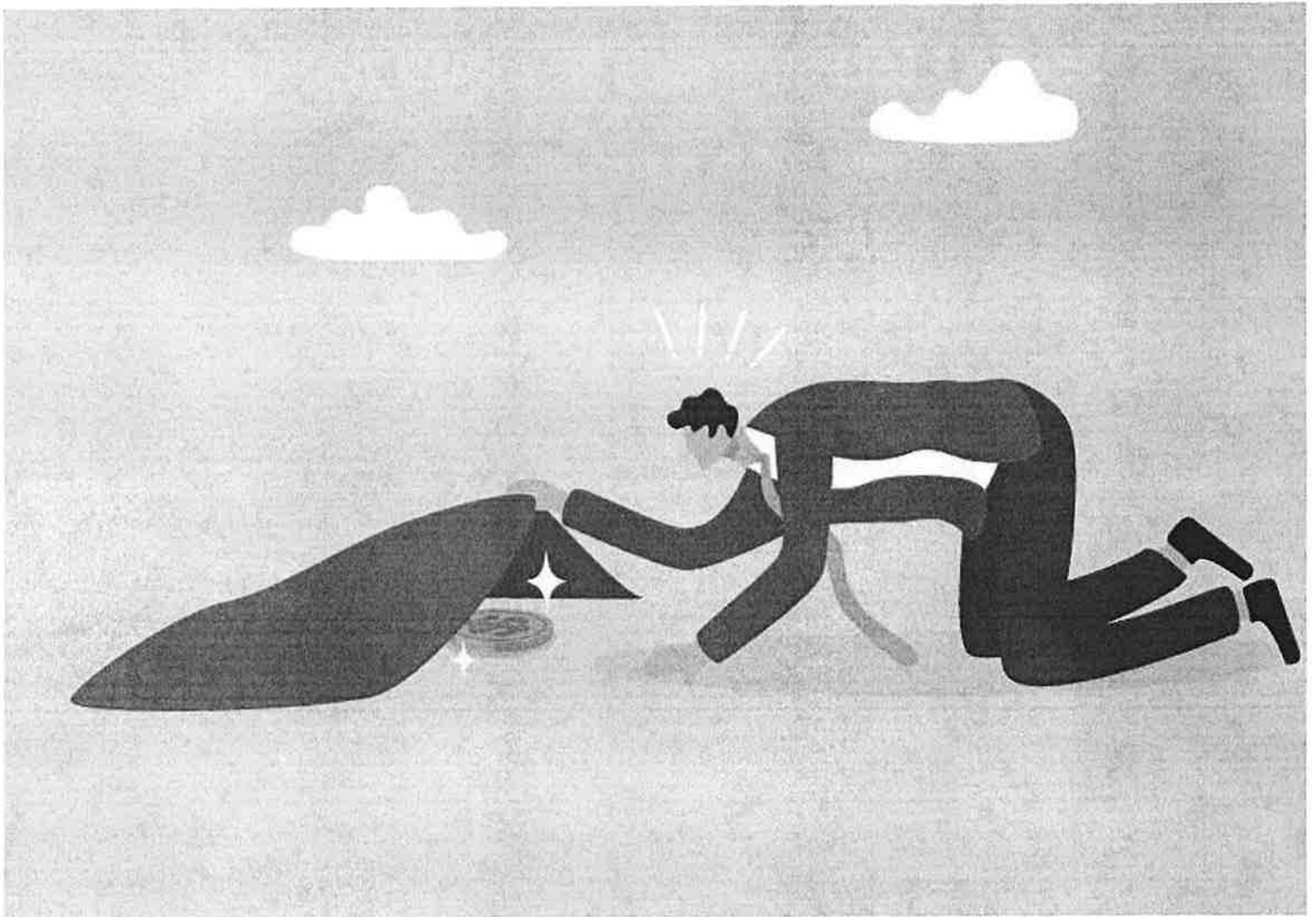


Hidden Costs of Commercial Leases

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Finding a new commercial tenant for a co-op space and negotiating the lease can be challenging. While filling an empty space is key, often money will have to be spent upfront on renovations and broker fees. A big part of the negotiations will be how to pay for these costs and when. Of course, you'll also want to find a tenant that can live happily within a residential setting.

THE RIGHT TENANT Along with financial concerns about a new tenant, there are lifestyle issues that you will want to consider. These can limit who you will want as a commercial tenant. For example, very few boards will agree to rent to an after-hours club because they don't want large noisy crowds outside at 2 a.m. Medical facilities and food establishments also present concerns for co-op shareholders. A supermarket will have loud deliveries in the morning and a lot of trash in the

evening, and restaurants involve cooking aromas and venting issues. A marijuana dispensary might also present image problems for a co-op.

RENT CONCESSIONS In most cases, a broker will negotiate the financial terms of the lease, including the base rent as well as any rent abatement to cover necessary renovations or space reconfiguration. We had a building where a delicatessen moved out after 30 years, taking their big freezers and refrigerators, and a lot of work had to be done to fix up the space. In a situation like this, you might give the new tenant three months rent free while the renovation work is being done. However, the lease may be over ten years, so rather than giving the tenant free rent upfront, it may be better for the co-op to spread the concession over time. In this way the co-op satisfies its own cash-flow issues.

BROKER FEE Commercial brokers earn fees, and they often want to be paid at lease signing. Their fee might be on a sliding scale, say 3% of the first year's rent, 2% of the next three years and 1% of the next four years. The co-op typically pays the tenant's broker a full commission and its own broker, if it has one, a half commission. Depending on the rent, broker fees could be several hundred thousand dollars, funds a co-op may not have. Just as with the rent concessions, I would negotiate to spread that payment over time. Brokers won't like that, but if they want the transaction to happen they will generally work with you.

BOTTOM LINE You want a viable tenant, even if you have to spend money upfront to get one.