

Surplus Office Space? Here's What You Should Be Thinking About

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What You Need To Know:

- Office space needs are in a time of flux like no other.
- When a company finds itself with excess office space, subleasing becomes a prime solution.
- Subleasing differs from direct leasing in numerous ways that you need to be mindful of before starting the process.

"When will I be required to return to the office?" is one of the most common questions employers hear from their employees these days. The answer to this question varies by industry and specific employer. For example, the tech sector, among others, is seeing a noticeable shift away from the need for office space in the near future and beyond.

In August and September 2020, the Savills Technology Practice Group (Savills) conducted a survey with several hundred tech sector tenants "to gauge the anticipated impacts of COVID-19 on their plans for office space both in the near term and in a post-vaccine world."¹ Savills found that 82 percent of the tech companies surveyed anticipated needing less office space over the next 12 to 18 months, and 55 percent of respondents had plans to dispose of existing office space over that time period.²

The diminishing need for office space has led many companies to realize they have surplus space and to explore disposing of that space. Unfortunately, disposing of surplus space is not as easy as it might seem at the outset. An early termination or "give back" right is not common in a lease, and would have been negotiated, at a

price, up front. So, if you are in this predicament, the first option is to approach your landlord and attempt to negotiate the surrender of the surplus space or an early termination of the lease. However, you will likely find your landlord is resistant to taking back surplus space because of the current oversupplied market for office space, or will consider doing so only at an exorbitant price.

Since it is unlikely that you will be able to give up your surplus space or terminate your existing lease, the next option is to sublease the space, because you will be able to recoup some of the losses in space that you would otherwise not be using.

Although the oversupply of available office space will likely drive down rental prices, and subleasing your surplus space will add to this oversupply, subleasing can still be a smart decision in the current market.

If you have decided to sublease some or all of your space, here are the initial steps a tenant (and future sublandlord) should be thinking about:

¹ https://www.savills.com/research_articles/255800/306105-0/covid-19-impacts-on-the-technology-industry

² Id.

The first step is to review your existing lease. A typical lease will contain specific subleasing requirements and limitations. You should review these provisions to understand your rights, obligations, and limitations related to subleasing any or all of your leased premises. Although each lease will be negotiated differently, there are certain common rights, obligations, and limitations for a tenant looking to sublease its space. For example, a tenant may be required to provide notice to the landlord of the tenant's intent to sublease and will almost certainly be required to receive consent from its landlord prior to consummating any sublease. You may need to notify the landlord even before the sublease space is put on the market. There may be other timing requirements or obligations that a tenant should be aware of and adhere to. Adhering to these requirements or obligations will prevent the landlord from blocking a potential sublease deal. Additionally, you should review your lease to see if the landlord has any rights to take back the space (a "recapture") and terminate the lease, which would be a happy result in this situation. You should also be wary of any limitations you may have on subletting your space. These limitations might include the quality of the subtenant, the permitted uses of the premises, the number of users permitted to occupy the premises, or the ability to divide an existing suite. A draconian example we sometimes see is that the tenant is required to use the landlord's broker choice to market the sublease space.

The second step is retaining a broker. Not all brokers are created equal, and this is particularly true when it comes to subleasing. You will want to find a broker experienced with subleasing and familiar with your local leasing market. In a city like New York, that market expertise can be hyperlocal to a smaller subset of the city. Once you identify a broker, the broker will want to enter into a brokerage agreement with you. It is important to get legal advice before entering into this brokerage agreement because this will be a new experience: You are now acting as the "landlord" in the sublease and will be responsible for paying the broker commissions if a sublease is ultimately consummated. There is typically no payment required unless a sublease is consummated. The broker exclusivity, duration of that exclusivity, commission rates, and commission payment schedule are all items that are negotiable when you enter into a sublease brokerage agreement. The commission is of particular note because it pays not only your broker, but also the subtenant's broker. It is important to strike the right balance so both brokers are

incentivized to work as hard as possible to find a subtenant for your space without you being taken advantage of in the process. Additionally, although this is unlikely to occur, many brokers seek the same commission for "negotiating" with the landlord to take back the space as the broker's commission for finding a subtenant. Reaching out to your landlord before engaging a broker can save you this broker's commission if the landlord is willing to take back the space.

Regardless of whether you are just contemplating disposing of surplus space or are ready to negotiate a sublease agreement, please contact one of the authors of this Client Alert to provide counsel each step of the way in this process. We can assist with analyzing your current lease, recommending brokers, negotiating broker agreements, and, ultimately, drafting and negotiating your sublease documents.

To see our prior alerts and other material related to the pandemic, please visit the [Coronavirus/COVID-19: Facts, Insights & Resources](#) page of our website by clicking [here](#).

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