

## Gotcha Renewal Commissions

By Joshua Stein



When a lease gives a tenant a renewal option, the tenant's broker often negotiates the right to receive another commission if and when the tenant exercises the option. It will usually equal whatever incremental commission the broker would have earned if the original lease term had included the option term at the ultimate option pricing.

It all sounds very fair. If the tenant exercises the option, then the landlord gets the benefit of the additional rent and should pay the broker for delivering the tenant.

As a practical matter, though, tenants rarely exercise renewal options in accordance with their terms. They negotiate something else – a longer or shorter term, more space or less space, other changes in the lease. So renewal commission agreements often award the broker a commission if, for example, the tenant “exercises its renewal option, whether or not in accordance with its terms.” The language is sloppy. It tries to capture the case where landlord and tenant negotiate some “other” deal instead of the tenant literally exercising the option. It's what usually happens. Again, the landlord gets the benefit of the tenant's rent, and ought to pay the broker for the value delivered. Whether the tenant technically exercised the option in accordance with its terms is beside the point.

As a result of all of this, leasing brokers often expect additional commissions on renewal options many years after the original lease was signed. In those many years, the landlord may have replaced its entire leasing department. Many other tenants will have come and gone. The landlord will have fired its overpriced lawyers and hired cheaper new ones, perhaps several times. Files will have been lost. Memories will fade. And the tenant may no longer have any relationship with the broker that negotiated the original lease. When the time comes to negotiate a renewal, the tenant may have hired another broker, who will legitimately expect compensation from the landlord if the tenant renews. No one except the tenant's original broker will remember the tenant's original broker and that broker's expectation of a commission if the tenant renews.

Of course, in a perfect world the landlord will maintain great records, sufficient to defeat the entropy that will otherwise reign. Whenever a landlord signs a commission agreement providing for renewal commissions, the landlord will make a note of it and never forget. The landlord will never face any risk of surprises or double commissions. In the real world, though, landlords aren't always so perfect.

As a result, if the tenant renews its lease and the original broker finds out about it, the landlord may face a surprise in the form of

a “left field” claim from the original broker, long since forgotten, for an additional commission.

To protect themselves, landlords can take the position that once they pay the broker the original commission, that's the end of that. Anything else is a pitfall and a lawsuit or arbitration waiting to happen. And the original commission adequately compensated the broker. That should suffice. If the broker wants more, they can take it up with their client, the tenant.

Brokers won't always agree with the landlord's position. Sometimes the parties negotiate a middle ground. For example, the broker might get a renewal commission only if the broker still acts for the tenant, or stays involved in the negotiations. After all, the tenant will still need a broker. It's up to the broker to maintain that relationship and keep a finger in the pie. Otherwise, the renewal commission is just a windfall for doing no incremental work. That all makes sense, perhaps.

As another approach, a landlord might insist that if a broker wants to recover a renewal commission, the broker bears the burden of reminding the landlord of the broker's existence – some reasonable time but not too long before the option exercise period begins.

For example, if the broker wants to claim a commission, the broker has to reach out to the landlord two years before lease expiration and offer to help with renewal negotiations at no charge beyond the renewal commission. This way, at least, the broker might help the landlord remember not to work with any other broker if the tenant wants to discuss renewal.

When that conversation starts, as another protective measure a landlord should quickly try to determine whether there might be some broker who worked on the original lease many years ago and is now waiting in the wings to claim another commission. The landlord's ability to do that will, of course, depend on whether the landlord maintained good records.

Going forward, at least, a landlord ought to try to prevent future surprises by rejecting the idea of renewal commissions entirely, or at least limiting them in ways suggested here.

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