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Key retail lease provisions to revisit in light of COVID-19.

Dan Villalpando

The outbreak of the COVID-19 pandemic forced many retailers to close their doors to customers beginning in March 2020, just as the overall economy was pushed into unprecedented disarray. Because of these circumstances and questions surrounding the unusual situation where municipalities were ordering stores to close, landlords and tenants looked to the four corners of their leases to determine their rights and obligations. Certain key lease provisions, like force majeure clauses, insurance provisions and operating covenants, warranted careful scrutiny as the parties sought to clarify their contractual responsibilities in light of the impacted retail landscape.

While many of those issues have yet to be resolved and most businesses are not yet running at full steam, it is not too early to analyze key lease provisions for the (hopefully not too distant) future, when new deals start getting done in the context of an uncertain and unstable landscape.

What follows is a brief discussion of a few common lease provisions involving common areas, common area costs and alterations that may need to be revisited to account for COVID-19 issues, and to put landlords in a better position to respond and react to the "new normal" that will exist until a vaccine is developed and widely distributed.

USE OF COMMON AREAS

Landlords should make sure that the control of common area language found in most leases is broad enough for landlords to respond and adapt to pandemics and similar emergencies, such as by installing items to improve health and safety conditions and making other (perhaps currently unforeseeable) changes to the common area to comply with recommendations or requirements of the CDC, WHO, or state or local authorities. As a result of physical distancing and store-capacity requirements, tenants may need the right to use portions of the common area (like sidewalks) for customers to form lines outside the stores. In addition, restaurant users may need the right to use part of the common area for seating for their customers if requirements do not allow them to provide tables inside for customers to eat. Landlords should do their best to work with tenants, where appropriate, to allow for the use of the common area for queuing and outdoor seating, as the ability to use such areas could be vital to the success of the applicable tenant. Nevertheless, a landlord can condition such use upon the tenant fulfilling certain conditions, such as giving the landlord prior written notice of such intent and the expected duration, peak times and specific area the tenant wants to use. Additionally, landlords may want to specifically require that the tenant cleans up the area used for queuing and/or outdoor seating on a daily basis.

COMMON AREA COST CAPS

In leases where a landlord provides a tenant with a cap on increases in common area costs, such cap does not typically apply to "uncontrollable" costs. Following COVID-19, landlords should consider expanding the list of "uncontrollable" costs. For example, costs associated with a pandemic and the related health or safety measures the landlord takes (i.e., installation of hand sanitizing stations, upgrades to automatic doors, use of more personnel to administer cleaning and to make sure guests comply with social distancing requirements, etc.) should be deemed "uncontrollable" and not be subject to any cap.

In addition, if it turns out that the "base year" for setting the "floor" for common area costs occurs during a year when the common areas are used less because of a pandemic or related outbreak, the landlord should consider including a "gross up" concept to bring the "floor" up to a number that is more reflective of what common area costs would have been but for the pandemic. Another alternative would be to modify the "cumulative" vs. "non-cumulative" nature of the cap for any period during which common area costs are artificially low. Leases with "cumulative" caps allow the landlord to apply any "unused" portion of the cap from prior years when applying the cap for the year in question.

ALTERATIONS

While some leases provide that any alterations made in the premises are the tenant's responsibility, others split the responsibility between the parties based on the nature of the alteration, whether it is required by law and whether it applies just to the tenant's space or to retail spaces in general. In light of the general uncertainty following COVID-19, landlords should make sure that their leases require tenants to make (at the tenants' expense) any and all alterations required by law, including those borne out of force majeure events. For example, from a landlord's perspective, the cost of any barriers within the premises required to force customers to "social distance" or to further separate customers from employees should be the responsibility of the tenant. If such barriers are structural in nature, a landlord will also want approval rights over the location of, and materials used for, such barriers. **SCB**

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