



Preliminary Negotiations of a Commercial Lease Agreement Between Landlord and Tenant

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This article deals with the preliminary negotiations between a prospective landlord and a prospective tenant. We make a couple of assumptions as follows:

From the perspective of the landlord:

1. The landlord has already chosen a qualified real estate broker to represent them exclusively in the leasing transaction, and a prospective tenant has requested a proposal outlining the basic lease terms for the available facility.
2. The landlord's next step is to make a written offer to the tenant outlining the basic terms and conditions upon which the landlord will lease to the tenant the desired facility.

From the perspective of the tenant:

1. The tenant has already chosen a qualified real estate broker to represent them exclusively in the leasing transaction, and together they have performed a site selection narrowing the field to one or two locations.
2. The tenant's next step is to make a written offer to the landlord outlining the basic terms and conditions upon which the tenant desires to lease the preferential location.



We suggest using a non-binding, in-formal document commonly called an "**Expression of Intent to Lease**" as the negotiating tool. Each lease transaction is an individual situation and has distinct problems associated with it, and while the below items are not all inclusive, they do cover a majority of the items that landlords and tenants spend most of their time negotiating.

We recommend the following items be included in the Expression of Intent to Lease. Please see below for more detailed information on each of the following sections:

- General Information;
- Summary of General Terms;
- Financial Consideration;
- Tenant Improvements;
- Other Terms Desired;
- Tenant Approval;
- Good Funds and Good Faith Deposit;
- Time is of the Essence and Remedies;
- Good Faith Deposit Dispute;
- Agency Disclosure
- Recommendation of Legal Counsel
- Summary and Signature of Parties

In addition, the proposal should include at least three attachments:

- The authorizing Corporate Resolution;
- A Credit Report Authorization; and
- The Broker's Commission Agreement

The **General Information** section should include the date, proposed address, suite or bay number, city, county, and state of the location. The following sentence should be included to protect the tenant from unintentional misinterpretations:

"This Expression of Intent to Lease is NOT BINDING on either party herein named, and only will be binding WHEN, AND AFTER there is a definitive lease agreement EXECUTED by both parties."



The **Summary of General Terms** section should include the following:

1. Square footage of the premises (rentable and useable square feet);
2. The premises' percentage of building leased;
3. Name, address and phone numbers of landlord or property manager acting for the landlord;
4. Tenant's name, address and phone numbers;
5. If required, the Guarantor's name, address and phone numbers;
6. The lease term and renewal options or first rights of refusal options; occupancy date and termination date;
7. The authorized use of the premises; and
8. Amount of Good Faith Deposit, if applicable.

The **Financial Consideration** section should include the following:

1. The initial amount of rent;
2. The amounts of pro rata common area maintenance (CAM) charges, if any, including: maintenance, management fees, reserves, property insurance and real estate taxes; and
3. The amount of the security deposit.
4. There should be a paragraph or section outlining the rent per month for each year of the lease term, when the rent will increase and to what amount if it is a fixed rate increase, or if a percentage rate increase, on what the percentage rate increase is being based, i.e. national or regional cost of living indexes;



5. Finally in this section there should be a summary paragraph indicating the total amount of funds required to be provided by the tenant at the time of execution of the formal lease agreement, i.e. 1st month's rent and CAM charges, plus the security deposit, less any previous good faith deposit.

The next section should outline what **Tenant Improvements** are requested from the landlord, and/or what tenant improvements are to be provided by the tenant at tenant's expense. It has been our experience that this is the area where most disputes arise. We suggest that the more detailed the descriptions can be, and who is going to pay for the improvements, the better understood it will be by all parties.

The **Other Terms** section should include a paragraph holding the landlord harmless from any claims from any brokers other than the one exclusively representing the tenant and the one representing the landlord. In addition, the tenant should indicate that they will provide a corporate resolution authorizing the signatory to sign on behalf of the corporate entity.

The **Tenant Approval** section should indicate what financial information the tenant and guarantor will provide to the landlord for approval of the tenant's financial condition. Usually this includes a signed and dated financial statement, and if unaudited, the tenant will more than likely be asked to provide two years of IRS tax returns. The tenant/guarantor will also have to provide a signed Authorization for Credit Approval, as well as a good faith deposit.

In the **Good Funds and Good Faith Deposit** section, the tenant indicates what amount of funds they will provide as "Good Faith" of their willingness to proceed with the negotiation process. In exchange for receipt of the good faith deposit, the landlord should withdraw the desired space from the market until negotiations are either concluded or terminated. The tenant should include a statement indicating the time and date that the tenant's proposal will expire, unless the landlord responds to the tenant's proposal. In the event that negotiations are terminated by the parties, the tenant should expect return of the uncashed good faith deposit without delay, usually within 24 to 48 hours of termination.



Time is of the Essence and Remedies section covers the transfer of the negotiations from the one party to the other with a response from the receiving party at the earliest possible time.

The **Remedies portion** covers what is to happen with the good faith deposit. As indicated above, if negotiations are terminated before a definitive lease is prepared, in most cases the landlord returns the good faith deposit. However, when a landlord accepts the terms as outlined within the Expression of Intent to Lease, takes the desired space off the market, prepares a definitive lease agreement for the tenant and his attorney to review, and the tenant then decides NOT to pursue negotiations in good faith to resolve any disputed lease terms or conditions, the tenant may lose their good faith deposit.

The deposit may be considered LIQUIDATED DAMAGES, which would be the landlord's SOLE AND ONLY REMEDY for the tenant's failure to execute the definitive lease agreement. **This is a very important aspect of the Expression of Intent to Lease, and should be fully understood by all parties as to the consequences in the event of the tenant's failure to perform.**

The next few sections are boiler plate, designed to protect the Listing and Leasing Brokers from being put in the middle of a legal dispute between a tenant and the landlord.

There should be a **Good Faith Deposit Dispute** section covering what happens in the event of a dispute between the landlord and the tenant.

The **Agency Disclosure** section, wherein the Listing and Leasing Brokers disclose in writing with whom they have an agency relationship and what form that agency relationship takes.

The **Recommendation of Legal Counsel** section, whereby the Listing and Leasing Brokers recommend to the parties to consult with their own legal counsel regarding any examination of the definitive lease agreement, or other related issues.



The **Summary and the Signature of Parties** sections indicate that this is all that is being proposed by the original offering party, as well as the signature of the parties, including a date and time of the signatures, indicating acceptance of the proposal as written. If the receiving party does not wish to accept certain provisions being proposed by the offering party, a written counter proposal indicating which areas are to be modified should be issued.

The three attachments accompanying the Expression of Intent to Lease are:

1. A copy of the tenant's **Corporate Resolution** signed by the corporate president and secretary or in the case of a LLC signed by the managing member authorizing the signatory to negotiate, sign and commit the corporate entity to the definitive lease agreement;
2. **Credit Report Authorization** form which allows the landlord to access the tenant's, and any guarantor's, credit reports; and
3. The **Commission Agreement** section which is the landlord's written agreement to compensate the Listing and the Leasing Brokers for their services assuming that the definitive lease agreement is executed by the parties. Tenants for the most part need not worry about this portion of the Expression of Intent to Lease, unless they have agreed to separately compensate their Leasing Broker. A real estate broker is not authorized to receive compensation from both parties, unless the broker has obtain written acknowledgment from both parties.

With mutual acceptance of the Expression of Intent to Lease, and upon receipt of the definitive lease agreement, it is time to have it reviewed with the tenant's legal counsel. Minimum changes relative to the individual situation may be able to be incorporated into the landlord's standard lease agreement, but tenants should not anticipate major changes to the lease agreement will be acceptable to the landlord. After tenant's attorney's review, we recommend discussing any requested changes with your real estate broker prior to having written requests for changes submitted to the landlord.



Lastly, remain flexible in your demands, and attempt to seek common ground to resolve any major issues. By using the above elements as part of your preliminary negotiations of a commercial lease agreement, you can be assured that you will overcome the largest obstacles up front.

Thereafter, the **Final Definitive Lease Agreement Phase** will be an easy transition to getting what you want from a lease situation.

Good luck with your next lease negotiation.

Editor's Note: James T Saint, Real Estate Advocate™ of Halo Realty & Investments Corporation is a CCIM, (Certified Commercial Investment Member). One of a network of 9,000 professionals across North America and 30 international countries holding one of the most coveted and respected designations in the industry, and one often referred to as the "Ph.D of commercial real estate". Mr. Saint specializes in large industrial and office properties for lease or acquisition, as well as tenant or corporate advisory services for improvement of the corporate bottom line. He may be contacted at Tel: (702) 838 - 4226, or by using our web mail form at: www.halorealty.com/contactus.htm.