

How to get besieged landlords to grant you—a financially squeezed retail or restaurant operator—relief.

## Getting noticed

### Lease restructuring done right

By Jared Morgan

All markets have changed dramatically. The Dow industrials have declined six consecutive quarters, restaurant same-store sales have dropped and real estate values have fallen anywhere from 20 to 50 percent. As a responsible operator who understands the role of real estate in the business, you owe it to yourself, shareholders, lenders and owners to critically review your lease obligations to ensure long-term viability of your stores.

The reality of the current economic environment prevents us from burying our head in the sand and pretending that business has not changed dramatically. As a result, operators are engaging third-party advisors to take on the challenging and sensitive role of negotiating with property owners. Right now a typical restaurant property owner has a stack of rent relief requests buried on their desk, and the pile is growing daily. Third parties are racing to the owner's doorstep with form letters threatening a store closure or lease rejection "unless something is done." I like to call this "the hammer approach." Rent relief, lease

abatement, rent restructuring, however you want to term it, is prevalent in today's market. Blanket requests are flooding the property owner's inbox as outside hired guns try to pick off the low hanging fruit and generate some temporary rent savings. The challenge facing restaurant operators is no longer pursuing lease restructuring, but rather how to move your rent relief request to the top of the pile.

#### First Step: Understand your audience

Current market conditions provide the opportunity to negotiate with landlords for some form of relief from lease obligations. I need to stress "form of relief"—let's not focus only on rent. Yes, rent abatement is the easiest form of relief for the operator or the third party chasing fees based on a percentage of savings, but it also can be the most sensitive deal point for the owner. A simplistic approach to a property owner will likely initiate a prompt response of "NO."

And let's not forget about the local lenders, managers of securitized CMBS pools, joint-venture partners, or anyone else who has recourse

to the restaurant (collateral) and final authority over decisions. In many lease restructurings, it is important that the appeal targets all decision makers, as opposed to just the name on the rent check.

Choosing the right third party that will approach negotiations from a well-informed, fact-based and long-term perspective is critical to bringing the owner's decision makers to the table.

#### Second Step: Creating the right approach

A common misconception among operators in the industry is that when targeting an owner for rent relief, the hammer approach works best. This may work if the operator is close to filing for bankruptcy, but not worth the inevitably damaged relationship with the landlord. When engaging a third party to pursue relief on your behalf, the more leverage



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and information the negotiator brings to the discussion, the higher the likelihood of having a productive exchange of ideas. Aggressiveness is one important aspect of negotiating style, but is more effective when coupled with the other tools required to convincingly present an argument for relief from lease obligations.

### Third Step: Creating tools for success

Be prepared. In too many cases the rent-relief game results in a third party dialing for dollars, and franchisees being represented by someone with little understanding of the intricacies of the sector. Next to the phone of that advisor is an address, rent per square foot and table calculating fees generated from savings. If I receive that call, I'm hanging up after the 10 seconds it takes to realize this person knows nothing about my site. An analysis of store-level performance data in conjunction with a thorough understanding of what makes that specific restaurant successful in the marketplace is critical prior to making any request. You need an outside party that understands all components of the lease, local market fundamentals, the store's performance relative to its peers, and the overall strengths/weaknesses of the relevant credit. The ultimate rent restructuring warrior is a hybrid of attorney, local broker and asset manager, all wound into a creative and experienced negotiator. Once you have identified the right warrior and collected the information needed to lay a foundation for the leverage, how does your advisor best execute lease restructuring negotiations?

### Final Step: The art of execution

Try to enter into every negotiation with the attitude that you can structure a win-win situation. Packaging solutions prior to that first phone call will get the owner's attention and drastically increase your hit rate. Below are examples of structures that will make you successful:

- **Give and take.** Commitment and term are as, if not more, important to an owner in this environment. The owner may come out with less rent but now has an additional five-year commitment. If a restaurant is sustainable in the market, improved unit-level metrics (reduced rent) combined with a longer term will potentially create more value for the owner.
- **Share information and tell the owner something they do not know.** The exchange of information can trigger productive conversations.
- **Make the operator accountable.** Structure performance terms that allow the owner some upside when the market finally turns.
- **Get creative.** Most restaurant deals are structured full net leased deals with all expenses passed through to the operator. Bypass lender constraints and push taxes back to the owner for a period of time. Southeastern restaurants paying higher insurance premiums during hurricane season, negotiate some seasonal relief.

Bottom line is that if you have not already engaged in this practice, you need to look at contributing to that owner's stack of requests. <sup>FT</sup>

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