the arbitrator/arbitration panel, but the arbitrator/arbitration panel is not bound to use either one and is free to develop his/her own fair market rental rate based on all the information submitted to the arbitrator/arbitration panel as part of this process.

If we are to define fair market rental rate as, “the rental rate a landlord that is not under any compulsion to lease and a tenant that is not any compulsion to lease would pay,” then we respectfully submit that none of the above arbitration mechanisms for determining fair market rental rate is likely to produce an accurate fair market rental rate, let alone the best market rent available!

It is our supposition that the only true test of what is the fair

market rental rate, is the use of inherently dynamic free market forces systematically exploited to identify the best rent available in the market. Any process sans of bringing these true market forces to bear, just cannot accurately produce a valid fair market rental rate. You say: “Wait a minute, will not the landlord and the tenant seek top of the line experienced professionals to produce an accurate fair market rental rate! If we hire the best in the industry won't this produce a true fair market rental rate? I hired the best real estate lawyer in the history of mankind, this lease is 250 pages long with 16 exhibits and now you tell me it's broke?” First, we will make the modest assumption that your lease contains a truly divinity inspired provision and is not only the best fair market rental rate formula in the U.S.A but the best in the entire galaxy. Secondly, let's further assume that you are able to find alternative landlords who are so terminally ignorant as to put their best deal on the table without any negotiation whatsoever and without any real hope of consummating a real deal. Then in such circumstance, yes, there is no need to employ a renewal strategy.

As any broker worth his salt will tell you, often the initial numbers presented in response to an RFP are negotiated downward for the benefit of the tenant. This being the case how can a true and viable fair market rental rate be established via arbitration?

Best Rent Available in the Market

Here are some things to consider when or prior to initiating arbitration for the determination of fair market rental rate. **First**, it is our opinion that arbitrated fair market rental rates are at best likely to produce a historical presentation of fair market rental rate (what was done, what is known and not what can be done). You must always remember we just don't know what we don't know. The best of the best of the appraisers and brokers are able to wax eloquently on what they **believe** is the fair market rental rate. Notwithstanding their innate brilliance, why do like skilled appraisers and brokers so often differ substantially in their determinations of fair market rental rate? Aren't all these professionals examining the same information? If they are applying the same tried and true scientific formulas how can their results differ so? After all if they didn't differ, arbitration would not be necessary in the first instance! Put simply it is their opinion and not a true test of what the market will bear!

Secondly, as the Tenant, do you desire a fair market rental rate or do you desire the best rental rate available? As the Tenant, do we really care if the Landlord must offer us a rate below the market in order to have us remain in his building? Does not a wise tenant take advantage of a bargain rental rate? As the Tenant, do we really care if the Landlord feels compelled by the current market forces to offer us a very low rate?

Third, the entire process of finding and analyzing comparables is extremely difficult. Each building and location is unique. The language we often find in leases is predicated upon finding comparable buildings, comparable locations, comparable landlords, comparable services, comparable ambience, etc. Assuming for a minute that the professionals can agree on what is comparable, isn't real estate unique? I am sure that duplicate or clone buildings exist but in my experience I have yet to see a matching set. Although comparable, they are in fact unique and determining proper adjustments to each such considered location and the proper application of these adjustments is much more of an art than a science.

Anyone with some significant years of real estate experience has had the joy of reading a fair market rental rate evaluation/appraisal where the art was plentiful and the science thin. Often when you view the landlord's and the tenant's appraisals many of the same buildings were analyzed as comparable buildings. Yet the appraisers differ greatly as to their adjustments. One appraiser will rate your building as superior in quality and adjust the rent accordingly and the other appraiser will view your building as inferior and adjust the rent accordingly. Who is right? Who is wrong? This is difficult to determine and may be impossible to conclude accurately one way or the other. Even Solomon would find this challenge as requiring a major Advil solution.

Last but not the least, of the reasons to seek market verification of the fair market rental rate is “**control**”. As the person responsible for real estate it is essential that you retain control over the process. I cannot think of a better and faster way to lose control of the entire process than to submit the determination of fair market rental rate to lawyers or brokers (acting as consultants) and appraisers. Relinquishing the process to such professionals is risky business at best. You ask why do you say this? Both sides to this arbitration will be attempting to hire the best of the best for this arbitration. Try finding a fully competent and qualified broker or appraiser that truly does not have some sort of conflict of interest is indeed difficult. The best of the best work all over town and purity is indeed rare in these circumstances. Let's assume that you are able to obtain the best without any conflict whatsoever! Next you have to consider that the best will be submitting their perfectly drafted and absolutely compelling, flawless and erudite opinions that any individual with a mere modicum of IQ will clearly understand to your favor! Oops, wait a minute isn't this individual known as a “neutral” and will not he/she be receiving equally well crafted documents etc., from the other side? Under such a scenario who has control, the lawyers, brokers, consultants, the neutral or you? I am not sure who has control but I would respectfully suggest probably not you!

Discussion of the Financial Analyses

Often Tenant's initiate the renewal process by contact with the Landlord. Sometimes this is accomplished verbally or on more a formal written basis (by adhering to the Renewal Option process set forth in the Lease). As a general rule, landlords initiate this contact but this is certainly not 100%. Landlords tend to initiate this process at the point of no return for the tenant (adequate time no longer exists for the tenant to canvass the market for suitable alternative locations). We would respectfully submit that in either circumstance this is absolutely the wrong way to commence a lease renewal process. In the vast majority of renewal situations the decision as to whether or not a Tenant stays in place or relocates is primarily a financial decision. To enter into economic discussions unprepared can lead to unjustified expectations for both parties. It is our recommendation that you enter such discussions only after you have taken the time and made the effort to be well prepared. The best way to be prepared is to know the market and the economics available prior to any discussions with your Landlord.

Depending on the size of a company it is rare that you will see the senior management become involved in the finances of a non-Magnum Lease. At the other end of the scale, it is indeed rare when senior management is not involved in a Magnum Lease. Often the CEO of the company is intimately involved in the entire process. Deals of this magnitude have an immediate and sustained impact on their bottom line and you can rest assured that many eyes will be on this transaction.

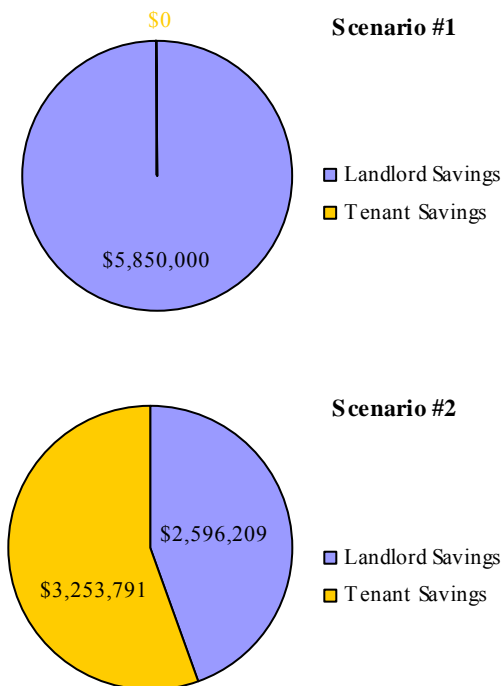
Attached we have provided six (6) financial pro-formas. The first pro-forma is from the Landlord's perspective and contains Scenarios #1 and #2. The second pro-forma is from the Tenant's perspective and contains scenarios #2, #3, #4, #5 and #6. Each scenario discusses one particular hypothetical and the potential financial implications of each to the Landlord and the Tenant. The astute businessman fully understands that he/she must know the financial aspects of renewal from both his/her and the Landlord's perspective. It is true that we could provide ten additional scenarios and still not cover your particular circumstance but we are confident that the financial matrix used in this analysis can be quickly modified to adequately address your unique needs and circumstances.

FINANCIAL ANALYSIS **

Landlord Income Analysis-100,000 RSF – Pro Forma I

Scenario #1 A New Tenant @ \$2.50/RSF vs. a Renewal @ \$2.50/RSF, will display a Windfall savings to the **Landlord** in the amount of **\$5,850,000** if the Landlord can convince you to renew @ \$2.50/RSF.

Scenario #2 A New Tenant @ \$2.50/RSF vs. Renewal @ \$2.00/RSF, displays a savings of **\$2,596,209** to the **Landlord**, if you renew @ \$2.00/RSF.



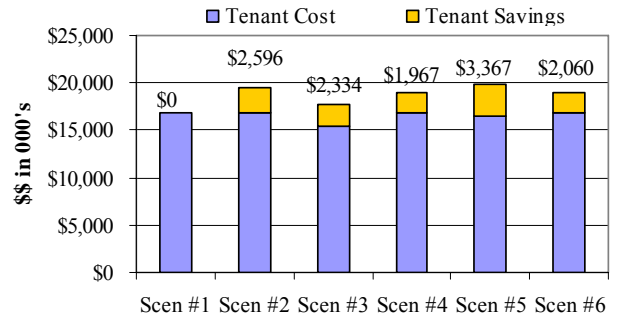
Tenant Savings Analysis-100,000 RSF – Pro Forma II

Scenario #3 Tenant Renews @ \$2.50/RSF vs. Renewal @ \$2.00/RSF, displays a savings of **\$2,333,791** to the **Tenant**, if you renew @ \$2.00/RSF.

Scenario #4 Tenant Relocates @ \$2.50/RSF vs. Renews @ \$2.50/RSF, displays a savings to **Tenant** of **\$1,966,758** to renew @ \$2.50/RSF.

Scenario #5. Tenant Relocates @ \$2.50/RSF vs. Renews @ \$2.00/RSF, displays a savings to the **Tenant** of **\$3,367,033**, if Tenant renews @ \$2.00/RSF.

Scenario #6, Tenant Exercises Option vs. Relocates @ \$2.40/RSF, displays a savings to Tenant of **\$2,060,110**, if Tenant renews @ \$2.40/RSF.



What is a fair objective? The simple answer again is it depends on a lot of things. Let us provide six possible views:

- ❖ Tenant Aggressive - Tenant should achieve 80% + of the Landlord's Windfall in Scenario #1.
- ❖ Upper Position - Tenant and Landlord should share 60/40 of the Landlord's Windfall in Scenario #1.
- ❖ Upper Middle Position - Tenant and Landlord should share 50/50 of the Landlord's Windfall in Scenario #1
- ❖ Middle Position - Add the Landlord's Windfall in Scenario #1 to Tenant's savings in Scenario #3 and split the savings 50/50.
- ❖ Lower Position - Add the Landlord's Windfall on Scenario #1 to the Tenant's savings in Scenario #4 and split the savings 50/50.
- ❖ Still Lower Position - achieve any deal better than exercising of the Option.

Your objectives in the final analysis will be a direct product of your needs and your willingness to accept risk. As with all things, the higher the risk the greater the potential reward. The higher the objective the greater the need to retain an experienced, dedicated and a qualified team of professionals to represent you!

Unknowns or at Least Difficult to Ascertain with Accuracy - How Motivated is the Landlord to Keep You in Place?

In our hypothetical deal we are in a semi-hot market but 100,000 RSF tenants are not readily available in the marketplace. As you can see from the above financial analyses if you determine to move you will in fact have a significant financial impact on this Building. Barring Landlord having a ready, able and willing tenant to take your space, either a new tenant or through options granted to another tenant in the Building, the Landlord will generally desire to keep you right in place paying rent in a timely and undisturbed fashion.

Leverage - How to Obtain It / How to Retain It

It is important to understand that without the acquisition and retention of leverage any real estate negotiations are merely an exercise in pure frustration. As with all real estate transactions the first order of priority is: (a) find locations; (b)

qualify locations; (c) obtain leverage; (d) retain leverage; (e) use leverage and (f) obtain location. Let's see if we can simplify the later part of this formula:

Leverage Obtained + Leverage Retained + Leverage Used Properly = Pretty Good Deal.

In a renewal scenario, leverage is not easy to obtain nor is it easy to retain and even more difficult to use properly in a timely fashion. The use of leverage must be conducted in accordance with a systematic plan. Leverage can be lost by a mere inadvertent communication and once it is lost, leverage is not easily regained. If we fail to obtain this precious commodity all of our attempts at maximizing corporate profit will be for the most part futile. A team of competent real estate professionals who will prepare a unique real estate strategy and execute that strategy with discreet negotiation tactics can best accomplish the obtaining and retention of leverage. This process is intended to obtain the best deal possible, satisfy all your objectives, all while maintaining control of the entire process. It will be much easier to exercise your leverage by now placing the Landlord in the market for a 100,000 RSF tenant. The key to making the Landlord the marketeer (new word we made it up) is convincing the Landlord that you are leaving.

Leverage Obtained

As any astute Landlord knows, tenants do not grow on trees, good tenants are well sought after and quality 100,000 RSF tenants may be on the endangered species list. A Tenant that is in need of 100,000 RSF of office space is by definition something that demands attention in most marketplaces. What does this mean for leverage? Basically it means that as a general rule a tenant with a Magnum Lease need has some significant leverage in the marketplace. The acquisition of leverage does not mean that you are invincible and can't lose it or that it is absolute as to all issues. What it does mean is that at least initially you have the upper hand. We have yet to see a real estate transaction where one party has absolute leverage on every issue raised or has been able to retain the upper hand throughout the entire negotiation process. There are just some issues that notwithstanding our strong position the landlord simply cannot or will not concede and vice versa.

Your need will have an immediate impact on the marketplace and if landlord A cannot provide you with what you need, landlord B might. Also, the landlords that have been invited to propose will generally do so and others that have not been invited to propose will be contacting you, your broker, your attorney, your space planner, your next of kin, all for the purpose of obtaining an opportunity to propose. You have obtained instant popularity and all without going to the gym or having plastic surgery!

Leverage Retained

The second part of this formula is the retention of leverage.

Leverage can only be maintained as long as preference is not perceived and commitment is not made. Don't waste leverage on non-substantive business or legal issues! Understanding when and where you have leverage is critical.

More importantly when and how to use leverage is absolutely essential to a well-negotiated deal. The longer your prospective landlords are at the table the more likely you will discover their true bottom line. Concede slowly, systematically, even on non-substantive issues.

Leverage Used Properly

Well now we have more or less established that we have leverage and we are assuming that you have retained it, now what do we do with it? The answer is simple, we: (a) cherish it; (b) safeguard it; and (c) most importantly use it properly. In order to fully comprehend our leverage we simply must understand all financial and legal aspects of the proposed transaction. The first task is to gain a thorough understanding of the financial implications of the Landlord's initial offer versus what is perceived to be available in the market. Any tenant that enters into a negotiation with the Landlord without fully evaluating the financial aspects of renewal is entering the negotiation either: (a) unprepared for success; or (b) well prepared for failure.

In order to use leverage properly we must identify our objectives and develop a strategy to obtain what is important, concede what is not (slowly) and focus on the majors. As a 100,000 RSF user you will more than likely be asking for terms, covenants and conditions that may require owner, investor or financier approval. No matter our leverage we simply will not have leverage on each and every issue.

Forgive our digression into an old war story but it is simply the best example of leverage improperly used that I am aware of. I was once part of a scheduled three (3) day negotiation session for a Magnum Lease. The theory was simple we were to meet in NY, and nobody was to leave until our deal was complete. This deal was so important to our client that the company CFO was part of our negotiation team. We arrived at our destination with the intent on spending as much time as necessary to complete the deal. Are instructions from the CEO was not to leave town until the deal was done.

Day One - In the a.m. of the first day we met with our team in a conference room. We specifically outlined each issue and our desired strategy to obtaining the desired changes in the draft lease (NY lease with some very harsh landlord language). We also agreed on a very simple strategy; address minor issues, get by them, build a spirit of cooperation, then move on to the heavy items. Our thoughts were to systematically concede some of the minors before we hit the heavy issues. We outlined what we thought could be major problems from the landlord's perspective and identified potential concessions, compromises and strategies to achieve our goals. Our perception was that most of these issues were

not critical to our side but could be very important to the landlord.

Day One - In the early afternoon we commenced our negotiation session with the landlord. Much to our surprise our client took the list of the issues we perceived as substantially important to the landlord and put it on the table immediately in front of the landlord. The CFO then announced that he was in a hurry to finalize this deal, had no time for the nonsense of a long drawn out negotiation and wanted to move onto other more pressing matters. He also went on to state that he was conceding all these points to the landlord, so the landlord would quickly concede the issues he wanted and we could finalize this lease today. Our client's intent was noble; he/she wanted to make this deal quickly and did not desire to spend a lot of time on insubstantial issues that were of little to no importance to him/her. His/her intent was to move this deal right along and not waste time negotiating the normal give and take scenario. What he/she misjudged is that our opponents were in no hurry to make the deal. When our client was through conceding all of the perceived substantial deal elements, the landlord team requested an immediate adjournment so they could discuss. As I viewed our opponent's demeanor they genuinely appeared to be in shock. Our client was dismayed and was hoping to receive some immediate gratification for his/her self perceived brilliant Napoleonic like move. Perplexed he/she

Any tenant that enters into a negotiation with the Landlord without fully evaluating the financial aspects of renewal is entering the negotiation fully: (a) unprepared for success; or (b) well prepared for failure!

was, as immediate concessions did not come from the landlord. This adjournment was a relatively long one – I suspect they were laughing in the other conference room and in partial disbelief–. When our opponent returned it became manifestly clear that our client's forthrightness and desire to move this lease to completion fell on deaf ears. Instead of inspiring our landlord into a spirit of cooperation, as our client had hoped it had just the opposite effect. When the landlord's team returned to the conference room, they said: "First, we want to sincerely thank you for your very generous and well thought out concessions and we too desire to move the transaction to a rapid and fair consummation. It is in this spirit that we took the time to outline what else we will need from you to finalize this deal quickly." The landlord then presented us with a substantial list of additional demands and failed to concede any single significant deal point we had previously requested!

Our client went ballistic, words like "bad faith"; severe and

sometimes harsh questions concerning our learned opponents, genealogy, sexual preference, chastity of their dear mother, their true heritage, patriotism and their significant resemblance to less than the best parts of the human anatomy were exchanged. Notwithstanding this strong stand, it had absolutely no effect on our opponent. Our opponent was fully prepared for a three (3) day negotiation and they were in a target rich environment. I do not believe that all of the harsh words even raised the blood pressure one point of our learned opponents. From their perspective they had three (3) days to make the deal better. Unfortunately, our opponent did not fully comprehend the fury of our client and the landlord eventually negotiated him/herself right out of the deal. This landlord fully bought into its newly perceived leverage and established new goals, which were totally inconsistent with the spirit of the transaction up to that point. Instead of the three (3) day session consummating in a deal it came to an end in day two (2).

Day Three – early morning, as we were checking out it occurred to even the dullest of us that the deal was in the process of being transported to the first available ICU and notwithstanding the diligent effort some of the best deal doctors, the deal was pronounced DOA. Our team was forced to find an alternative location and we all had learned from this expensive lesson. In retrospect, I believe our immediate concessions created some very unrealistic expectations on the part of our opponent. If it is important to your opponent and not to you – first make sure it is important to your opponent – second, concede the point but make him/her earn it. If not, you could be conceding points that you perceive as major concessions only to find out it means little to your opponent.

The above transaction was definitely a Magnum Lease, we had significant leverage and in a mere twinkling of an eye we lost it!

Commitment to Move - Assembly of the Team

First Step Obtain, Retain and Use Leverage - Commit to Move - Assemble the Team - Make No Commitment

Astute landlords simply will not put their best deal on the table until the Landlord is convinced that there is at least a substantial probability that you will be moving. The Landlord's perception is simple, without the potential for loss; there is simply no need to concede. Notwithstanding that he/she is aware that you are in the market soliciting proposals, the Landlord inherently knows that in most circumstances he/she can continue to bid for your retention until you have signed a lease with another landlord. Unfortunately, this is true. Until you have another lease signed, sealed and delivered you are more or less foolish not to listen to your Landlord. Landlords will typically refer to this as the "**last look option**." Although, the Landlord will always have this last look option there are some steps that

you can take to convince the Landlord that his/her last look may be more like a **“last glimpse option.”**

(a) Retain a top-notch **tenant representation broker**. These individuals do not waste their time on leases that are not likely to happen;

(b) Retain an experienced **real estate lease lawyer** –the earlier the better–. Even the best of lawyers can do little to remediate incomplete or poorly prepared RFPs and letters of intent. Landlords and their lawyers tend to prefer short, incomplete letters of intent while tenants and lawyers –that primarily represent tenants – tend to prefer detailed letters of intent (see my article “Letters of Intent, Use and Strategy,” July 23, 2002). It is very important to retain the deal negotiated. Essential to retention of a well-negotiated deal is the proper preparation and of a request for proposal and letter of intent. These lessons have been learned through much heartache and the spilling of much blood! The message to the Landlord is clear; companies do not spend money on lawyers to prepare requests for proposal or letters of intent unless they are serious;

The Landlord's perception is simple, without the potential for loss; there is simply no need to concede.

(c) Retain a **space planner** to prepare fit plans. Companies do not spend money on space planners to prepare fit plans unless they are serious;

(f) If your search is too narrow the Landlord may obtain leverage. As with any good illusion your audience must not be able to see through this illusion, to the reality. This illusion could be based on a perceived alternative with financial savings, better location, better image, or superior terms. For example, if all the leases for Area A (comparable buildings), are plus or minus 10% of the Landlord's offer and your search is limited to Area A the Landlord will know what he or she is bidding against and given the above financial analysis it is not likely that you would move. On the other hand, if your search includes Areas A, B and C and within B or C lie superior financial incentives by 20-30%, the Landlord may in fact lose his/her perceived leverage;

(h) If at all possible, tour another building that the Landlord also owns or manages. It is our supposition that matters discussed with the broker for this alternative site may just be shared with your Landlord. A recent bogus survey conducted by the Totally Facetious Consultants, Inc., has lead us to the conclusion this is at the top of the list of totally believable but unverifiable facts. Let's just call it a strong hunch. When selecting your real estate representative due care must be taken to avoid any potential for this type conflict of interest; and

(i) In addition to the above, a lease of this size includes due consideration for the retention of the following professionals (unless such skills are available in-house):

- ◆ Move coordinator;
- ◆ Furniture purchaser;
- ◆ Telecommunication consultant;
- ◆ Financial analyst/Tax consultant;
- ◆ Contractor;
- ◆ Entitlement and/or municipal incentives consultant;
- ◆ Project manager; and
- ◆ Other professionals may become necessary if one of your viable alternatives is in the development stage (beyond the purview of this article).

What to Expect from the Landlord: “The Game is Afoot”

Lease negotiations often do not proceed according to plan, as rapidly or smoothly as desired. Similar to the game of chess if your opponent is a novice and unskilled you can quickly move to checkmate. On the other hand, if your opponent is highly skilled just when you call “check” he/she calls “checkmate”. Landlords are smart people; well-educated, highly skilled and smart people represent them. The Landlord and his/her team will know exactly what you are trying to accomplish. The best of landlords will be with you step by step at each negotiation stage –if not ahead of you–! Even the best of plans will require constant monitoring and modification to meet the stated objective. As with all plans it is only valid until the Landlord implements its own counter measures.

Once you bite be aware that further concessions will be of a nominal nature. Once on the proverbial hook/trap there is little need to cuddle the prey.

Many of you have been part of a lease negotiation conducted by sophisticated real estate lease professionals. May be it is just me but I am amazed how the parties continually interrupt each other in the middle of sentences. Sometimes this sort of resembles one of our currently popular TV political analysis shows. You are never quite sure if the other side hears what you said let alone cares for what you say? The more experienced, the more energetic, the more interruptions. These are not inherently rude people, so why is this the case?

The more learned and experienced the parties the more they know – or at least they think they know – what the other party is about to say before they say it. Most have been there before and have an inherently brilliant response to the point about to be made and just can't wait to provide it. It is my supposition that great dividends can be reaped if one can only control ones desire to respond eloquently to the point about to be made, until you know the point about to be made. I have been part of more than one negotiation where I was interrupted by an extremely learned, distinguished, state of the art, sophisticated, erudite real estate professional. Much

to my surprise my learned opponent conceded a point that I was not about to make. Naturally, I thanked him/her for the concession and went on to state my point differently so it was perceived as a totally new issue. I vividly remember one negotiation held in the golden triangle of Beverly Hills. I was about to make a point when opposing counsel, the broker and the principal became visibly upset vigorously commenced a fist pounding, airborne distribution of saliva, all with veins protruding from their temples and neck, all to demonstrate their sincerity and righteousness of their cause. Although the magic words, "take it or leave it", "not subject to further discussions," weren't used we all understood what was being said. As I recall, they even invoked divine guidance by stating their proposition was "right in God's eyes" – some negotiators love to call upon the deity to intervene on their behalf –. I must admit that on this occasion I was befuddled and was about to opine eloquently, when my brilliant and manifestly brutal partner kicked me under the table. Since my partner and I had previously worked out this highly intricate, clandestine and complex procedure I knew exactly what he meant by the stiff kick. As I gracefully and nonchalantly bent over to rub my shin, I then begrudgingly conceded the point to our opponent and acknowledged that: "I would never do anything that wasn't right in God's eyes." In this circumstance, I was particularly graced with a partner who possessed superior financial acumen and knew immediately what we were given (he didn't need no stinking calculator). I on the other hand knew something was amiss and was about to pull out my 12C (OK I know this dates me) and in all likelihood would have spilled the beans with a totally innocent or ignorant question or two. Although I instinctively knew something was askew my partner knew exactly what we were given during this tirade and my partners single was clear –shut up–! My partner also knew me well enough to know that if he let me talk I would inadvertently point out the errors of their ways before I figured out that their ill presented offer was much to our benefit. During their short-lived tirade they conceded something that we weren't even going to ask for and much more than we had possibly hoped. The lesson learned was simple; often some of the best concessions come while you are just listening. Never underestimate your opponent but don't over estimate them either!

Stuff always seems to happen and landlords know from experience, that there will be days, in which your commitment to relocate – whether real or perceived – will not be as strong as in others. Some of the **strategies the Landlord** will use to keep you interested:

1. Landlord will call and let you know that the Landlord has commenced lease negotiations with another, very viable tenant. Most of the time this is an illusion and a viable tenant may have only visited the space but it's truly difficult for you to ascertain (know what you don't know).

2. The Landlord will attempt to keep you focused on your side of the financials. The Landlord will either directly or indirectly refer to the expense of hiring a broker, lawyer, designer, moving cost, loss of productivity, etc., and the time necessary to look, find and negotiate for alternative space. The astute Landlord will even offer to *share some of the savings while retaining the lion's share* for him/herself. If the Landlord can keep you focused on your side of the equation, the fair sharing of the Windfall will be lost.
3. The first relationship the Landlord will try to test is the Broker-Tenant relationship. The Landlord will undoubtedly discuss a sharing in savings of the brokerage commission. After all, this is just a renewal; what do you need a broker for? We can handle this and the broker just costs both of us money! Ultimately you will have to determine whether the retention of a broker to represent you in this process is in your best interest or not. It is not the intent of this article to be totally expositive on this issue but here is some guidance. If your current broker is a "space finder" (i.e., one who locates space but does not provide sophisticated financial and negotiation skills) the value of such retention may be nominal. On the other hand, if your broker displays creativity and the leadership to negotiate leases that meet your objectives then retention is probably desirable. The second type of broker will more than pay for him/herself through the process. ***No matter how competent and qualified the Tenant, superior results will occur through the execution of a strategy targeted to access the Landlord's Windfall for the benefit of the Tenant.*** Competent external professionals dedicated to achieving the results that the Tenant desires best execute this type of strategy. If you are a lawyer or space planner do not be concerned; the Landlord will get around to testing your relationship with the client! "We have operated under this lease for 10 years and it has always worked well so why do we want to muck this up with lawyers." "My space planner knows this building better than anyone else, can do a better job for you and do it for less."
4. Some landlords will attempt to make this negotiation personal. They may at some point mention his/her close relationship with a member of your senior management. You may be subjected to discussions regarding this wonderful and long-standing relationship and how much he/she appreciates you as a Tenant and doesn't want to lose you. A smart Landlord will often position him/herself as your advocate to the owner of the Building ("I would give it to you but the owner is just being obstinate") or ("I would give it to you but the lender prohibits this sort of concession") or ("You are an experienced and sophisticated real estate professional and a deal maker, it is up to us to make this deal"). Although, this is an area where you truly don't know what you don't know, use of common sense can produce

great dividends. You should ask yourself the question: does it really make sense for the lender or the landlord to be overly concerned about what occurs in this circumstance?

5. Until your new lease is complete the Landlord may bait/tempo you with concessions in an effort to get you back to the table. For example, if the location of your visitor parking is an issue he/she may concede that point and offer some visitor parking reserved specifically for your organization. If this fails to get you back to the table he/she may concede another point (e.g., provide you with another month's free rent, an increased tenant improvement allowance, etc.). We call this strategy "fisherman style retention" or the "bottom dredging technique." The Landlord may just continue to bait you in an effort to identify your bottom line. Once you bite be aware that further concessions will be of a nominal nature. Once on the proverbial hook/trap there is little need to cuddle the prey.

Sophisticated landlords will only put on the table what they must in order to retain a viable tenant. The Landlord has several arrows in his/her quiver in which to accomplish this through informal casual conversation concessions: (a) "what must I get from my owner to retain you?" or – my personal favorite – (b) "if I am able to get this concession from the Landlord do we have a deal?" I call this the reverse commitment scenario. You are committed but the Landlord is not! The Landlord has managed to identify your bottom line without revealing his/hers and without conceding anything whatsoever; caution: The Landlord is attempting to get you to bid against yourself! or (c) "what buildings and landlords are you dealing with?" Once the Landlord has identified its competition, Landlords are expert at obtaining market knowledge and pointing out the benefits of staying in their Building.

6. The Landlord will make sure that when and if a truly viable tenant is touring, your space will be toured during normal business hours. The Landlord will do this whether or not it is allowed by the terms of the Lease. The Landlord knows that by conducting this tour he has effectively invaded your private space, started rumors throughout your organization and negatively affected productivity. The more prestigious the prospective tenant the more likely the tour will occur during normal business hours. The message is obvious to you and your organization: Something is up and you can be replaced! In reality this tour may be the tenth property that this potential tenant toured that day and the likelihood of your premises meeting XYZ Corporation's needs may be in fact remote. The other message is to the employees of your organization: "Something is up". Often tenants make the mistake of keeping the general parameters of a potential move from their employees. Often the logic is well intentioned (no need to alarm the team) but could have some dire results. We have known employees of a

tenant to actually call the landlord to find out what is going on! Nothing is so disclosed as a well-kept secret; rumors will run rampant and productivity will suffer. Those actually in the know will feel compelled to disclose to their close friends and so on. Through the years some of your employees will develop close relationships with the Building's personnel, which could lead to inadvertent disclosure of our true intent.

7. The Landlord in most circumstances will know its market very well. As a result, he/she will also know what alternatives you will have in its area. ***If you restrict your search to the Landlord's market he/she will have a very good idea what offer is on your table.*** If this occurs the Landlord will only share in his Windfall to the extent necessary to match your cost of the equation, plus a little incentive. Although, the Landlord's lease may have a total cost less than the alternative, it is not a fair sharing of his Windfall. Stay the course; the Landlord has room and great rewards can be achieved if patience, diligence and persistence are used.
8. How will you know that the Landlord is buying your story? When he starts making significant concessions that go beyond what he/she has offered you in the past. Specifically, the Landlord starts granting concessions that exceed your breakeven point, more fairly sharing his/her stay in place Windfall. I wish I had a nickel every time a landlord or tenant has stated: "This is the final and best offer and no other offers will be forthcoming," or "Take it or leave it." Very few things are forever and often better offers are forthcoming if you just stay the course.
9. Knowing when to accept the Landlord's offer and when there is more room is part a function of an astute financial analysis prepared by your representatives and in part good old fashion negotiation skills. Knowing when your team has achieved its goals and reached optimal results is much more an art than a science. Only a team of competent real estate professionals fully committed to executing a well-conceived strategy to near perfection can achieve the best deal. Your attorney's role is to ensure that the documents accurately reflect the deal obtained and to prevent dilution in the details. The broker's role is to manage this process and to keep you on track to achieving your stated goals, objectives and knowing when there are simply no more concessions forthcoming from your Landlord. Only then will you be in a position to make an informed and competent decision as to your market alternatives.

Knowing when your team has achieved its goals and reached optimal results is much more an art than a science.

10. In addition to all the other typical Landlord tactics, some Landlords may attempt the old end around. This is a very dangerous borderline unethical strategy and most landlords will refrain from its use but nonetheless it is mentioned here since it does happen. A lease of this size is prized and desperate landlords will on rare occasion address your senior management directly (sometimes even Board members). As negotiations progress the Landlord will also execute its plan to optimize its profits. In our hypothetical scenario we already have an established relationship with senior management and this is a very real potential. If you do not have the support of senior management this could be a very dangerous but successful strategy by your Landlord. You have asked for several concessions and the Landlord has refused to grant them. The next thing you know the Landlord has offered the same requested terms or superior terms to a member of your senior management. This offer is so good that as an ethical executive responsible for real estate you are mandated to analyze and present it to your senior management. You must put aside your personal feelings toward the Landlord and perform your duty well. You now have the lease you desire but you must concede to an opponent who has conducted him/herself in an unethical fashion and at the same time damaged your authority and credibility within your organization. Thank goodness that this is a rare maneuver and could easily backfire in the Landlord's face.

Challenges You Will Face as the Tenant

Unless senior management is convinced that relocation is desirable for some other business reason (image, location, access, etc.) they must be convinced that the financial benefits of any move will greatly exceed the *stay in place* scenario.

For a transaction of this magnitude it is essential that all communications are strictly controlled by and between you, your Landlord and any other potential landlord. This is the primary role of your professional real estate broker. This individual must act as the conduit for all communications in this transaction and should be present any time you anticipate communications with your Landlord or any potential landlord – make your broker earn his/her fee–.

In a lease of this magnitude the Landlord will know what your alternatives are and which of those alternatives are truly viable to your stated culture. Care must be taken not to bluff with any alternative building or location that the Landlord knows you clearly would not relocate to.

Never underestimate the Landlord's ability. The Landlord negotiates leases each and every day and is good at it! In many circumstances the Landlord will know his lease better than your attorney. Your attorney has read it once or twice the Landlord has read it dozens of times. We are playing in the Landlord's backyard. The Landlord knows his/her Building and his/her market better than most. The Landlord also has a very deep appreciation that in most circumstances it is easier and cheaper for the Tenant to stay in place and not relocate. After all is said and done this is in most circumstances the simplest if not the most viable solution. All other things being equal the Landlord knows that any lease that costs you less than a full-fledged relocation is a better lease for you. The Landlord is in the business of real estate and in most circumstances you are not. When all else fails remember the Landlord has the Windfall to play with and still break even. The Landlord will in most cases know your bottom line, where you are more or less making a very educated guess at his/her bottom line.

Know Your Objectives before Commencing

Just about every book on negotiation will advise that the higher the aspirations the better the result. We would temper that with the higher your *realistic* aspirations the better the result. Don't ask for something the Landlord truly cannot give you and don't fall prey to your own brilliant logic and lose sight of your true objectives. Often tenants commence this renewal process with a breakeven or a slight savings mentality. This being the case the tenant is less likely to achieve the results that are desired and more importantly a fair sharing of the Windfall. I have often heard "just get a market deal", or "just get a lease which saves us the cost of relocating" or another personal favorite "we are not in the real estate business; we just need a place to keep the rain off of us." Although in some situations those objectives may be the best that can be hoped for, in most circumstances tenants can do much better if professionally represented through the process. At the other end of the scale is the tenant that desires 100% of the Landlord's Windfall. The logic is that I am still saving the landlord attorney and other fees; therefore this is a good deal for the landlord. Although on rare occasion a deal can be struck at 100% of the Landlord's Windfall these victories are rare and generally short lived. No matter the sophistication used in the negotiation of the Lease document an embittered Landlord will find a way to exact his just dues. The tenant must refrain from the concept of taking every last dollar on the table. Remember you are living in the Landlord's house and as such he has some degree of control over your daily affairs.

The Lease Document

In this case the Lease document is ten (10) years old. If it appears to be a fair document, that is one in which problems have not arisen it is difficult to justify the time and expense of

a full terms, covenants and conditions negotiation (a new lease document). It is true that a re-negotiation of the Lease document by a competent real estate attorney can be costly and time consuming. This conclusion can be a costly and a shortsighted mistake. The state of the art for tenant lease representation has improved dramatically during the last ten (10) years, brokers and lawyers have discovered that some of the sacred lease language works while other language doesn't work so well. Additionally, your leverage may have improved dramatically during the past ten (10) years and many very undesirable provisions may have been previously forced upon you. Leases like most agreements are in essence doomsday documents. It is not unusual for parties to seldom

Nothing is so disclosed as a well-kept secret; rumors will run rampant and productivity will suffer. Those actually in the know will feel compelled to disclose to their close friends and so on.

read or review their leases. Most of the time the lease is only reviewed when one party is upset at the other. In other words, one party has asked for or insisted upon a certain action or forbearance and the other party has refused to conduct themselves in accordance with their wishes. At this time one or both parties will run to the lease to find out what it says. In other words, whether a lease is a fair document can only be determined after the parties have bumped heads a few times. Our experience also suggests that it is well worthwhile retaining an experienced real estate lease lawyer for the purpose of reviewing your lease document – we cannot over emphasize real estate lease lawyer-. This is a very specialized field and although many venture into this field few are truly expert. Sometimes a great transaction can be negotiated only to be lost in the drafting process.

I have observed a very simple rule, the more complex the lease the more that has fallen through the cracks. You simply cannot provide a formula one racing car to beginner and expect him/her to win the race. A good example of this occurred several years ago. I was called upon by a client, to resolve a dispute by and between him and his landlord. The lease was a very complex lease and the base document was close to 200 pages. As typical with most of these disputes both sides had already thoroughly read the lease and quoted same or similar provisions to mean different things. As is also typical of most of these disputes, this dispute concerned duties and responsibilities. At the heart of the problem was the issues of what is covered by the base rent, what is covered by the operating expense pass throughs and what is an additional charge item? After struggling with the lengthy document the only thing that was clear is that it was not clear. Even though this lease was prepared by who most would readily acknowledge as two of the countries finest real estate

leasing lawyers, the lease was less than totally expositive on this particular lease issue. I am sure any real estate lease lawyer will tell you it simply is impossible to be totally clear, concise and expositive on each and every issue. If the perfect lease has been created I have never seen it, nor do I know anyone who has seen it and we doubt that it exists. If the totally clear, concise and complete lease exists it must be so clear that it is almost totally transparent! Please let me know if you find it, I would love to read it!

When I first met with the landlord's representative he/she admitted that he/she didn't understand the lease. As a matter of fact, he/she retained a different law firm – other than the one that prepared the lease in the first instance – to prepare a summary of the lease for her/his own use. The summary of the lease was 30 pages and was less than expositive on most of the issues. As the old saying goes "**lawyers draft them, property managers interpret them and judges tell you what you really said and meant.**" Since the lease was less than totally expositive as to this particular issue, the parties agreed to disagree for a time but we did eventually strike a settlement. The settlement involved an amendment to the lease in an effort to clarify the allegedly ambiguous provisions of the lease.

The initial legal review should be limited to: (a) Assessing the validity of the Lease itself (amendments, estoppels, non-disturbance, subordination and attornment agreements, assignment to parent, subsidiary, name change etc.). The question here is whether the Lease accurately reflects the agreement and the practices that the parties are operating under; (b) Ensure that neither party is in technical breach (e.g., was all free rent applied, is the security deposit in place per the lease, etc.) The more complex the free rent scenario the less likely the free rent is properly applied; (c) whether or not there are any other terms, covenants or conditions that you should now have in place (are you being over-charged for electricity, after-hours HVAC, day porter, extra-janitorial services, etc.). It is my supposition that many – I would like to say most – of the seasoned Magnum Leases are in some sort of minor technical breach. Notwithstanding the brilliant negotiations by and between the parties, landlords and tenants often operate per the spirit of the transaction rather than the black letter of the lease. These minor technical breaches are in fact never raised until the parties are at odds with each other. This is an opportunity to modify the lease to actually conform to the custom and practices by and between the landlord and the tenant.

Here are a few simple examples of things or provisions you may want to have your attorney review: (i) Do we have copies of all the relevant lease documents, it is surprising how often parts of the actual original documents are missing; (ii) Security deposit - ten (10) years ago maybe this was justified but now you are a seasoned Tenant and it may not be prudent to provide a security deposit. Additionally, in the last ten

(10) years the Building has been sold twice and the location of your security deposit is uncertain; (iii) The assignment and subletting provisions are overly burdensome and do not allow for consultants to occupy space in your premises or assignment to a wholly owned affiliate or subsidiary; (iv) Have all delayed concessions due to the Tenant been accounted for? Again this is another area where the more complex the lease the more likely something has slipped through the cracks. It is surprising how often staggered/deferred rent and other deferred benefits like free parking are double paid; (v) You may no longer desire to grant Landlord the right to recapture the space or to relocate you within the Building; (vi) You may desire a mutual estoppel certificate provision to accommodate corporate mergers, restructuring etc.; and (vii) Other issues such as operating expense exclusions, sign rights, parking etc.

There is little doubt that the list of potential Lease issues is limitless. At the same time, if we are serious about renewing our list should be kept short, sweet and limited to the majors. We should not attempt to unjustly improve our position but where legitimate concerns exist now is the time to address them.

The magnitude of this lease has greatly enhanced the potential savings and the potential detriment if this process is not handled properly. Additional goals for the relocation should be clearly set prior to commencing the search process. Often goals within an organization will become confused. Here are a few examples for a lease of this size:

- ✓ Obtain the right location and exclusive sign rights;
- ✓ Expansion options on all contiguous floors;
- ✓ Extension options;
- ✓ Option early termination and contraction options;
- ✓ Extended Building Hours and Building Days;
- ✓ Limit Building Holidays;
- ✓ Obtain incentives from the municipality either to remain or relocate within its jurisdiction;
- ✓ Enhanced security for the Building and parking lot;
- ✓ No leases to competing companies, if applicable; and
- ✓ Visitor parking, more covered parking spaces etc.

For a much stronger reason than in smaller transaction, this ten (10) year old lease will contain terms, covenants and conditions that a sophisticated real estate attorney may be able to greatly improve upon. The experienced real estate attorney should be able to provide you with a realistic assessment on whether or not there is a lot to be potentially gained by a full terms, covenants and conditions negotiation (a new lease document). Although costly, it should more than pay for itself during the term of the new lease.

I have often heard let's just let the lawyer's handle the "legal issues" and the broker's and the client handle the "business points". Although this sounds innocent enough I believe

purity in this sense is more of a figment of one's imagination rather than a reality. Such a concept is more akin to hiring the Three Stooges Design and Construction to remodel your home. To illustrate our point, let's take the most Snow White – in this sense the purest of them all – of business issues "rent". I have a few questions:

- Is the rent based on RSF, USF or just an agreed upon amount?
- Is the rent to be based on the measurement of the premises? If so,
 - ✓ How measured?
 - ✓ What standard is to be used?
 - ✓ When measured?
 - ✓ What happens if Tenant measures and space smaller than anticipated?
 - Can Tenant terminate the Lease?
 - Tenant improvement allowance increased or decreased in accordance with the measurement?
 - ✓ What happens if Tenant's representative says "X" RSF/USF and Landlord's representative says "Y" RSF/USF?
- What happens if the RSF/USF is found to be incorrect years later?
 - ✓ In such event who owes whom money? When is that money payable?
 - ✓ Can such a delta be used as an offset against rent?
- What happens if the payment of rent is late:
 - Late charge;
 - Interest;
 - Default;
 - Grace period.
- What happens to rent if the premises are or become uninhabitable because of a breach by landlord?
- What happens to rent if the premises become uninhabitable because of something a third party does?
- What offsets apply to rent?

Are the above questions primarily legal or business? It has been my experience that the best of the best in the industry fully comprehend that each business point has a legal component and each legal point has a dollar value attached to it. **Purity by and between legal and business points is indeed rare if it exists at all!**

Summary of the 100,000 RSF Lease

Renewal transactions are as a general rule very profitable to landlords and there is a lot to be gained by sophisticated representation during this process. The best rent can only be gained by the development and implementation of a strategy, carefully executed by a team of experienced and dedicated real estate professionals.

Your lease renewal is a time of great opportunity for you and your Landlord! If properly prepared and represented you will obtain your fair share of the Landlord's projected savings or relocate to a better location and/or with a better lease. We

believe the most critical elements are as follows in their descending order of importance:

Time is the most critical element and we have never started too early but we have started too late. If time is on your side you have one very big advantage;

Assemble the right team to conduct the assessment. At a minimum a sophisticated broker and lawyer. Both of these individuals must be top-notch negotiators;
Obtain **senior management support** and involvement;

Undertake a **realistic assessment of the market**;

Truly **understand the Landlord's savings** in a renewal scenario;

Gain and maintain **control over the process**; and

Formulate **sound and clear objectives** agreed to by your organization and your team of professionals.

CONCLUSION – “LAFTCO”

Below we have set forth a short checklist of some of the thoughts you should at least consider in any renewal scenario.

- ✓ **Leverage** - obtain, retain and properly use;
- ✓ **Assemble Team** - correct for the task;
- ✓ **Financial Analysis** - know the numbers;
- ✓ **Time** - start early;
- ✓ **Communications** - control the process; and
- ✓ **Objectives** - aggressive and realistic considering all relevant factors. Know thyself; how much reward you are seeking and measure carefully against the risk. The more aggressive your position the greater the risk, also greater the reward.

Last but not the least, the real estate team that has prepared this article collectively possess over 70 years of combined real estate experience. In our many years of experience we have yet to find an in-house corporate executive responsible for real estate that has fairly represented his or her added value to their organization. Often real estate is viewed as a “commodity” that is merely to be purchased. Real estate is unique and requires detailed and sophisticated negotiation tactics to maximize an organization's profits. It is our hope that the sum and substance of this article will provide you with some useful tools that will clearly and accurately display your value!

**** THE SPREADSHEETS ARE AVAILABLE UPON REQUEST TO DENNIS NEGRON VIA EMAIL DENNIS@DIRTATTY.COM. PLEASE PROVIDE ALL CONTACT INFORMATION.**

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