



Trends in commercial leasing in New York City - by Michael Nerenberg

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While 2020 has been a year many of us in New York real estate would like to forget, it would be useful to remind ourselves that certain trends that became more noticeable and accelerated during the pandemic actually started years prior.

For several years we have seen retail space in prime areas go vacant as owners maintained empty storefronts rather than (even temporarily) reducing rent for existing or prospective tenants. Contributing factors were online sales and that large companies no longer conceded what was previously an acceptable cost of doing business – multiple flagship locations in Manhattan. Add the addition of retail and office space in Hudson Yards and there was a potential for a crisis in the market well before the pandemic ravaged our great city.

In the last few months, my practice has been devoted to renegotiation of office and retail leases for both owner and tenant clients. Some tenants have been negotiating reductions in lease term, whereby the parties have a mutually beneficial shortened commitment to each other. Alternatively, the parties have agreed to severely reduce the base rent in the short term, with an opportunity to revisit in the spring. While it will potentially take years to recover, many owners are looking at spring 2021 as a time to reassess. This would follow a possible “second wave” of COVID-19, and akin to this summer, be a potential opportunity for outdoor activity that would bring life—and thus business—back to city streets.

Parties have also discussed percentage leasing or “income-based” rent, whereby a tenant pays a reduced base rent, and the owner takes a percentage of the tenant’s gross income. The risk to the tenant is limited, and all parties succeed if the tenant thrives.

Remarkably, there have been new leases being signed in the last few months. Where terms ended during or just prior to the pandemic, tenants were in the enviable position of effectively dictating their own terms either in their current space, where owners were loathe to lose existing tenants, or in the multitude of empty spaces throughout the city. Smaller businesses, perhaps with just one or a few locations, were able to act nimbly and move quickly on an advantageous lease that should allow the business to survive. Larger businesses and national chains are cutting staff and locations, finding that there are not currently enough customers to sustain the existing model of multiple locations clustered closely together.

Tenants in non-essential businesses are taking advantage of Local Law 1932(a), otherwise known as the “guarantor protection clause,” whereby a guarantor is not obligated to guarantee rent for non-essential businesses between March 7th and September 30th. Tenants are utilizing the option to vacate their space with the notice required, whereby there would be no liability on the guarantor for the notice period.

Clients have asked whether their lease had a force majeure clause, whereby their obligations to the lease would terminate—or be suspended—for acts of God. While certain businesses were unable to operate due to COVID-19, it is often difficult to make the case that the pandemic was an “act of God” when the source was animal-to-human transmission. “Acts of God” are generally interpreted as a natural disaster. I do believe, however, that there will be a push to add “government action” to future leases, so that if there is a government-enforced lockdown limiting or shuttering a business’ operation, the tenant’s obligations under the lease would terminate or be suspended.

Another clause I have started negotiating into leases dictates that a lease term will not commence until the business is able to operate. This clause allows landlords to find tenants who would otherwise be skittish to sign a long-term lease, but are willing to do so if the cost to operate is zero until they can open. I would negotiate that the tenant must build-out the space—if that is part and parcel to the lease—during the lockdown period since construction is ongoing. The tenant cannot wait until the business is permitted to open.

As for restaurant tenants, it is unquestionably an impossible time for a sector in which, even in prosperous periods, it is difficult to succeed. There has yet to be a concrete plan as to how indoor dining will be implemented in the city, both with regard to the required health metrics and safety precautions necessary for opening. If a restaurant tenant is to survive the most difficult period of this pandemic—

which I believe to be the coming months of a potential “second wave,” they lose the ability to have outdoor dining due to colder weather, and will need a severe reduction of rent to make it to 2021.

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