

The Association of the Bar of the City of the City of New York

Committee on Real Property Law

Model New York City Retail Lease

COMMENTARY

Introduction

For decades, landlords and tenants of retail space have relied on forms promulgated by the Real Estate Board of New York, Inc. (“REBNY”), a trade organization for real estate owners and brokers. Real estate attorneys, for landlords and tenants, typically add one or more riders to the “boilerplate” form to reflect negotiated provisions and the terms of the specific transaction. The result is a lengthy document that often contains duplicative, and sometimes conflicting, provisions that may produce unintended results and requires the reader to look in several places in order to administer the lease.

Throughout the five boroughs comprising New York City, there are small buildings with only one or two retail tenants. Some of the buildings may have a retail space on the ground level and two or more floors of residential or office tenants above the store. Some of the buildings may be so called “taxpayers” - a few retail tenants in a line on ground level with or without parking area or common area. The lease form that we propose is an attempt to provide a more user friendly document. In deference to the industry custom that has landlord’s attorney preparing the lease, it is more landlord oriented than tenant oriented, but it is more balanced than the REBNY boilerplate form. It begins with terms to which a landlord’s attorney would likely agree in the negotiation of the initial draft lease.

Specific Provisions

Article 1. Basic Terms and Definitions. (a) In addition to providing certain definitions, for ease of administration, it is suggested that this article also contain a brief recitation of some provisions that are specific to the transaction, e.g. an option to extend or cancel the term, a right of first offer or an exclusive use.

(b) The definition of “Fixed Rent” contemplates that the Fixed Rent is to be set forth on an exhibit to the lease, Exhibit A, in order to make it easy for the parties to view at a glance this very important provision of the lease without using a substantial portion of the first page that is devoted to other basic terms. Note that the definition of “Rent” includes, by incorporation of the term “Additional Rent”, all sums payable by Tenant to Landlord under the lease.

(c) If the Premises is described by a stated square footage (as opposed to a space number such as space A, or a diagram), the parties may want to state that the square footage is approximate or is “deemed to be” the stated size.

(d) Tenant should determine whether the Permitted Use is permitted under the existing certificate of occupancy for the Premises.

(e) The definition of “Proportionate Share” contemplates that the parties will insert a percentage figure, which is the basis for the payments the Tenant will make under the tax and expense sharing provisions of the lease. The initial determination of this percentage is to be made by Landlord, but Tenant should review and understand, and perhaps question, Landlord’s percentage calculation.

(f) Note that the definition of Security provides for increases as the Fixed Rent increases, and through a reference to the article on Security, for increases after default. Tenant may try to negotiate for a reduction in the Security if Tenant has not been in default of its lease obligations after some period of time.

(g) Text for a sample Tenant’s right of extension, which could be adapted for a right of expansion, is provided in a rider. Tenant loses its right if Tenant is in default either at the time of notification of its exercise of the right or at the time that the original term is scheduled to expire.

Article 2. Demise; Rent. In the event that Landlord cannot deliver the Premises on or before a date certain, neither Tenant nor Landlord is given a right to terminate. Some would argue that Tenant should have that right because Tenant has no control over Landlord’s delivery and should not be locked indefinitely into a lease. However, Landlord’s delivery of space possessed by a holdover tenant may be controlled by a court, not the Landlord. This will surely be a matter of negotiation if the Premises is not vacant or if Landlord has major work to prepare the Premises for Tenant’s occupancy. As the Commencement Date and other lease dates may not be known when the lease is executed, the lease includes an exhibit of a sample document that can be used later when the dates are known.

Article 3. Use; Rules; Tenant Operations; Signs. (a) Many Landlords will agree not to enforce rules and regulations in a discriminatory manner. However, this does leave Landlord open to a charge that it is violating this provision if, for example, Landlord begins to enforce a rule against Tenant only after it has received complaints from other tenants.

(b) Signage is a major concern for retail tenants and should be carefully negotiated.

(c) The text in this Article and in Article 8 should be revised if Landlord provides trash removal services.

(d) There is a rider for food use that should be referenced if applicable.

Article 4. Condition of the Premises; Landlord’s Work. If Landlord is performing any Landlord’s Work, text should be added to provide a mechanism to determine that such work has been substantially completed, subject to punchlist items (e.g., provision for notification, inspection, the issuance of an amendment to the certificate of occupancy, etc.).

Article 5. Tenant’s Work. Landlords will often want Tenant, at Tenant’s expense, to remove Tenant’s Work at the Expiration Date so that Landlord, at Landlord’s expense, does not have to demolish Tenant’s Work as part of the preparation of the Premises for

the next lessee. Tenants do not want to have to go to the expense of such removal. The parties may compromise by requiring that Landlord inform Tenant as to which component of Tenant's Work must be removed at the time Landlord responds to Tenant's request for approval of Tenant's Work or they may modify the lease to provide that Tenant will only have to remove specialty alterations which are generally those that are not part of a basic alteration such as reinforced flooring, vaults, floor penetrations and the like. Tenant may also want to modify the lease to specify the amount of liability insurance it and its contractors will be required to carry and to quantify what security will be required of it in connection with the performance of Tenant's Work. The parties may also want to consider inserting specific time periods within which Tenant will have to deliver Tenant's Plans to Landlord, and thereafter, Landlord will have to respond.

Article 6. Tax Payments. Retail tenants typically pay a portion of the real estate taxes and assessments on the Building. The proportionate share is commonly based on the relative size of the Premises and its location relative to the rest of the Building, though other factors may be considered in multi-use Buildings. Tenant should understand how Landlord has derived Tenant's Proportionate Share in order to determine whether to try to negotiate it. Whether the taxes are a direct pass through, or are a share of increases over a base year, is deal specific; the lease provides separate exhibits for each alternative.

Article 7. Expense Payments. It is common in shopping center or strip mall leases for Tenant to be required to pay its Proportionate Share of Operating Expenses incurred for the operation and maintenance of the Common Areas. Operating Expenses often will include capital expenditures, but limited to an annual amount amortized over a period of time and for items such as a roof, or those required to comply with laws enacted after the date of the lease or for cost saving devices. Operating Expenses are most commonly paid as increases over a base year, but some leases pass Tenant's Proportionate Share of the Operating Expenses directly to Tenant. In buildings that are not in a shopping center or strip mall but which have some Common Areas, it may be appropriate for Tenant to pay some Operating Expenses tailored to the specific transaction. Exclusions from Operating Expenses are generally negotiated. In small buildings without any Common Areas, Landlord may still require Tenant to pay its Proportionate Share of insurance and/or fuel costs, either as increases over a base year, or as a direct pass through. The lease includes an exhibit with text for several Operating Expense sharing alternatives.

Article 11. Laws; Hazardous Substances. (a) Tenant should note that as part of its requirement to comply with Laws, it may be required to perform structural work to the Premises, but only if such work is needed as a result of Tenant's acts (e.g., Tenant's Work, Tenant's Property, Tenant's manner of use of the Premises, or Tenant's negligence).

(b) The responsibility for remediation of Hazardous Substances is subject to negotiation. This document does not make Landlord expressly responsible for conditions that pre-exist the start of the lease, but does limit Tenant's responsibility for remediation to that arising from Tenant's actions or omissions to act. Tenant may want to negotiate to specifically require that Landlord be responsible for the remediation of Hazardous Substances existing at the Commencement Date. As lessees cannot get a building permit

from the Department of Buildings of the City of New York without providing a certificate stating that the work will not disturb asbestos, or if asbestos will be disturbed by such work, that remediation will be performed, Tenant may negotiate with Landlord specifically about asbestos; it is not uncommon for Landlords to agree to provide such a certificate.

Article 13. Insurance. Landlord and Tenant should consult with their respective risk managers or insurance brokers or consultants to confirm that the required insurance coverages are available and are at commercially reasonable rates.

Article 15. Condemnation. If parking is included in the Common Area, Tenant should consider whether a significant reduction in parking following condemnation should permit Tenant to terminate the lease.

Article 16. Assignment and Subletting. After basic provisions such as space, rent and term, probably the most important provisions to both Landlord and Tenant are those relating to assignment and subletting. Tenants want the right to sell the business that may, in part, depend upon the location. Tenants also want to have flexibility if their space needs change. Landlords care about the identity of the entities/people in their buildings. Many, but not all, Landlords will agree not to unreasonably withhold consent provided that certain conditions are met. Should Landlords be able to recapture the space? Should Landlord obtain a share of the profit that Tenant can make by subletting space at a higher rent than it is paying to Landlord? These provisions are among the most heavily negotiated by both sides.

Article 18. Default. Tenant may wish to increase the cure period for monetary defaults from 3 days. Landlord may want to specifically state what Tenant is required to do in order to demonstrate that it is diligently curing a non-monetary default.

Article 19. Remedies. (a) Although Tenant may seek a provision requiring Landlord to mitigate its damages by using commercially reasonable efforts to relet the Premises, until it is required by Laws to do so, Landlord may refuse for several reasons, including the difficulty of proving compliance with that requirement and the fact that Landlord may not want to be required to relet the Premises when it has other vacant property to rent. (b) Landlord and Tenant should carefully consider the circumstances under which attorneys' fees are recoverable, recognizing that legal fee provisions are generally strictly construed by New York courts against the recovery of fees.

Article 20. Security. Many smaller Tenants and Landlords will want to have Security in the form of a cash deposit, rather than a letter of credit. The advantages and disadvantages of both forms of security should be considered by the parties. The provision regarding the cash deposit does not require that Landlord place the cash in an interest bearing account unless that is required by any Laws; Tenant may want to negotiate this, especially if the amount of cash is large and/or interest rates are high. There is a provision for conversion to a letter of credit, and a sample form of letter of credit attached to the lease. There is also provision for Landlord to require Tenant to

replace the letter of credit issuer if it has a credit rating by Standard & Poor's of less than AA, and if Tenant does not timely do so, for Landlord to draw on the letter of credit even if Tenant is not otherwise in default.

Article 22. Notices, Consents and Approvals. (a) The parties may wish to provide that notices sent by overnight courier are deemed effective one business day after being sent to eliminate any disputes concerning rejection and attempted delivery of notices sent in this manner. They may also wish to provide that notices sent by registered or certified mail are effective five days, or alternatively, three business days, after being sent, since notices may not arrive three days after mailing.

(b) Landlord may wish to provide that notices may be signed and given by Landlord's attorney in addition to its managing agent.

Article 23. No Representations; Liability; Tenant Indemnity. Landlord may want to add property specific disclaimers regarding, for example, the Permitted Use, the fitness of the Premises for the Permitted Use including fire protection, the existence of a certificate of occupancy, the existence of violations, income and expenses for the property and the nature of the other tenancies at the property.

Article 24. End of Term. Tenant's attorney should be sure that Tenant understands that Tenant may be liable to Landlord for consequential damages resulting from Tenant's failure to timely vacate and surrender the Premises in the condition required by the lease.

Section 25.1 Guaranty. There are two forms of Guaranty attached to the lease – a full guaranty for the entire Term, and a “good guy” guaranty, also known as a possession guaranty. The good guy guaranty, a full guaranty that terminates when the Premises is vacated by Tenant after notice of Tenant's intention to vacate, has become very common, especially when Tenant may have been newly created just to lease the particular space and is thinly capitalized. The guarantor is typically a principal of Tenant and may have some assets in addition to his/her interest in Tenant. The guarantor, the “good guy”, will be released when Tenant vacates the Premises, even though Tenant, typically a worthless shell, continues to be liable for its lease obligations. Leasing lore is that the origin of the term “good guy” was to address the situation of an honest, hard-working Tenant principal who just could not make his/her business in the Premises profitable and needed to escape his/her obligations. Landlord's inducement to accept such a limited in time guaranty is that without it, Tenant can stop fulfilling its lease obligations, and through court delays, remain in the Premises, which prevents Landlord from getting possession of the Premises to re-rent.