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LEASE CONCESSIONS: TAX AND ACCOUNTING CONSIDERATIONS

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Due to the state of the national office market (Pollina Corporate Report, 4th Quarter, 1989), developers of new and existing office buildings have become very aggressive in their pursuit of new tenants and in their efforts to maintain existing tenants. In addition to the standard lease concessions such as rent abatement and above standard construction allowances, incentives in the form of equity participation and payments to a tenant's current landlord to terminate its existing lease have become common. This article will deal with the impact of various concessions on a tenant's financial statements and tax returns.

Landlords typically have a pool of concession dollars available for tenants and some flexibility as to how those dollars can be offered. Decisions regarding which concession is most appropriate for a given situation will depend in part on what the tenant needs in up-front cash to relocate and/or terminate an existing lease, how much administrative complexity a landlord and tenant will accept in accounting for the concessions, and what effect the concessions will have on a tenant's income statement and tax return. The tax and accounting treatment of lease concessions vary based on the type of lease concession. Described below are several of the most common lease concessions and the tenant's required tax and accounting treatment. For tax and accounting purposes, keep in mind that a tenant acting as a sublessor is required to account for lease concessions given to each sublessee in the same manner as a landlord.



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Keith Nakamoto has been with Coopers & Lybrand for over 16 years. During the last eight years, he has focused entirely on real estate, specializing in tax and financial planning for his firm's real estate clients.

Mr. Nakamoto is recognized for his ability to structure transactions and develop computer models to test the impact of variables on these structures. He is also known for his ability to develop tax compliance systems and to monitor and modify these systems to adapt to changing tax environments. Mr. Nakamoto is a member of his firm's National Tax Oriented Investment Group.



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Arnold Bargielski serves as head of Coopers & Lybrand Construction and Real Estate Development team. His 18 years experience with the firm includes consulting on various aspects of real estate related activities such as the structuring, valuation and financing of transactions. He has been involved in the registration of over 25 MLPs, REITs or limited partnerships with the SEC for major real estate companies.

Mr. Bargielski is active in formulating his firm's analysis and position on real estate industry technical issues, including developing and authoring the firm's response to the SEC on Staff Accounting Bulletin, No. 71.