

Real Estate Strategies

Long Leases: A Lawyer's Reflections Of Today's Changing Market

BY SCOTT H. MILLER

RECENTLY I GOT A CALL FROM A POTENTIAL CLIENT WHO WAS NEGOTIATING THE BUSINESS TERMS FOR A DOWNTOWN OFFICE LEASE WITH A LANDLORD. HE WOULD LEASE A SMALL SPACE IN A LARGE BUILDING FOR TWO OR THREE YEARS.

The deal was as simple as they come. And yet the landlord's lease Documentation was hefty enough to measure in pounds. The caller wanted to know: Could I help?

That's a great question and I still don't really know the answer. The negotiating leverage of the tenant was zero, so there was not much I could do at the bargaining table. I could read the documents and explain to my client, who knew little about leases, as much as he could tolerate about what he was in for. And charge him for that crash course in onerous lease documents. Not very satisfying, though my malpractice carrier might approve.

Does the lease need to be that long? Why are leases so much longer now than they were years ago? Why are leases generally so one-sided? After almost twenty-five years as a lawyer, most of them in commercial real estate, I know that it is fairly easy to write a comprehensive lease that few tenants with significant assets will sign without protracted negotiation. Here are a few reflections on the rapidly evolving world of increasingly complicated office leases.

There are many forces at work in commercial leasing that contribute to long one-sided documents and the

resulting negotiations and legal bills. The lease is the meeting ground for today's rapid pace of business and a landlord/tenant relationship that will last for years. No landlords or tenants want long documents or protracted negotiations, but very few will readily give up what they perceive they need. In the case of tenants, the need often includes better information to assess the likelihood of future maintenance, capital improvement, operation and tax increases due to building transfers.

Real Estate is a Big Business. Many years ago there were not that many large buildings and real estate was not as big of a business. Real estate ownership tended to be simpler. Now real estate has a place in all institutional portfolios.

Ownership of Real Estate is Often Complex. The ownership structure for larger office buildings has become more layered and complex. Real estate competes with other businesses for investment dollars, creating greater stress for leases to produced ascertainable returns. The lease is

expected to act like a bond with a fixed return and all contingent risks and expenses pushed onto the tenant.

Decision-Making Can Be Difficult. When ownership of real estate is simple,



the owner can more easily decide how long and one-sided to make the lease form and make quicker decisions during lease negotiations. In a more institutional ownership structure, it tends to be more difficult to obtain clear-cut decisions that deviate from a very risk-averse approach.

The Pace Of Business Has Accelerated. Service businesses, specifically those that tend to use office space, have grown enormously. Also, the pace of business transactions has increased. Businesses also expand, merge, contract, or die at a greater rate than in the past. Tenants are driven to have flexibility in their long-term space commitments and to quantify their total monetary lease obligations to facilitate planning and budgeting.

Real Estate Has Its Own Pace. Real estate tends not to move as fast as the Internet. Owners and tenants have to try and project years in advance when they commit to a lease. The flexibility and certainty sought by each party can result in the negotiation of many issues.

Inherent Unknowns. Commercial real estate has inherent unknowns. It is extremely sensitive to the economy, and an expanding list of legal requirements (ADA, asbestos, seismic, sprinklering), and it is often hard to predict what will be next. A lease is about a future relationship. No matter how many contingencies one tries to anticipate, the future tends to provide others.

Technology. Technology plays a role too. When carbon paper was king, you got to the point quickly when drafting a document. By contrast, word

processing encourages increasing amounts of boilerplate because it does not require a decision to accept a risk.

Job Mobility. People are more mobile and stay in their jobs for a shorter period of time. Since a lease is a relationship over years, everyone now has to assume that the same people will not be around to settle the inevitable issues and the document is asked to address more.

The Defensive Practice of Law. Law, like medicine, is practiced more defensively these days. Remember all those expensive tests for your headache? Well, how about all those expensive documents with literally hundreds of issues and sub-issues? Only the lawyers understand them comprehensively. If only the lawyers thoroughly understand the documents, and they (the lawyers and documents) are too downside-

oriented to begin with, it is difficult to break the logjam? The above factors do not preclude briefer leases or efficient negotiations. Current business environment puts a premium on the importance of (1) paying attention to the fit between the tenant and the landlord, and not just the tenant and the premises, (2) owners making clear strategic decisions when preparing their lease forms, and (3) tenant attorneys understanding the lease deal and their client's business so they can provide quality risk/benefit analysis with respect to various lease issues.

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