

Negotiating a Contraction Option? Here Are Some Details to Consider

A contraction option is a fixed right in your lease to reduce the size of your premises at some future date, but prior to your lease expiration date. You can use it to downsize an office space prior to the lease's scheduled expiration date.

As you might expect, landlords (and their lenders) vigorously resist giving tenants this right. However, a creditworthy tenant in the market for a sizeable amount of space may be able to extract this concession if tenant's representative addresses the issue early in the negotiation process.

CHECKLIST FOR NEGOTIATING A CONTRACTION OPTION

- ❖ Do you have the right to contract the Premises throughout a defined period of time, or is it a one-time right?
- ❖ Is the contraction date variable? Or is it fixed?
- ❖ Size of contraction space variable within a specified size range? Or is it fixed?
- ❖ How much prior notice, in advance of the effective date, are you required to provide the landlord?
- ❖ Are you permitted to identify the particular space when exercising the option? Or is the contraction space specified at the time the lease is signed?
- ❖ If you may identify the contraction space when exercising the option, is the landlord's approval limited to concerns of access, code compliance, and marketable configuration? Or are you limited to giving up a full floor or floors, not a partial floor?
- ❖ Is the contraction fee limited to Landlord's unamortized costs for said space? Is the landlord required to substantiate (e.g., provide copies of paid invoices) for said costs?
- ❖ Is there an additional agreed-upon penalty sum added to the fee? If you have an ongoing right to downsize, does this additional fee decrease as the remaining lease term shortens?
- ❖ Is the method of amortization and the discount rate, if any, clearly stated? Is the amortization period specified?
- ❖ If the contraction space is a partial floor, are demising costs the landlord's responsibility? Or does the contraction fee also include an estimate of the landlord's actual, reasonable, and necessary demising costs?
- ❖ Is the contraction fee due upon exercise of option or at effective date of contraction? If due upon exercise of option, may it be paid in installments? Do you receive a pro rata credit for any prepaid utilities or taxes against the final fee installment?
- ❖ Is there a pro rata reduction of the amount of any security deposit or letter of credit build into the contraction right?
- ❖ Are you released from any claims and liabilities relating to the contraction space after the contraction date?

- ❖ Are expansion rights, signage rights, exclusivity rights, or other tenant rights impacted by you exercise of the Contraction Option?
- ❖ May an assignee of subtenant exercise the Contraction Option or is it personal to you?

*Need help negotiating your contract when
your lease is due to expire?
Call Mike for a consultation.*

Mike Maroon, SIOR is the Managing Partner of The Acclaim Group, a leading real estate adviser to corporations locally, nationally and globally.