

REAL ESTATE COUNSELORS, PLLC



YOUR BEST DEFENSE

An Experienced Team gets the Best Result for your Real Estate Leases.

Bruce G. Rosen, Esquire ©2010

Introduction. Defense contractors often lease space because of a focused business decision – a contract award or similar market-driven event. Whether it's office space, a warehouse or factory, defense contractors have special requirements and are best served by a experienced team of skilled brokers and real estate attorneys aware of their needs and expectations.

The Team. Involve an experienced real estate broker early on in the leasing process. They are your best guide to what space is available in a given location and if rates and prices quoted to you are above, at or below market. Likewise, protect your interests by engaging attorney *specializing in commercial real estate*, ideally with experience representing defense contractors.

Step 1 - Letter of Intent. The general terms of a proposed lease transaction are put in writing by the landlord or its broker and given to the tenant. This is a *Letter of Intent* or *LOI*. Some parties prefer to negotiate every detail and then execute the LOI. Others start with an unsigned LOI, then jump right to lease negotiations. In either case it's crucial that your LOI includes all critical business terms (and excludes any terms flatly unacceptable to you). Next we discuss key issues that arise in lease negotiations. If they are relevant to your transaction, you may want to address some or all of them in the LOI. Deals slow down (and cost more) when parties try to change LOI terms or introduce new and significant deal points. Getting the LOI right saves time and money down the road.

Step 2 – Key Leasing Issues. There are many significant business and legal issues arising in even seemingly basic transactions. We now focus on those issues most relevant to defense contractors.

What is being leased? The lease should be clear on whether you are leasing interior building space, the entire building, or a parcel of real estate which may include one or more buildings (as well as other exterior areas). Also consider if you need exterior parking or space for an external generator, satellite dish or similar equipment. The scope of what you lease impacts your maintenance, insurance and other important obligations.

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Contingencies. Both your LOI and lease should clearly reflect whether your need for the space is contingent upon you being awarded one or more government contracts. You may have to live with the strict terms of any contingency clause, so make sure all likely possibilities are thought through.

Build-out. Regardless of whether you or the landlord is responsible for getting the premises ready for your occupancy, the lease should reflect any special improvements such as a SCIF or supplement HVAC system. Consider also what improvements the lease requires you to remove at the end of the term.

Operations. Defense contractors' operational issues are different than basic office users. Storage of sensitive technology or hazardous materials may be required. Equipment may need above-standard electrical service. Make sure the operational provisions of the lease match your needs and anticipated use of the site.

Access & Security. Standard lease forms often give landlords the right to enter your premises at any time, for any reasonable purpose, sometimes without prior notice. They may also require you to give your landlord copies of all keys to locked areas in your space. You may not be able to accept the standard language on these points. For certain operations you may want to install your own security system or connect to landlord's system. In any case, your security needs should be appropriately reflected in the lease.

Landlord Remedies. Leases often provide landlords with draconian remedies such as having a lien on all equipment and inventory in your space, and the right to remove you with force following a tenant default. Creditworthy tenants should resist such provisions. Your real estate attorney will help you negotiate a balanced result.

Subcontractors & Other Subletting Issues. If you need to let your contracting partners occasionally work out of your space, make sure the subletting provisions of your lease permit this without landlord objection or additional charges.

Mergers & Other Assignment Issues. Industry consolidation is common. Your lease should permit transfers to any company that you merge with or that acquires your business. Consider the need for assignments to third-parties as well.

Your Space Needs & Flexibility. A tenant's right to extend its lease term, or to expand the premises (or contract if needed) should be clearly set out in both the LOI and lease. Building in flexibility now can prevent difficult negotiations (and disruption of business) in the future.

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A Negotiated Peace – Non-Disturbance Agreements. Two leasing scenarios present special risks: Subleasing space from a tenant, and leasing space in a mortgaged building. In each case a third party may impact your right to occupy the premises.

Subleasing. Your right to occupy subleased-space depends upon your sublandlord staying in good graces with its landlord. If your sublandlord defaults as a tenant under its prime lease, you may be evicted along with the defaulting tenant. If you plan to sublease a large space (5,000 sf or more), for a fair market rate, you may be able to negotiate a protective agreement with the building owner, a non-disturbance agreement. This lets you stay in your space if the tenant defaults (for reasons unrelated to your actions). Subtenants leasing small sites, or getting below market terms from their sublandlord, may find landlords unwilling to enter such an agreement, however.

Lenders. Landlords with mortgages on their buildings present the same risks to tenants as subtenants face. If the landlord defaults in its mortgage, you may be evicted from your space when the lender forecloses and takes possession of the property. If you plan to lease a large space (5,000 sf or more), for a term of 5 years or more, you may be able to negotiate an agreement with the landlord's lender to let you stay in your space, even if the landlord defaults under its mortgage loan. This is known as a subordination, non-disturbance agreement or SNDA for short. Lenders are very hesitant, however, to enter into such agreements with tenants leasing small sites, or for short-term occupancies.

Final Thoughts. These are only a handful of points which may be relevant in your leasing transaction. An experienced leasing team, focused on your business needs, is the best defense against leasing headaches.



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Real Estate Counselors is a boutique law firm specializing in commercial real estate and business transactions.

Bruce Rosen's practice includes representing defense contractors, national retailers and real estate investment trusts. He is the Managing Partner of Real Estate Counselors. Prior to that, he was with the law firm of Akin, Gump, Strauss, Hauer & Feld.