

What Should I Be Doing About My Leased Space?

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Within weeks after COVID-19 resulted in many corporate offices sending workers home to work remotely, many of whom had never done so on such a scale, people started talking about whether working from home was becoming a “new normal.” Then those making leasing arrangements for office space for corporations around the world started wondering if they should be asking their landlords for concessions or taking more drastic measures to significantly reduce (or eliminate!) their office footprints. We have counseled landlord and tenant clients in that regard over the last year. Now companies are making plans to bring office workers back to the office. Many are looking at “hybrid” work solutions, although some are focused primarily on either keeping the office workforce remote or, conversely, largely returning workers to the office. This client alert looks at patterns discernible from reports and studies that have been made during the past year, and in particular in recent weeks, and provides thoughts on how such ongoing discussions might inform your company’s considerations of its plans for office space utilization as post-COVID plans take shape.

Relevant questions:

1. Can I (still) push my landlord for rent concessions for under-utilized space?
2. What can I do to reduce my office space without paying (or overpaying) for landlord cooperation?
3. What else should I be thinking about?

This client alert provides practical guidelines for circumstances where conversations with your landlord may be productive and cautions as well against polluting good relationships by making requests that aren’t grounded in either current practice or your company’s circumstances.

Can I (still) push my landlord for rent concessions for under-utilized space?

It is unlikely that asking for rent reductions based on lower-than-expected occupancy of leased space will be successful. We have not seen this strategy be particularly effective in the last year, and as workers start to return to the office the case becomes even less compelling. Many companies successfully transitioned workers to remote working. This meant that company earnings were not

negatively impacted by emptying offices. Noticing that you are paying for space humans aren't fully occupying illustrates only one side of the equation. The landlord may have experienced lower operating costs, but it also had certain increases, and some landlords did see tenants' companies fail (and leases default). Many companies also maintained some level of use of their full space. Their FFE (furniture, fixtures, and equipment) remained secure in the space. Employees came in from time to time. The entire space may be desired as COVID -19 restrictions abate and employees return.

What about reducing space or terminating leases?

If your company is considering consolidating and needs less space, you likely want to talk to your landlord about terminating your lease (or a portion of it) or subleasing. Typically, before you talk to your landlord, you want to be as clear as you can be on your plans. If you desire to move, for instance, do you have a new location in mind already – and some idea of what your timing would optimally be? (Don't forget to take into account recent supply chain challenges – cost and availability of building materials – in considering any tenant build-outs you may need.) The less you know about your plans, the less productive conversations with your landlord will be. Simply raising the issue of wanting a change to your lease without providing any parameters doesn't give the landlord anything concrete to work with or plan around. In any event, given the volatile leasing market, even including that many think the market is somewhat tenant-friendly, do not anticipate that landlords will leap to provide this kind of concession to your expenses (and their income streams). Working to keep an existing tenant happy is less of a factor if the tenant is seeking to reduce or terminate its space in a landlord's building.

Are other concessions appropriate?

Are you planning on keeping or expanding existing space? Your continued commitment to your space could prove helpful to you. Is your landlord already upgrading cleaning systems and/or ventilation systems? Are you looking at reconfiguring your space now that the trends may be shifting more quickly away from denser office layouts – or away from so much open concept seating¹ or free-addressing that has people regularly sharing spaces? Are there things that employees miss about being in the office that should be informing how you think about your space as people return to the office (better collaborative spaces)? Are there things you could use help with if you are shifting to a hybrid model where employees are in the premises part of the week but not others – and not all at the same time (for example, improving infrastructure and technology to assist with more agile office space)? Also, can you offer anything in exchange for your landlord providing something outside of the existing lease requirements – such as an extension of the lease term?

One problem with the planning for more flexibility in office space is that people simply do not know yet what is going to work. There are numerous articles these days about the disconnect between what employers think their employees should be doing and what employees want. But employers have generally not implemented and employees have generally not worked under a hybrid model yet. I've been saying for some time that even folks who think the COVID-19 is going to create some interesting new choices may not be aware of what sort of flexibility is anticipated – we are in an “and” environment right now, not an “or” environment, where employees and employers want the best of both virtual and in-person efficiencies, but most folks don't really know how that works when we aren't operating in a pandemic forcing certain behaviors. How do companies optimize on some people being in some of the time? (Or would they prefer days where almost everyone is in the office, to maximize the possibility of having those accidental interactions that employees have been missing and to reduce FOMO – Fear of Missing Out – by those who would otherwise prefer to work at home some days or hours?) Your workplace will likely be re-imagined (likely more than once!) going

forward as people navigate new possibilities and also the limitations those bring. Your company's unique circumstances will play an important role in determining how your office functions going forward, so your workforce and company can reap the benefits of efficiently working from home without losing the advantage people sometimes get by working together in person, particularly for companies (or teams within companies) that function best as teams or where there are newer team members that need the mentoring and "presence" with more senior people to properly progress and achieve. If you are not yet in a position to know what you and your employees want out of your workspace, it might be too early to talk to your landlord about your lease agreement.

What limitations do landlords face in offering concessions?

Let's assume you are ready to talk re-imagined space needs with your landlord. A pillar of all negotiations should be borne in mind – get an understanding of what is important to the other side. Besides not wanting to make less revenue, landlords have to consider whether providing concessions to one tenant will "open the floodgates" to requests from other tenants. Also, most landlords have financed their buildings, and their lender would have to approve lease revisions, particularly those affecting their borrower's income stream. Where you are located may have a big influence on your landlord's willingness to make changes not required by your lease agreement – some markets remain relatively robust, and less pressure exists on landlords in those cities. (Or alternatively, they may feel more optimistic about replacing certain tenant space with a new tenant.)

Finally, be aware that once you have received some sort of assistance from your landlord, you will be less likely to receive other concessions that could be more meaningful to you and your employees in the long run – particularly if you approach your landlord for reasons your landlord deems "greedy" or unfairly opportunistic and not well-tuned to your needs and market conditions. Unless you have clear plans for your use of space and are ready to commit to those plans, this may be the worst time to ask your landlord for changes to your lease. Landlords hearing about a tidal wave of lease renegotiations will feel more resistant until they know what they are actually facing. If companies are going to implement truly hybrid workplaces, and if they in fact bring back more people, more often, and at similar or higher uses of space, landlords may feel less anxious about finding replacement tenants for those companies that actually do implement smaller footprints. They will also be more open to discussions about next steps if you can commit to what your next steps are. If you don't know yet, it's probably too early to tell your landlord you'd like to talk about reducing your rent. The landlord will want to protect its investment in (and financing on) its building. However, if you have clarity on what you need from your space, and it's different from what you have now, you can start planning with your landlord for ways to seek mutually acceptable plans for changing your lease obligations.

¹ A pre-COVID study (December 2019) in Harvard Business Review found that face-to-face interactions dropped by roughly 70% after firms moved to open floor plan offices, while electronic interactions increased, making long-term deployment of such plans questionable when people return to the office specifically to interact with one another.