MAZIROW

COMMERCIAL, INC.

FOUR STRATEGIES TO MITIGATE RISKS OF HOLDOVER

Most building owner lease forms include onerous holdover provisions that, if unmodified, create significant exposure for commercial tenants. A holdover provision typically penalizes a tenant for its failure to vacate the premises in a timely manner at the expiration of the lease. Penalties for holdover generally include payment of increased rent (often at double or triple the rent due during the last month of the lease), and potential liability for consequential damages the owner suffers as a result of the tenant's holdover.

Although, as you know, Mazirow Commercial only represents tenants*, it is not unreasonable* to penalize a tenant that breaches its contract due to its failure to vacate the premises on time. After all, it's foreseeable that an owner could sustain damages due to a tenant's holdover because as long as the tenant remains in the premises, the owner can't deliver the premises to a new tenant. Nevertheless, many tenants find themselves with no choice other than to hold over following lease expiration pending negotiation of a renewal or a new lease. In fact, under threat of holdover and the penalties associated therewith, ***tenants often negotiate lease relocations on above-market terms, with much fewer concessions because their soon to be new landlord senses desperation in the new tenant***.

Because most holdover provisions include severe penalties for holdover, tenants should pay careful attention to the language used to define "holdover" in their leases. In particular, while most leases define holdover as a tenant's continued occupancy of the premises after lease expiration, depending on the language in the lease, holdover might be triggered simply by a tenant's failure to deliver the premises at expiration in the condition required under the lease. So even a tenant that vacates the premises on time could be found guilty of holding over if it doesn't surrender the premises in the condition required under the lease. And such a result wouldn't be totally unreasonable. If a tenant that's obligated to remove significant improvements prior to expiration fails to do so (note, many landlords now are trying to get the tenant to remove IT cabling), the owner will be unable to deliver the premises to a new tenant immediately and will incur the same damages it would have incurred had the tenant continued to actually occupy the premises after expiration.

Although it's easy to understand why owners would use such onerous holdover terms, that doesn't mean that you shouldn't protect your own interests – because if you do not – Mazirow Commercial will!

Holdover provisions typically receive less attention during lease negotiations than provisions (unless, Mazirow Commercial is on your side) that will have a more immediate impact on the landlord-tenant relationship, so landlords typically have greater flexibility when it comes to holdover provisions.

Tenants should be careful to define holdover narrowly, and to limit the penalties and damages recoverable by owners as a result of holdover. Keep in mind that many commercial owners rely on overly ***punitive holdover provisions for leverage during renewal negotiations***.

The following four strategies Mazirow Commercial employs can not only minimize the risk of holdover, but also level the playing field for purposes of renewal.

699 Hampshire Road, Suite 101, Westlake Village, California 91361
Telephone: 805.449.1945 • Facsimile: 805.449.1946
Web site: www.tenantadvisory.com

DELAY ASSESSMENT OF HOLDOVER RENT FOLLOWING EXPIRATION

Landlord lease forms typically require tenants to pay holdover rent at a rate far exceeding market rent. It's common to see a landlord lease require holdover rent equal to between 125 percent and 200 percent of the monthly rent due during the last month of the lease term. To minimize the risk of holdover, tenants are advised to delay any rent escalations for as long as possible.

Many landlords are willing to delay rent escalation during the first 60 days of holdover. Other owners insist that holdover rent begin accruing on the first day of holdover, but they agree to delay significant increases until the passage of 60 or 90 days. Before agreeing to holdover rent of 200 percent on day one of holdover, try to negotiate a lesser amount, say 125 percent or 150 percent, during the first 60 days of holdover. Most landlords are willing to grant a "grace period" before assessing significant rent increases. Mazirow Commercial is successful in doing this.

LIMIT HOLDOVER PENALTIES TO "BASE RENT"

Most leases define "rent" as the combination of "base rent" and "additional rent." (Additional rent typically includes reimbursement for operating expenses, taxes, and insurance.) Many leases that provide for rent increases during holdover ***refer only to "rent," without distinguishing between base rent and additional rent.*** Accordingly, many tenants fall into the trap of agreeing to pay 150 percent or 200 percent of base rent and additional rent during holdover.

The most significant components of additional rent are designed to reimburse owners for actual costs incurred. An owner that receives greater than 100 percent of its actual costs arguably receives a windfall. Therefore, Mazirow Commercial tries to limit any increases during holdover to "base rent."

Sheryl Mazirow, *CCIM*
President

INCLUDE A WAIVER OF CONSEQUENTIAL DAMAGES

Holdover rent is designed to compensate landlords for damages they could sustain as a result of holdover. Accordingly, holdover rent is a form of "liquidated damages." A tenant that agrees to holdover rent in excess of the rent it normally would pay should include a statement that ***holdover rent represents all the tenant will be obligated to pay in the event of holdover***. Language should be included in the holdover provision indicating that holdover rent constitutes liquidated damages, which shall be the owner's exclusive remedy in the event the tenant fails to vacate the premises in a timely manner following the expiration of the lease.

The holdover provision also should include a waiver by the owner of any damages resulting from holdover. While no tenant wants to pay holdover rent, holdover rent can be a benefit to a tenant if it limits its exposure for damages the landlord might sustain as a result of the tenant's failure to vacate the premises on time, such as damages resulting from the owner's inability to enter into a lease with a new tenant.

Sophisticated landlords might be hesitant to waive their rights to recover consequential damages. While many owners are reluctant to agree to an absolute waiver of consequential damages, some landlords are willing to waive consequential damages resulting from holdover during the first 60 or 90 days after the lease expires.

Our Difference is your Advantage

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