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LEASE ADMINISTRATION

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PROPERTY MANAGEMENT

REAL ESTATE BROKERAGE

## PERCENTAGE RENT: A MISSED OPPORTUNITY COMPOUNDED

### SCENARIO

Consider the case of a large national developer who several years ago negotiated a long term lease with an up and coming restaurant who was performing at a high rate of gross sales per square foot. The lease was well negotiated and contained an ironclad percentage rent clause. Unfortunately, the lease administrator failed to collect the gross sales statements and the percentage rent was left unbilled. By the time the problem was discovered the percentage rent due had ballooned to over \$60,000.00. Once the oversight had been discovered the percentage rent was billed. Upon receipt, the tenant immediately asked for a deduction in exchange for a large amount upfront. Obviously this put the landlord in a bind; neither accepting less, amortizing payments, or losing the tenant to bankruptcy were ideal.

### COMMENTARY

A great amount of effort is put into the negotiation of retail lease agreements. Unfortunately, the varied nature of the commercial lease coupled with lengthy terms often results in complications when it comes to the collection of rent. These issues tend to compound, eventually turning relatively small problems into massive liabilities.

Anyone familiar with large scale lease administration will not doubt understand the agony brought on by the realization that just due rent was not billed. An error with respect to the collection of rent only gets worse when viewed from the perspective of asset valuation. Consider the aforementioned case. The monthly rent left unbilled amounted to less than \$3,000 a month. However, had the property in question been priced to sell, the error would have been monumental. Using a 7% CAP rate the property would be undervalued by more than \$500,000.00. A simple failure in process held the potential to significantly injure the performance of a sound investment. The question then becomes, what, if anything, can be done?

Paramount to the avoidance of missed opportunities is the recognition of the uniqueness inherent in commercial lease agreements. Humans are conditioned to organize and process information in blocks; applying this concept to leases removes their uniqueness and leaves one susceptible to missed opportunities. Not to mention, the length of commercial leases means that over the life of a landlord-tenant relationship there will be a number of individuals in whom the responsibility lies for the timely collection of rent. Sound processes and procedures are a great first step.

The second issue faced by landlords is related to the implementation of software. While there are a myriad of good accounting platforms built for commercial real estate market, the fact remains that the uniqueness of legal language renders them unsuitable for the administration of leases. It's not a coincidence that 40% of landlords report using excel to administer leases independent of their accounting platform.

The last major hurdle is related to the time it takes to administer leases. If it can be reasonably assumed that an efficient lease administrator can handle 500 leases at a time then it's not hard to see why landlords are by law always inefficiently staffed. A company with 400 leases and one administrator is spending too much money per lease. Conversely, a company with 600 leases and one lease administrator is not devoting enough time to each lease. Both scenarios leave a landlord open to loss.

At Grant & Lewis we believe that our unique approach to lease administration provides landlords with a better way of doing business. Our proprietary software was built solely from the perspective of the lease administrator and designed with variability in mind, our lease administrators are expertly trained, and our services are priced so as to be instantly scalable. Owning and investing in commercial property can be highly rewarding; don't let the pain associated with administering leases prevent the enjoyment of successful investment. If you find the aforementioned case study at all familiar give us a call for a free consultation.