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# Fundamentals of Subleasing

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Presenters

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# Fundamentals of the Sublease Agreement

## Comparison between Sublease and Assignment

- Whether to assign or sublease

## Basics of Liability under a Sublease

- Tenant remains directly liable to Master Landlord for remainder of Term
- Subtenant only liable to Tenant under the Sublease

## Tenant Has Minimal Operational Responsibility for Subleased Space

- Master Landlord remains responsible under Master Lease
- Tenant's obligation is to try to enforce Master Lease for Subtenant

## Master Lease Incorporated by Reference into Sublease

## Nearly All Leases Require Master Landlord's Consent to Sublease or Other Transfers



# Factors to Consider When Making the Decision to Sublease the Premises

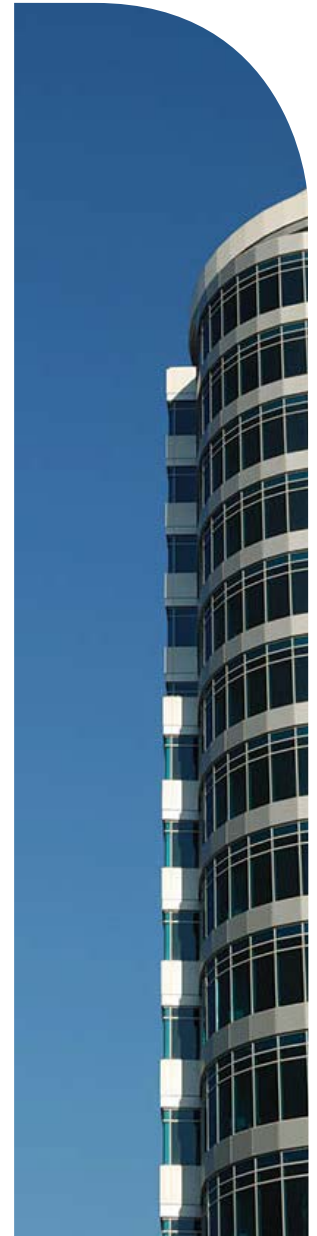
## Review the Master Lease Provision on Transfers to Determine Process and Timing

## Review Specific Restrictions on Transfer in the Master Lease

- Existing tenants of the Building
- Third party Master Landlord has been or currently is negotiating with proposed Subtenant
- Use Restrictions
- Cotenancy and other retail specific issues

## Does Master Landlord Have a Right to Recapture?

- Is Master Landlord likely to Recapture in this market based upon the Master Lease terms?
- Is Recapture a desired result?
- When in the process must the Recapture right be exercised by Master Landlord?



# Factors to Consider When Making the Decision to Sublease the Premises (Continued)

## Determine Whether Tenant is Obligated to Pay a “Transfer Premium” to the Master Landlord for Sublease Profits

- Consider separate payments for existing Alterations
- Consider separate payments for Personal Property (e.g., FF&E, IT equipment, and security systems)

## Determine Whether Tenant will lose any Important Rights as a Result of the Sublease

- Expansion or Contraction Options, Signage, Renewal Rights, Competitor Restrictions
- Consider any RSF thresholds to lose rights and plan accordingly



# Factors to Consider When Making the Decision to Sublease the Premises (Continued)

**If Tenant is in Default, Master Landlord may be Able to Withhold Consent until the Default is Cured**

**Determine Whether There are Any Existing Improvements Requiring Restoration at the End of the Term**

- Is Subtenant taking responsibility to restore existing Alterations?
- If Tenant retains responsibility how much time will be needed to restore at end of Sublease Term?





# Key Letter of Intent Terms in Typical Sublease Agreements

**Base Rent, Annual Increases, Free Rent Periods**

**Tenant Improvement Allowance**

**Pass Through of Operating Expenses**

- Triple Net Lease
- Gross Lease (and consider impact of Base Year)

**Term Length and Renewal Options**

**Condition of Premises upon Delivery**

- As-Is
- Does Tenant need to make any improvements?

**Inclusion or Exclusion of Existing FF&E**

**Penalties or Termination Right for Late Delivery**



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# Key Letter of Intent Terms in Typical Sublease Agreements (Continued)

## Restoration Obligations

## Security Deposit or Letter of Credit

- Letter of credit is better security if there are issues with bankruptcy

## Benefit of Expansion or Contraction Rights

## Termination Right If Master Landlord Does Not Consent

## Requirement to Obtain Recognition Agreement

## Required Changes to Master Lease Approved by Master Landlord



# Process and Issues of Obtaining Master Landlord's Consent to Sublease

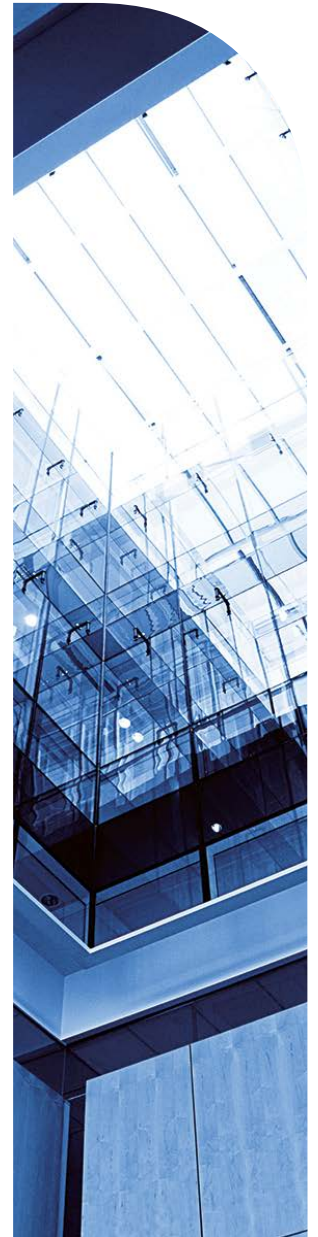
## Understand Timing and Process for Requesting Consent to Sublease

### Consider Whether to Approach Master Landlord at LOI Stage

- Request Master Landlord's Consent form early if Sublease Term commences soon
- If Master Landlord has right of Recapture request Consent and waiver of Recapture

### How the Consent to Sublease Works

- Three parties to this Agreement (Master Landlord, Tenant, Subtenant)
- Subtenant agrees to attorn to Master Landlord upon termination of Lease
- Modifications to Master Lease applicable to Subtenant contained in Consent





# Process and Issues of Obtaining Master Landlord's Consent to Sublease (Continued)

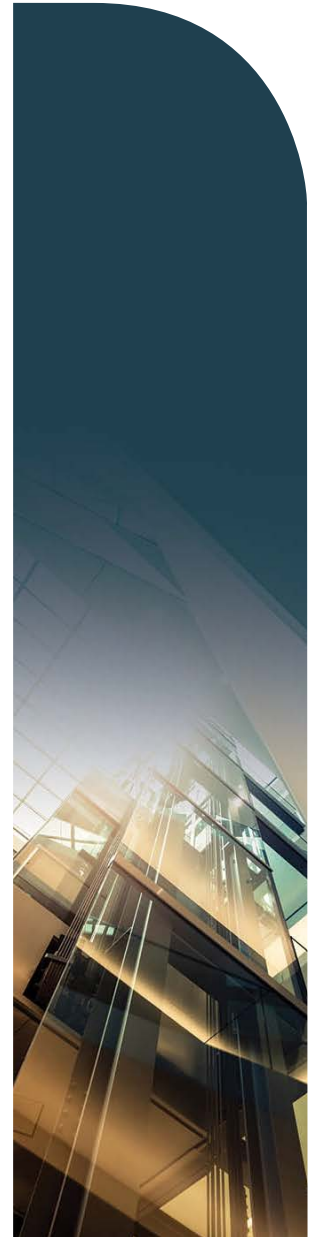
## How the Consent to Sublease Works (continued)

- Subtenant should require estoppel language to confirm Master Lease terms and no defaults
- Is Lender approval of the Sublease required under any SNDA or Master Landlord Loan Documents?

## Factors for Master Landlord's Consent

- Typically a reasonable approval standard
- Very important to review the specific criteria contained in the Master Lease
- Creditworthiness of Subtenant is often an issue

## Consider Whether Corporate Transactions Such As Sales of Stock, Issuance of Debt or Equity, or Sales of Assets Trigger Owner Consent Requirement



# Subtenant Risks in the Sublease Relationship

## Termination of Master Lease Terminates Sublease

- Consider whether to request a Recognition Agreement if Master Lease terminates
- Unless Master Landlord agrees or elects to require attornment, Subtenant must vacate if Master Lease terminates

## Tenant Should Agree That It Will Not Voluntarily Terminate Master Lease

## Subtenant May Want Notice and Opportunity to Cure Master Lease Defaults



# Subtenant Risks in the Sublease Relationship (Continued)

**Tenant Should Enforce Rights to Obtain and Enforce an SNDA**

**Should Tenant Be Required to Terminate Rights under the Master Lease That Impact Subtenant?**

- Expansion
- Renewal
- Contraction / Early Termination

**Pre-Approval of Subtenant Initial Alterations and Right to Make Future Alterations**

**Tenant Rejection of Master Lease and/or Sublease in Bankruptcy**



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# Additional Considerations in the Sublease Arrangement

**Tenant to Prepare a Redacted Master Lease for Subtenant Review**

**Determine Allocation of Signage Rights between Tenant and Subtenant**

- Consider lobby, desk, exterior, interior, elevator, etc.
- Consider Master Landlord consent requirement and RSF thresholds

**Determine Allocation of Parking Rights between Tenant and Subtenant**

**Determine Allocation of Lobby Rights and Common Areas between Tenant and Subtenant**



# Additional Considerations in the Sublease Arrangement (Continued)

**Separation of Security, IT, and Utilities for Subleased Premises and Retained Premises**

**Further Transfers by Subtenant**

**Consider Whether Subtenant Holdover or Failure to Restore Will Result in Holdover of Entire Premises**

- Potentially a huge issue for Tenant if small Sublease causes holdover of Master Lease
- Timing to restore





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# Presenters



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