

# RETAIL PERSPECTIVES

■ FALL 2012

RETAIL PERSPECTIVES

## DRAFTING AND NEGOTIATING A LANDLORD'S RIGHT TO RELOCATE A RETAIL TENANT

### Introduction

From a landlord's perspective, a retail lease provision granting the landlord a right to relocate a tenant can be essential to protect the landlord's ability to control its shopping or mixed-use center. Tenants, however, are generally wary of these provisions. The landlord may need to relocate the tenant for a variety of reasons, including a proposed expansion or renovation of the center or the accommodation of another tenant that wishes to lease a large amount of space. It is particularly important to the landlord that a long-term lease, taking any renewal rights into consideration, should include a relocation provision, because the landlord's right to relocate a tenant may affect the landlord's ability to expand, renovate, or transfer the center at a later date.

At first, a tenant may resist signing a lease that includes a relocation provision. The tenant has chosen to lease a particular space, and the landlord and tenant have agreed to the economic terms of their transaction based on the tenant's lease of that space. Relocation may result in the disruption of the tenant's business and the loss of customers. The new location may be more difficult for the tenant's existing or potential customers to find than the original location because it is farther away or less visible from parking areas, access roads, or pedestrian bridges. In addition, the tenant may not want to relocate because the new premises are closer to businesses the tenant finds undesirable or farther away from businesses that the tenant relied on to draw foot traffic to the tenant's store.

Skillful drafting and negotiating of the relocation provision, however, can protect a landlord's right to maintain control over its center while addressing the tenant's concerns. The parties may save money and effort, and can avoid uncertainty. Without an express relocation right under the lease, the landlord may find it necessary to either pay the tenant to relocate or seek to have governmental authorities condemn the tenant's premises. Landlords and tenants may reach a number of different compromises when negotiating a relocation provision, but the final version will depend on the relative bargaining power of the parties.

### Drafting a Relocation Provision

#### *Initial Considerations*

The initial draft of a relocation provision for a landlord's retail lease should expressly set forth the terms of the relocation right, provide that the lease will be amended in the event of a relocation, and address the issue of how a relocation would affect or be affected by other rights granted to the tenant under the lease.

#### *Setting Forth the Right To Relocate the Tenant*

The relocation provision should indicate both the landlord's right to relocate the tenant and the circumstances in which the landlord may exercise that right. Specifying that the landlord can relocate the tenant at any time during the lease term (and any extension of the lease term) may, depending on how the commencement date of the lease term is defined, preclude the landlord from relocating the

## NEGOTIATING CAM CAPS: BALANCING THE INTERESTS OF LANDLORDS AND TENANTS

In today's economic environment, and in the not too distant past, developers and retailers have both experienced the volatility of an unpredictable economy in recession and retail business negatively affected by unforeseen and costly factors, such as increasing utility and security costs. Such developments have reinforced the importance to developers of recapturing as much of their project operating costs as possible, in an effort to maximize the bottom line. By the same token, retailers have found themselves in situations where consumer spending has slowed or dropped, requiring tenants to control revenues in other ways, including by minimizing extraordinary operating costs (including costs under their leases).

One way in which tenants have been attempting to minimize costs and/or potentially great cost exposure, is by negotiating limits (or "caps") on common area expense obligations under their leases. Caps on common area expenses may take any number of forms. Depending on the situation and the circumstances of the particular transaction, a tenant may be successful in negotiating a cap on CAM by negotiating a "gross" lease (meaning the rent and all pass through expenses are consolidated into one fixed base rent figure), a "base year" deal (whereby the tenant will only be responsible for its share of increases in operating and similar expenses over the amounts for such expenses in a base year) or any other number of hybrid scenarios.

However, and probably most popular, is a cap on the amount that the tenant's share of common area expenses may increase from any one year to the next. Usually this type of cap limits the tenant's share of common area expenses from increasing by more than a negotiated percentage -- usually 3% to 6% -- from the tenant's share of such costs in the previous year. And, sometimes, tenants are able to negotiate specific dollar limits on their exposure for common area expenses for the first year of a lease, followed by a percentage cap on common area expenses for future years.

No matter the type of cap negotiated, caps on common area expenses shift the risk of unforeseen increases in operating costs from the tenant to the landlord. If common area expenses increase from any one year to the next at a rate in excess of the fixed percentage increase set forth in a tenant's CAM cap provision, the excess will not be the tenant's responsibility. Instead, either the landlord will be responsible for such costs, or the excesses will be passed through to other tenants of the particular project who have leases which permit the landlord to pass through the unrecovered costs of other tenants (*i.e.*, leases which require the tenant to subsidize other tenants).

In an economic climate where more and more tenants are requesting and obtaining CAM caps, it is important for the landlord to understand its risks and minimize the items to which its CAM cap provisions will apply. Therefore, it is important when representing landlords that, when agreeing to caps on expenses, items which are not controllable by the landlord are not subject to the cap. For example, in most situations, taxes, assessments and other governmental impositions, insurance costs (including premiums and deductibles), utility expenses, security expenses and related items, should be excluded from any particular limit on common area expenses. By doing this, both the landlord's and tenant's interests can be protected -- the tenant is protected from snowballing extraordinary costs incurred by a landlord that does not competitively price common area services and landlords are protected from increases in costs over which they have very little or no control.

CAM cap provisions are very important and may be very complicated. How a CAM cap provision is negotiated and drafted will definitely affect the economics of a transaction. Leases should be carefully drafted to ensure that the risks of the retailer and developer, as the case may be, are properly protected. ►

## DRAFTING AND NEGOTIATING A LANDLORD'S RIGHT TO RELOCATE A RETAIL TENANT

*continued from page 1*

tenant during the period of time after the lease is executed but before the tenant takes possession of the premises or before a set commencement date. The relocation provision should also provide that the relocation right is a continuing, as opposed to a one-time, right. Finally, the tenant should be required to leave the premises in a condition similar to the condition it was in when the tenant opened for business.

### ***Providing for a Lease Amendment***

The relocation provision should state that, once the landlord has exercised its right to relocate the tenant, the parties will document the relocation by entering into a lease amendment. It should be made clear that the amendment will describe the new premises, including the new square footage and an exhibit depicting the location of the new premises, and will provide that the lease applies to the new premises as though it were the original premises. The amendment should also modify any lease terms that change as a result of relocation, including rent and the tenant's prorata share for purposes of calculating common-area maintenance charges and taxes. Finally, the amendment should reaffirm the continuing liability of any guarantors to the lease.

### ***Describing How Relocation Interacts With Tenant's Other Rights***

If the lease provides the tenant with rights or obligations in connection with other space in the center, the relocation provision should describe the effect of the relocation on these rights or obligations. In particular, the relocation provision should specify whether expansion rights or obligations relating to space adjacent to the original premises will remain, become void, or transfer to space adjacent to the new premises, subject to any rights held by other tenants. Other lease rights that should be addressed are rights to use patio space adjacent to or near the tenant's premises or space on the roof of the building in which its premises are located for satellite installation or other purposes. The relocation provision should also address any exclusive or prohibited use clauses under which certain uses may not be located within a specified distance from the tenant's premises.

### ***Using Specific Language***

Landlords and tenants can avoid disputes at the time of relocation by describing the relocation right as specifically as possible in the lease. A relocation provision may be of little use to a landlord if its terms are vague to the point of being unenforceable. Keep in mind that starting with a provision that gives a landlord overly broad or unreasonable relocation rights may damage the landlord's ability to negotiate successfully with the tenant; however, it is important to draft a provision that does not restrict the landlord's relocation rights so much that the landlord has no room to negotiate.

### ***Finding Room To Agree***

#### ***Getting Beyond a Tenant's Request To Delete the Relocation Provision***

Unless it is impractical to contemplate relocation because the tenant's premises are very large or unique in some other way, a landlord can often preserve its relocation right by limiting the circumstances under which it can relocate the tenant, representing that the new premises will meet specified criteria, and making certain concessions regarding the actual move to the new premises.

### ***Limiting Circumstances of Relocation***

Tenants will want to narrowly define when and under what circumstances a landlord may exercise its relocation right. A landlord may be willing to limit its relocation right to certain situations, such as the renovation of all or a specified portion of the center, the expansion of the center, or the accommodation of another tenant that is taking a large block of space that includes the tenant's premises. In addition, if the landlord plans to demolish the premises after the tenant relocates, the tenant may not be required to leave the premises in a condition similar to the condition it was in on the day the tenant opened for business.

The landlord and tenant may agree to limit the number of times the landlord is allowed to relocate the tenant, *e.g.*, not more than twice during the lease term, or not more than once during any five-year period of the lease term or any extension of the lease term. When negotiating this point, the landlord should keep in mind that it may be necessary to relocate a tenant more than once in the event of a phased renovation of a center.

## DRAFTING AND NEGOTIATING A LANDLORD'S RIGHT TO RELOCATE A RETAIL TENANT

*continued from page 3*

Also, a tenant typically will not want to be relocated during certain times that are important to its business, such as the holiday or back-to-school season. Another timing issue involves the amount of advance notice a landlord must give the tenant before carrying out a relocation.

### ***Approving the New Premises***

Tenants may ask for the right to approve the new location. Granting the tenant such an approval right, however, may lead to a long, protracted dispute, unless the relocation provision limits the time period within which the tenant must approve or disapprove the new premises and provides that if the tenant disapproves the new premises, then either the landlord or the tenant may terminate the lease. The landlord, however, may want to have the right to nullify the tenant's termination of the lease and allow the tenant to stay in the original premises.

Another option is for the landlord to offer the tenant a choice of at least a specified number of new locations to choose from, provided that the landlord will select the new premises if the tenant fails to choose one of the proposed locations within a specified time period.

### ***Agreeing on Other Criteria***

Landlords and tenants may agree that the new premises will meet certain criteria, such as the following:

- *Improvements.* The landlord will construct improvements in the new premises that are substantially similar to, or better than, the improvements in the original premises.
- *Square Footage.* The new premises will have the same square footage as the tenant's original premises or a higher square footage, the same square footage as the tenant's original premises plus or minus an agreed-upon percentage of the square footage of the original premises, or a set square footage minimum and/or maximum.
- *Attributes.* The new premises will have the same or comparable frontage, layout, or view line as the original premises, or must be on the same floor as the original premises if the center has more than one level.
- *Proximity.* The new premises will have a specified proximity to access roads, pedestrian walkways, a certain number of parking spaces, an anchor tenant, or a tenant that uses its premises for a certain business use (whether this means that the tenant will be far from a use the tenant finds undesirable or close to a use the tenant finds desirable).
- *Location in the center.* The new premises will be located in a specific portion of the center described in the lease or set forth on an exhibit to the lease.
- *Rent.* Rent and other charges based on the square footage of the premises (e.g., taxes and common-area maintenance charges) will not increase even if the new premises are larger than the original premises and will decrease if the new premises are smaller than the original premises.

As mentioned above, when drafting and negotiating any of these compromises, it is important to be as precise as possible to avoid disputes when the landlord actually seeks to exercise its relocation right.

### ***Agreeing on Moving Concessions***

A tenant may request that the new premises must be ready for the tenant to operate its business before the tenant is obligated to move from its original premises, or that the tenant will not be obligated to pay rent for any period during which it is unable to remain in the original premises and unable to operate its business in the new location.

Additionally, a landlord may agree to reimburse the tenant for its actual out-of-pocket costs in relocating to the new premises, but will not typically agree to be liable for any other costs or damages, such as lost profits, claimed by the tenant in connection with the relocation. However, if the tenant is relocated before it has taken possession of the original premises, the landlord should not have to pay moving costs.

## DRAFTING AND NEGOTIATING A LANDLORD’S RIGHT TO RELOCATE A RETAIL TENANT

*continued from page 4*

Other concessions a landlord may agree to in connection with relocating the tenant include paying for advertising the new premises to tenant’s customers and posting signs to direct the tenant’s customers from the original premises to the new premises. The time period during which this advertising will occur and the signs will remain in place should be set forth in the relocation provision to avoid future disputes.

### Conclusion

When negotiating any of the issues described above, the landlord needs to take into account several practical considerations that may affect its ability to relocate the tenant. For example, restrictions that make sense in theory may, because of the physical layout of the center, make it impossible for the landlord to exercise its relocation right. A landlord should determine how many other locations in the center meet the criteria agreed to by landlord and tenant to assess the likelihood that the landlord will be able to relocate the tenant. In addition, the exclusive, permitted, and prohibited uses set forth in other leases may also restrict a landlord’s options for relocating a tenant. Also, while there are many factors to consider when drafting and negotiating the relocation provision of a retail lease, the end result will largely depend on the landlord’s bargaining power relative to the tenant. Finally, if the landlord and tenant agree to subjective criteria for the new premises, the relocation provision should designate specific venues for dispute resolution, such as arbitration, so that any disagreement on the suitability of the new premises may be resolved as quickly as possible. ►

The Retail Group of Cox, Castle & Nicholson LLP has extensive experience in acquiring, developing, constructing, leasing, financing and disposing of all types of retail projects, including regional enclosed malls, lifestyle community centers, neighborhood centers, and mixed-use projects. Members of the Retail Group include attorneys who are experts in sales and acquisitions, design, engineering, and construction contracts, reciprocal easement agreements, development and management agreements, and leasing.

## The Retail Group of Cox, Castle & Nicholson LLP

### LOS ANGELES OFFICE

2049 Century Park East, 28<sup>th</sup> Floor  
Los Angeles, California 90067-3284  
P 310.284.2200 F 310.284.2100

GARY GLICK  
SCOTT GROSSFELD  
DAN VILLALPANDO  
MATT SEEBERGER  
CHRIS RIZZA  
AIMEE FRANK

### ORANGE COUNTY OFFICE

19800 MacArthur Blvd., Suite 500  
Irvine, California 92612-2435  
P 949.260.4600 F 949.260.4699

DAVID WENSLEY  
BOB SYKES  
HANS LAUTERBACH  
F. JULIAN FREEMAN

### SAN FRANCISCO OFFICE

555 California Street, 10th Floor  
San Francisco, California 94104  
P 415.262.5100 F 415.262.5199

SCOTT BROOKS  
GREGORY CALIGARI