

REAL ESTATE COUNSELORS, PLLC



ONE LEASE DOES NOT FIT ALL

*Professional Office Tenants in Retail Projects
have Unique Issues that should be addressed*

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Introduction. To provide their clients with more accessibility and convenience, dentists, optometrists, veterinarians and other professionals are gravitating to space in retail settings. Retail landlords typically have only one lease form that they provide to all of their tenants (including professional tenants). Professional tenants in a retail project are advised to pay particular attention to certain lease provisions typically found in retail lease forms but often times not applicable to a professional user.

Some key provisions to be aware of are as follows:

- **Use and Operations.**

- **Permitted Use.** Landlords under a retail lease want to retain tight control over the use tenants make of the property. A professional tenant needs to have the flexibility to modify its use from time-to-time to add ancillary services.
- **Trade Name.** Retail tenants often conduct their business under a specific trade name and the lease usually provides that changes to the name must be approved by the landlord. Lease provisions relating to trade names are generally not relevant to professional office tenants.
- **Continuous Operations.** Landlords require continuous operation and extended hours for retail tenants because tenants in retail centers typically pay a percentage of gross revenues as additional rent - percentage rent, so a tight control on hours and operations is essential to maximize the tenant's profits (and increase Landlord's percentage rent). Additionally, retail tenants are often interdependent on one another for success. A full, open center benefits all of the tenants and enhances the value of the property.

Continuous operations and extended hours may not make sense for a professional, such as an accountant. Such provisions should be flexible to be more suitable for professional office tenants.

- **Radius Restrictions.** A retail tenant's lease will often contain radius restrictions. This is an agreement that a retail tenant will not open a competing business within a certain radius from the premises. The landlord aims to avoid low sales due to market saturation, and more importantly, the landlord aims to create exclusivity and drive as much traffic as possible to its own retail centers and (when applicable) increase percentage rent. Radius restrictions are not applicable to a professional tenant and should be stricken from the lease.
- **Transfer Provisions.** In a true retail lease, landlords typically prohibit the tenant from assigning the lease, or transfer a controlling interest in the tenant's business, since the landlord typically believes that the owner of the retail business may have a significant connection with its operations, and a successor may not run the business as well.

In professional leases, a landlord should agree not to unreasonably withhold its consent if the tenant desires to assign the lease or transfer a controlling interest in the tenant's business. This is especially true for regulated professions, since the regulating body assures the landlord that the successor will be qualified.

- **Economic Issues.**

- **Gross Sales Reports.** As most retail leases contemplate percentage, the lease form typically requires the retail tenant to provide monthly, quarterly or annual statements of gross sales. A professional tenant should try to strike such a requirement, or at a minimum add language requiring the landlord to keep such information confidential.
- **Operating Expenses.** Retail leases treat operating expense pass-throughs differently from professional office leases. The retail tenant pays the tenant's share of taxes, maintenance, and insurance, in addition to base rent.

In most office leases, tenants pay their share of operating expenses only if those expenses exceed a base year or expense stop. It's important for the tenant to understand the differences when they are comparing professional space in an office building to one in a retail center.

▪ Construction and Maintenance.

- **Interior Alterations.** Because retail space is accessed by the general public, a retail landlord will typically require tight control over every aspect of a retail tenant's build-out. A retail tenant seeking to make interior alterations will have to submit their plans and get approval of the landlord. The landlord will often not allow even minor alterations without approval.

Interior alterations are not as significant for professional space. In professional leases, a landlord should agree not to unreasonably withhold its consent if the tenant desires to perform interior, non-structural alterations.

- **Maintenance Obligations.** Retail tenants are generally responsible for all maintenance and repair within the walls of their premises. This can include the replacement of the HVAC unit serving the space and can be quite expensive.

In a professional office lease, most repairs and maintenance are performed by the landlord. Professional office tenants should review the lease provisions to ensure they have an understanding of maintenance obligations and the financial burdens they entail.

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

Peter Pokorny focuses on commercial real estate leasing and business transactions. Prior to joining Real Estate Counselors, Mr. Pokorny was counsel to the Real Estate Practice Group of the Pennsylvania Bar Association. He also served as Assistant General Counsel for the Council of Better Business Bureaus, the network hub for BBB's in the US and Canada.