

LAST WORD

Subleasing Rules for the Road

Attention to detail helps tenants avoid costly leasing potholes.

By Alicia B. Clark

When Associates Commercial Corp., a financial company, needed more office space and wanted to move, it hoped the process would be easy. There was a tenant in the same building who wanted to sublease the space. All Associates Commercial, based in Louisiana, needed was permission from the landlord.

It wasn't so simple.

The landlord, Bayou Management, refused to consent. Associates Commercial paid 13 months rent and an early lease termination fee. The landlord then leased the office space to subtenant Associates Commercial had proposed, charging them more rent than Associates Commercial had been paying.

Associates Commercial sued. The landlord had to refund the rent and fee. The landlord also had to pay damages for the lost profit Associates Commercial would have made by subleasing the space.

Having a lease that spells out the requirements for a lease transfer or sublease could have prevented pain on both sides of the courtroom aisle. Attention to detail is particularly important these days. The economic downturn has resulted in a significant increase in subleasing activity.

Subleasing unused or unwanted space is not simply a matter of a tenant's finding a subtenant. Most leases today require the landlord's consent. Provisions generally fall into one of three categories:

► **"Silent" Consent Clause:** In this case, consent is required but there is no guidance on the criteria for granting or denying consent. In many states, courts require that the landlord act reasonably.

► **Consent, not to be unreasonably withheld:** This common lease provision is preferable to a "silent" consent clause because it specifically requires the landlord to act reasonably when reviewing a proposed sub-tenancy.

► **Consent, subject to a list of specified standards:** This lease includes a list of standards for approval and a provision that the landlord may refuse consent if the standards aren't met.

Courts have held that arbitrary considerations, such as "personal taste, convenience or sensibility" are not appropriate reasons to refuse consent. A refusal must be based on something "objectively sensible and of some significance." For example, it would be considered reasonable for a landlord to refuse consent if the sublease negatively affected the value, operations or maintenance of the property.

It is also reasonable for an owner to consider the financial strength of the subtenant and the compatibility of the new business with existing tenants. An owner may reasonably refuse consent if the subtenant will increase burdens on building facilities or hurt property value. Another factor deemed reasonable by courts is whether the new tenant will require building alterations.

Owners may not deny consent to a sublease simply because they would prefer to increase the rent, renegotiate the lease or rent directly to the subtenant. It is also considered unreasonable for an owner to require payment from the subtenant in addition to the rent.

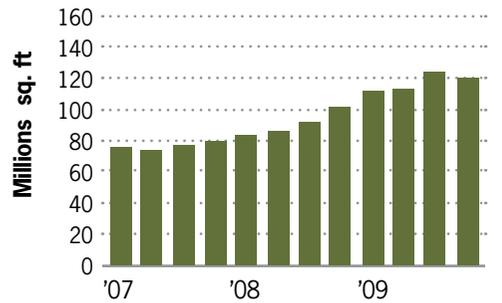
Lease standards are key

Critical time and effort is wasted when a tenant does not understand when a landlord is justified in refusing consent. And landlords subject themselves to the risk of lawsuits if they don't understand the limits of their ability to withhold consent. Leases that provide clear guidance benefit everyone.

To protect the landlord, a lease should include a clause that the sublease won't breach the landlord's obligation to other tenants. It should include a requirement

OFFICE SUBLEASE SPACE ON THE RISE

A growing number of tenants need to sublease space that they have vacated. The original lease can hinder the deal.



Source: Reis

that the subtenant meet specified financial and insurance requirements and that the proposed use be compatible with other uses in the building. Further, the subtenant should not impose burdens on parking or facilities and the tenant not be in default when he makes a sublease request.

To protect the tenant, a lease should require that the landlord cannot deny consent to sublease because he is negotiating with a subtenant for other space in the building. In addition, landlords and tenants will benefit from lease provisions that spell out the type of information a tenant must submit with a sublease request and the amount of time the landlord will have to consider the request and related information.

Properly crafted lease and sublease agreements protect the landlord, the tenant and the subtenant. They can help avoid costly litigation, preserve relationships among parties, and facilitate the productive use of space that would otherwise remain unused or unwanted. Navigating the road to business success isn't easy. But the right tools can smooth an otherwise bumpy ride and, in this economy, that can make a big difference.



Alicia B. Clark is counsel in the Real Estate Department in the Denver office of Ballard Spahr LLP. She practices general real estate law. Contact her at clarka@ballardspahr.com or (303) 299.7341.