

# COMMERCIAL LEASING in HAWAII AND TOP 10 SERVICE CONTRACT ISSUES

- A Combined Presentation by Duane R. Fisher, Esq.©
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# Commercial Leasing in Hawaii

A Real Estate Lawyer's Summary for Businesses

Focus today is on business leases, not residential leases, not ground leases

- For example: office leases, retail leases
- Generally focusing on issues that should be considered from the tenant's perspective

## A few basic concepts:

- Leases both convey a real estate interest AND are contracts.
- Leases must be in writing, unless they are for a term of less than one year (HRS §666-4). But even for leases of less than one year, creating a written document is almost always a good idea!
- Tenant's interest cannot be greater than the landlord's interest. (The Landlord cannot convey what she does not have).
- No "Commercial" landlord-tenant code in Hawaii as such. Borrow from residential landlord-tenant code.

# Title Reports and Title Insurance

- What is a title report?
- When are they useful?
  - Confirm ownership of the property
  - Determine whether the landlord's interest is subject to any matters that could impact tenant's operations.
- What is an SNDA?
- When should a tenant seek an SNDA?
- Leasehold Title Insurance

# Typical Commercial Lease Structure

- No universal standard form in Hawaii – Each landlord typically creates their own form.
- Typical structure is to divide the lease into two parts:
  - Part 1 = Specific Provisions. These are terms that vary from deal to deal.
  - Part 2 = General Provisions. These are terms that usually do not vary from deal to deal.
- Typical 2-part structure applies for both office and retail leases.

Focus today on select Specific Provisions and  
General Provisions

# Specific Provisions - Parties

- Parties – Proper identification of landlord and tenant.
- Will a single purpose entity be used by tenant?
- Consistency between preamble and signature blocks.



## Specific Provisions – The “Premises”

- Proper identification of the premises being leased.
- Heads up re subdivision issues
- Use of exhibits

# Specific Provisions – Use of Premises

- What uses by tenant are permitted?
- What uses (if any) by tenant are prohibited?
- Retail Leases: Does tenant have any “exclusive” rights?
- What uses of other spaces by landlord are permitted / prohibited?
- Trade name?
- Continuous operation covenant?
- Hours of operation?
- Parking needs?

# Specific Provisions - Term

- Term = duration of the lease.
- If five years or longer, conveyance tax is payable.
- “Commencement Date” timing vis a vis construction of improvements, ability to take occupancy and timing of rent commencement.
- Beware of Possible Trap: Rent due before operations commence!
- Option to extend term?

# Specific Provisions – Rent and Security Deposit

- Base rent. Typically payable in advance. How described? Per square foot per month? (Note: mainland jurisdictions often describe in per square foot per year).
- Percentage rent. Payable in arrears. Landlord right to review receipts, etc.
- “Additional Rent” (e.g., taxes, common area maintenance, etc.).
- CAM traps: Landlord attempts to pass along capital costs to tenants.
- Rent re-openers / arbitration.
- Security Deposit. No statutory limit in commercial leases, but one month’s base rent is typical.

# Select Issues: Office versus Retail Lease

- Rent:
  - Both Office and Retail Leases will require payment of Base Rent.
  - Office Leases normally WILL NOT contain any Percentage Rent requirement.
  - Retail Leases typically WILL contain Percentage Rent provisions.
- Select Percentage Rent Issues:
  - Definition of Gross Revenues. What's included and what's not included?
  - Cash register receipts
  - Tenant records
  - Landlord's audit rights
  - True Ups

# Specific Provisions – Landlord and Tenant Improvements

- Clarity on Scope of the improvements to be made.
- Clarity as to who is paying for what.
- Clarity on timing of completion of improvements, and interface with rent obligations.
- Beware of potential timing problems:
  - Landlord's right to approve drawings etc.
  - Time needed to obtain building permits.
  - Landlord reimbursements after all work is complete.

# Specific Provisions - Guarantor

- Basics of a guaranty
  - Intent to have person / entity with financial wherewithal stand behind tenant's obligations.
  - Absolute, unconditional obligation.
- Alternatives to / Softening of a guaranty
  - Limit duration (e.g., if pay rent currently for 1 year, guaranty terminates)
  - Limit amount (e.g., cap amount for which guarantor is liable at \$\_\_\_\_\_)
  - Larger security deposit in lieu of guaranty

# Specific Provisions - Signage

- Will Tenant use a sign for the premises?
- Landlord approval rights?
- Local zoning ordinances (e.g., ROH §21-7.1) may apply and restrict size and other aspects.



# Select General Provisions

- Default / time to cure
  - Is failure to pay rent when due automatically a default or will tenant get notice and a period of time within which to pay before a default is declared?
  - Non-monetary defaults . . . “commence to cure and diligently pursue . . .”
- Taxes
  - Conveyance
  - Real Property
  - General Excise
- Landlord’s right to relocate the tenant
  - Strategies for handling
- CAM charges
- Services provided by Landlord
- Insurance requirements: Check with your insurance broker.

## Select General Provisions (continued)

- Condemnation
- Damage / Destruction of premises
- Assignability
- Tenant Financing / Right to Mortgage / Mortgagee protection
- AS IS condition of Premises; ADA compliance; Compliance with laws
- Estoppel Certificates
- Notice requirements: Follow them!

# LEASING Q & A

# Top 10 Service Contract Issues

- Focus on BUSINESS contracts. Not consumer contracts.

# What is a Business Service Contract?

- A Business Service Contract is an agreement by which a service provider (vendor) agrees to provide certain specified services to a business in exchange for payment.

# Quick Disclaimer

- This list is NOT exhaustive. There are other issues.
- However, this list contains the presenter's view of 10 of the more significant and most commonly faced issues when negotiating a business service contract.

# Issue #1 – Scope of Services to be Provided

- Clarity on WHAT services the vendor is providing.
- Service provider seeks to be vague and have wiggle room.
- Business owner seeks to be specific about exactly what the service provider will be doing.
- If you (as the business owner) cannot tell exactly what services are being provided when you read the contract, then add language to be specific about what services are being provided.

## Issue #2 – Performance Standards

- Clarity on WHEN the services are to be performed.
- Clarity on HOW the services are to be performed and what is expected. Set clear criteria for measuring.
- Clarity on the CONSEQUENCES of the vendor's failure to perform (Liquidated damages per diem? Price discount? Right to terminate?)



## Issue #3 - Pricing

- Clarity on HOW MUCH the business is paying the vendor for the services and WHEN payments are due.
- “Basic Services” versus “Additional Services” – Clarity.
- Note: NEVER prepay entire amount for the services. ALWAYS keep some money back until all services are completed to business’ satisfaction.

## Issue #4 – Cure Periods

- Beware of giving the vendor lengthy or open-ended cure periods.
- Better for the business to have a reasonably short, definite period within which vendor must perform.

## Issue #5 – Termination Rights

- Businesses generally prefer the agreement to be terminable, without cause, by the business on some reasonable period of notice to the vendor. This is not always acceptable to the vendor – especially if they have significant start-up costs.
- The agreement should always be terminable on short notice after default (and expiration of cure period).

## Issue #6 – Limitation of Liability

- These provisions usually impact a business in two ways: (A) Most vendors try to completely eliminate the client's right to consequential damages like lost profits, and only allow direct, out of pocket damages to be recovered. (B) Most vendors try to impose an absolute cap on the level of damages the client can recover. The cap is often tied to the level of fees paid by the client over some period of time (*e.g.*, 3, 6, or 12 months) preceding the event giving rise to the claim. Client should consider whether the limitations of liability should be MUTUAL, rather than one-sided in favor of the vendor. Each Client needs to make a business decision about the acceptable level of limitation on a case by case basis

## Issue #7 – Assignability

- Especially important in a business sale if the contract is a key contract.
- The client generally want the right to assign its contracts to any entity that acquires the business or assets of the client, whether by asset sale, stock sale, merger or otherwise, WITHOUT needing the consent of the vendor.
- The client generally does not want the vendor to assign the contract to another vendor without Client's prior consent.

## Issue #8 – Force Majeure

- In critical contracts, be mindful of Force Majeure (acts of God, war, terrorist attacks, labor strikes, etc.) provisions where the client could end up stuck with the contract (without a right of termination) for some open-ended or lengthy period of time.
- Ask yourself how being stuck in that position would impact the business or its customers.

## Issue #9 – Governing Law

- Hawaii businesses should insist on contract being governed by Hawaii law.

## Issue #10 – Forum Selection / Venue

- Where will disputes be resolved?
- Hawaii usually first choice.
- Avoid agreeing to resolve disputes exclusively in jurisdictions outside of Hawaii.
- Possible Compromise Provision: “Other Party’s Home Court”



# Q&A on Service Contracts

# THANK YOU!

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