When you can say 'yes'

In the second of a two-part article, when is it appropriate to agree to changes in payments from commercial tenants?

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The economic downturn in the late noughties caught a lot of people by surprise, particularly those whose funding relied on Icelandic banks, and this was a significant problem for retailers, many of whom fell into this category.

The insolvency of the lenders meant that affected companies found their overdraft facilities had evaporated overnight. As a rental quarter day approached, they simply did not have access to enough money to pay the landlords in full – or at all in some cases.

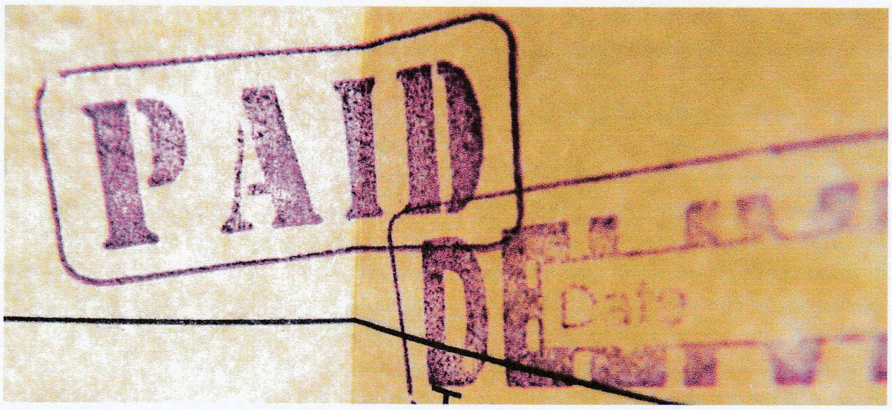
Notwithstanding my cynical comments last month on about the use of landlords as a source of free working capital by badly run tenants ("The bank of first refusal", p14-15) in exceptional circumstances like this, it is only sensible for landlords to engage and assist tenants in getting through a critical situation – provided they are not taking unnecessary risks themselves.

Possible options

In this type of situation, allowing a tenant to pay monthly instead of quarterly will smooth the tenant's outgoings and prevent it from being declared insolvent through no fault of its own.

The secret here is full disclosure by the tenant of all relevant information, including corporate and management accounts, debt structure, and a forecast of how the monthly arrangement will fix the problem.

Remember, the landlord is not legally obliged to do anything at all, and, at the time of the crunch, some of the biggest commercial-property groups had to resort to multi-million pound rights issues



If it does not and there are other variables involved, then, by agreeing to it, the landlord is foregoing two months income it would otherwise have had, without having any guarantee that the tenant will not fall into an insolvency regime anyway.

Remember, the landlord is not legally obliged to do anything at all, and, at the time of the crunch, some of the biggest commercial-property groups had to resort to multi-million pound rights issues in order to avoid their own banking-covenant breaches.

In certain exceptional circumstances that everybody faced, a few monthly rent concessions – and there were not actually that many – were a small price to pay to keep otherwise well run tenants afloat.

Of course, the inevitable happened and the standard monthly rent application letters citing 'economic conditions' began to turn up on landlords' doorsteps up and down the country, without any financial information to back up the requests.

Some of these were actually sent without the tenants' knowledge by their property agents as a way of earning extra commission. My answer to all these was the standard request for financial disclosure in order to prove manageable distress, and, funnily enough, most of them fell away at that point.

Unfair prejudice

There will be circumstances where a landlord will look favourably on a tenant's request to modify the terms of the lease – and the payment frequency – in exchange for something the landlord wants or needs.

However, as with any agreed variation to lease terms, it is important to remember that the tenant in question is often only one of many, and any off-lease deal you do with one operator will inevitably be viewed as favouritism by the others. So the effect on the mood of the entire tenant portfolio needs to be taken into account.

Where I have seen payment concessions granted to one tenant in the past, I have soon heard grumblings from the surrounding operators along the lines of 'why is the landlord helping this badly run tenant to compete on prejudicial terms with well-run operators like us?' They are absolutely right to ask, so have your answers ready! CCR