

# YOU'RE READY TO SELL YOUR FIRM, BUT IS YOUR LEASE READY?

By: Jack Garson, Esq.

When you started your business on the kitchen table 20 years ago, you didn't know it would grow to be a \$100 million business. But it did.

Even better, you have a buyer for the business and all its assets, including the leases for your various locations.

So, what's the problem?

To transfer your leases, you need the consent of your landlords, and some are balking. One wants a rent increase. Another wants cash for the consent. Still, another wants you to surrender valuable option terms.

These entanglements are going to affect the sale of the business and cost you money.

Your lease should not hurt the sale of your business. But most leases do just that.

Over the years, the restrictions imposed by leases have been limited only by the creativity of the person who drafts them. Formerly simple leases are now 60-page, exhibit-heavy contracts. These super-sized leases restrict who can own stock in your business, to whom you can sell your business and what rights will transfer to any purchaser.

At the very least, landlords should agree not to unreasonably withhold their consent to any such assignment or subletting. However, some decisions to sell your business should not even be subject to your landlord's reasonable consent.

**Waiving the consent requirement.** Savvy tenants get their landlords to waive the consent requirement in certain circumstances.

If you are a franchiser of stores, you might require that the landlord automatically consents to any bona fide franchisee that meets your standard franchisee requirements.

Or if you are a tenant in an office, where each tenant use of

the premises usually is fairly standard, you might require that the landlord agrees to consent to a purchaser of your business who has a certain net worth and amount of experience.

If you have multiple leases, it is important to ensure that no landlord can prevent the sale of your business by withholding consent to an assignment or subletting.

**Limits on stock transfers?** Typical leases also prevent you from selling or otherwise transferring stock (or other equity interests) in your business.

Normally, this restriction applies where you are transferring a majority of the equity in your company.

While most businesses are sold by transferring assets (including your lease), some are sold by a transfer of stock or other equity interests,

especially where certain tax or licensing considerations apply.

Again, your landlord should waive this restriction or agree to reasonably or automatically grant consent when you satisfy certain conditions.

**Keep favorable options.** Your lease may also restrict your ability to sell your business in less obvious ways. Consider the situation where you have an option to renew your lease at a fixed rent. If the fixed rent is or will be below prevailing market rents when you renew, this option to renew can be a valuable asset.

For example, if you are renting 10,000 square feet and your option rent is \$5 per square foot below market, then a five-year option to renew is worth about \$250,000 (\$5 times 10,000 square feet times five years).

Many leases, however, provide that if you assign your lease, the assignee that is, the purchaser of your business loses any such option to renew. That lost option reduces the value of your business to a purchaser, resulting in a lower sales price.



This type of restriction should be eliminated if you are selling your business in compliance with the assignment and subletting provisions of the lease.

**Special retail lease concerns.** Many retail leases require that you pay the landlord a percentage of your sales as percentage rent.

A typical companion of such a provision is a radius restriction that prohibits you from operating another store within a certain radius to prevent you from diverting sales to nearby stores and thereby reduce the percentage rent.

If potential purchasers have stores within that radius, the restriction can limit your ability to sell your business. Any nearby purchasers would automatically be in violation of your lease if they buy your store. Therefore, you must insist on a purchaser exemption to any radius restrictions.

**Avoid hidden traps.** Other seemingly innocuous lease provisions may also impair your ability to sell your business.

The typical commercial lease limits your use of the premises to one particular use. Seems OK, right?

Yet this limitation prevents the sale of your business to a purchaser with a broader use. If you are a dentist and your permitted use is only periodontics, you could not sell your practice to a general dentistry conglomerate that wants to buy it for millions of dollars because the purchaser's proposed use would violate your narrow use clause.

**Pay attention to your business future.** You must review any new lease, or lease renewal, with a critical understanding of all the restrictions in contemporary leases. A minor oversight can cause enormous losses later when you are ready to sell your business. To protect your business future, read carefully, understand your lease and negotiate necessary changes.

## ABOUT JACK GARSON



Jack.garson@offitkurman.com | 240.507.1744

Jack Garson's practice focuses on Real Estate, Construction and Business law. He serves as a legal advisor for numerous local, regional and national companies. In his role as legal counsel, Jack also serves as a strategic advisor and lead negotiator. Further, Jack provides guidance on the structure of complex transactions, the resolution of business disputes, the growth and sale of companies, and the management of issues such as liability and risk reduction, employment practices, and enhancing profitability.

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