

## ***Real Property Lease Checklist***

*The real property lease checklist addresses some of the most common issues that occur when a real property lease is being negotiated. After reviewing it, you should be in good position to understand what to look for in any real property lease. Of course, before signing a real property lease, make sure that you have your attorney review it.*

- **Nature and duration of the lease.** Determine the term of the lease, and when the lessee is entitled to possession. Is the lease to be a net lease? What are the duties of the lessor?
- **Rent.** In the contract, make sure that the amount of rent and when and how it is payable is stated. If the lessee holds over, what is the rent for this period?
- **Escalation clause.** Since most commercial leases contain a rent escalation clause, determine whether the escalation is keyed to actual increases in operating costs or if it is keyed to some index.
- **Competition.** In the case of a lease of retail space, such as a store in a shopping mall, there may be restrictions placed on the landlord's right to lease nearby space to businesses similar to the lessee's business. Are the restrictions reasonable? What rights does the lessee have in the event the lessor violates any restrictive covenant, thereby reducing the value of the lease to the lessee?
- **Renewal.** Is there an option to renew, and what is the term of each option? What is the rent for each renewal period? How must the option to renew be exercised?
- **Subletting.** Is the lessee entitled to sublease the property or to assign the lease? What is required before the lessee may sublease?
- **Space.** What the landlord considers rentable square feet and what the tenant gets in usable square feet space can vastly differ. Designers and space planners can often save costs by laying out the facility to fit the space efficiently. The location of a building's columns, windows and mullions can affect a tenant's total space requirements. Determine whether the lease provides an option for additional space. Is the lessee given a right of first refusal when additional space becomes available? Can other tenants be moved when additional space becomes available so that the lessee's areas are contiguous?
- **Taxes and expenses.** Determine who is responsible for the real property taxes. If the lessee is agreeing to pay only for increases, is there a stated maximum? Who pays for general maintenance and services? If it's the lessee, is the lessee free to contract with whomever they want for these services, or must they be obtained from or through the lessor? Who is responsible for extraordinary or structural repairs or alterations?
- **Construction.** Does the lessor warrant that the building conforms to all local laws and codes, and will the lessor reimburse the lessee for correcting any code violations? Does lessee have right to inspect before execution of lease and before taking possession? Are there adequate parking facilities and other transportation facilities?
- **Workletter.** Space is rarely taken by major tenants in "as is" condition, whether the building is new or old. The fitting out of the premises to mutually agreed specifications is accomplished by a workletter. The latter is a contract between the landlord and tenant describing what is to be constructed, who pays for it and how, what the schedule for completion is, who is responsible for delays and cost overrun and more.
- **Zoning.** What zoning applies to the building, and is lessee's intended use permitted? Are there covenants or restrictions on the property? Easements? How about easements the lessee must have on adjacent property in order to fully utilize the leased property?

- **Liability and insurance.** Who is responsible for liability insurance, and what are the limits? Who carries theft, fire and other casualty insurance? To what extent does the lessor or lessee excuse the other party for liability for injury to persons or property? Lessees should scrutinize any hold-harmless provisions within the lease with great care. While a lessee may be willing to reimburse the landlord for losses caused by the lessee, most lessees would not want to hold a landlord harmless for damage caused by actions of the landlord. The provisions should indemnify the landlord only for harm caused by the lessee within the leased space.
- **Tenant "going dark" rights.** A fear of many small tenants in a shopping center is that a major tenant will go out of business or not renew its lease ("going dark"). In an economic climate in which major department stores are filing for bankruptcy and closing stores, going dark is a real problem. One remedy is to negotiate a clause that gives a tenant the right to close its store or get a substantial rent reduction if a major tenant or several other tenants go dark. Defining "major tenant" is usually a simple matter; defining "other tenants" may be in terms of a percentage of the total square feet occupied by all other tenants.
- **Landlord's solvency.** Is the lessor able to deliver on promises? When the real estate market becomes depressed, more developers and landlords find themselves in financial trouble that could lead to foreclosure on the leased premises.
- **Destruction or condemnation.** Is lessor required to rebuild if property is destroyed, and what is "destruction"? Will rent be abated? May the lessee terminate following total or partial destruction of improvements? What are the rights of the parties if some or all of the property is taken by eminent domain?
- **Termination.** What obligations are imposed on the lessee as to the condition of the property at the end of the lease term? Are ordinary wear and tear excepted from lessee's obligation to return property in good condition?
- **Waste.** The cause of action for waste is a damage claim by owners against tenants for improper use of property. Under the laws of some states, the claim survives a sale of the property so that the former owner may recover the difference between the unimpaired value and the selling price. To avoid this result, the lease might provide that the owner waives any claims in the event of a sale.
- **Purchase option.** Does the lease give the lessee an option to purchase the leased property? What is the option price, and when and how must the option be exercised?
- **Grace period.** Are there grace periods for default on rent or other conditions in the lease? What are the lengths of the grace periods?
- **Enforcement.** Are damages specified for breaches of various lease conditions? What about attorney's fees for actions to enforce lease provisions?
- **Lease commencement date.** It is not unusual for a lease to commence on a date based upon some external event, such as completion of improvements or upon the present tenant vacating. Once the commencement date has been established, the parties should sign an amendment setting forth that date as well as the starting date for payment of rent. This will avoid problems that may arise in the future, such as the expiration date and base periods for determining rental and escalation increases. Arbitration should be provided for to resolve any dispute, or if a party refuses to sign the amendment. To avoid delaying tactics, a simple expedient is to provide that the losing party pays the arbitration costs, including legal fees.
- **Representations and warranties.** The landlord may want the tenant to agree to disclaim any implied warranty or take the premises on an "as-is" basis without any landlord representations or warranties as to its condition or history. In either case, such a clause will impede the tenant from holding the landlord responsible for losses attributable to it. A tenant still wishing to lease the space on such a basis should at least request the landlord's specific representation as to any problem of which the landlord is already aware, and ask the landlord to have pre-lease tests conducted by an independent expert.

- **Use restrictions.** The nature of the tenant's prospective use of the premises may lead the landlord to impose limitations or guidelines. This would be particularly so if the tenant plans to use equipment or chemicals that emit toxic pollutants.
- **Improvements.** The tenant may wish to add "improvements" to the premises which might be of value to the tenant, but not future tenants. Determine the extent to which the landlord will allow improvements.
- **Right of entry.** It may be in the best interests of both landlord and tenant that the landlord be permitted entry to the premises on an as-needed basis, despite inconvenience to the tenant, even if a shutdown for repairs is necessary. The tenant should plan to cooperate in these situations. Rent abatement for shut-down might be considered.
- **Expense allocation.** A related issue involves the extent to which landlords may treat as operating expenses the costs of periodic testing and of changes to correct problems. Clearly, installation or replacements of heating and cooling systems would be capital improvements. Maintenance costs, such as for cleaning and changing filters, would be operating expenses. Some costs, such as for periodic testing and for minor systems modifications, might not be clearly characterized. From the tenant's point of view, work done before moving in should not be deemed operating expenses. Expenses for periodic testing and minor modification costs, up to a specified limit, might be acceptable to the tenant as operating expenses.
- **Government reports.** Under various federal, state and local laws, landlords and tenants may be required to report to a governmental agency the storage, use or release of hazardous substances. Under the lease, each party should agree to comply with all such laws and to provide to the other party a copy of any filing or report within a specified period following filing. The landlord should also agree to provide to the tenant, within a specified period after the landlord receives it, a copy of any filing or report made by any other tenant of the building.
- **Legal compliance.** The landlord may want to include a provision whereby the tenant is obligated to comply with all present and future federal, state and local laws, including future environmental laws, affecting the leased premises, tenant's business, or any activity or condition involving the premises; to change, reduce or cease any noncomplying activity; and to install pollution control systems, equipment, safety devices and the like in order to comply.