

# WESTERN REAL ESTATE BUSINESS®

Connecting Real Estate in the West

## CONSTRUCTING A BETTER TOMORROW

There are a number of best practices developed within the construction industry over the past few years that have made the job easier, safer, less costly and faster to complete.



Graycor joined a collaborative design-build team early to map out a precise schedule and budget for Camelback Collective, a mixed-use office and hotel project in Phoenix.

### BUILDING SOLUTIONS

By Todd Ostransky, General Manager, Southwest Division, Graycor Construction Company

With commercial construction activity up by double digits in 2016 and projected to increase another 5 percent in 2017, the industry continues to keep a keen eye on labor shortages and construction costs. This rings even more true in the face of today's increasingly stringent financing requirements — a critical project element that can push construction schedules out by months. In the process, this can create challenges with accurate pro forma data, true labor schedules and pricing.

The balance between schedule shifts and a backlog of work has proven particularly challenging for the entire industry, and presumably shows no sign of relief. For optimal success, teams must diligently focus on cross-functional communication, design-build principles and early strategic planning to protect from the pitfalls of 2017's momentum. Focusing on this early planning gives clients two of the greatest advantages available in our current building climate: a forum for unearthing issues proactively and time to plan for solutions.

In cases where design-build isn't possible, teams can still capture the

see **CONSTRUCTION**, page 27



Denver's newest skyscraper is Hines' 40-story tower at 1144 Fifteenth Street.

## WESTERN SKYLINES OUTPERFORM

Many national skyline markets are at an inflection point, but many markets throughout the West still have room to run, particularly in secondary markets.

By Patricia Raicht

The Western United States is home to 14 of the 50 office skyline markets tracked by JLL. Although West Coast markets show up at the highest and the lowest end of the vacancy spectrum, the region boasts more low vacancy skyline markets than any other region, with six of 14 markets enjoying single-digit rates. Average asking rents trend higher in the West with 12 of the region's 14 markets among the top 25 rental rate markets in the United States. All but two of the Western skyline markets experienced year-over-year rental rate growth.

Some Western skylines reflect the trends of the U.S. skylines overall, but a few are bucking those trends. Many skyline markets are at an inflection

point with slowing rent growth and vacancies inching up as deliveries hit the market. This is true for various primary Western markets, but many of the secondary markets still have room to run with new development or significant redevelopment activity entering the pipeline and solid rental rate growth. Skyline properties across the U.S. have been slow to capture tech tenants, but redevelopment activity and new tech-friendly buildings are increasingly bringing tech users to skyline buildings. Sales of skyline buildings in the West have been brisk, however many have already traded this cycle and volumes will be muted for primary markets while secondary markets could still see high-water mark pricing in the next year.

see **SKYLINES**, page 29

### INSIDE THIS ISSUE



Rising Above The Multifamily Competition

page 25

Phoenix  
Market Highlight

page 16

Colorado  
Market Highlight

page 20

Let's See What's Happening  
with CMBS

page 22

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# NEGOTIATING ASSIGNMENT, SUBLETTING PROVISIONS IN RETAIL LEASES

It's oftentimes better to deal with the tenant you know than a tenant you don't know when it comes to subletting space in shopping centers.

By Scott Timpe



Timpe

**W**hile the golden rule of treating others as you wish to be treated arguably applies to landlord-tenant relationship, there is another lesser-known golden rule that also applies: the one with the

gold gets to make the rules. In many retail leasing situations, the landlord is the one typically making the rules. One common rule made by landlords with the power to dictate lease terms is that a tenant may not assign its interest in its lease or sublet its premises without the consent of the landlord. However, certain tenants have the so-called "gold" — the financial strength and negotiating leverage — to demand exceptions to this rule. This may include the right to assign

their lease or sublet their premises without landlord consent. In negotiating assignment and subleasing clauses with tenants holding some of the gold, landlords must exercise great care to avoid being stuck with assignees or subtenants that do not fit the merchandising of their shopping center or are less creditworthy than the original tenant.

In particular, landlords should consider the following:

## Seek To Impose Control Over Creditworthiness

More often than not, a landlord's first and foremost concern is the ability of a tenant to pay rent, in full, on a timely basis. It should come as no surprise that once a landlord determines a tenant is acceptable from a credit standpoint, the landlord typically does not want such tenant to assign its lease or sublease its premises to another tenant without having the

right to approve the proposed transferee. In instances where a tenant has enough leverage to reject an assignment and subletting provision that gives the landlord sole and absolute discretion, there are many other compromises a landlord can try to reach to maintain a modicum of control over the financial strength of a transferee. For example, a landlord can negotiate requirements that a prospective assignee or subtenant must meet, such as a minimum net worth requirement, a minimum gross sales requirement or a minimum number of stores requirement.

## Demand the Right to Recapture the Premises

If a tenant seeks to assign its lease or sublet its premises, one way a landlord may protect itself is to exercise a right to recapture the premises. A recapture right allows the landlord to essentially block the assignment or subletting by terminating the lease and retaining possession of the premises. Following termination, the landlord can elect to lease the premises to whomever it chooses so as to retain control over its real estate.

## Keep the Original Tenant on the Hook

Landlords should strongly oppose any assignment provision that relieves the original tenant of its obligations under the lease upon an assignment. Having a tenant with a truly vested interest in the ability of an assignee to meet its obligations under the lease is very helpful to ensure that a lease is not assigned to an assignee with weak credit. If a tenant knows it is still on the hook, it will have a strong incentive to scrutinize the ability of a potential assignee to meet the financial and other obligations under the lease, thereby mitigating the landlord's exposure to default risk. Additionally, in the event the assignee does ultimately default, if the original tenant's liability has been preserved, then the landlord's chances of recovery are improved.

## Limit Use Rights

Landlords must also be mindful of the rights of an assignee or subtenant to use the subject premises. Particularly in the case of tenants who have the leverage to negotiate broad use clauses in their leases, it is crucial that a landlord negotiate to limit the acceptable uses of a subsequent

assignee or subtenant. A landlord should always seek to protect its right to control the mix of tenants in its shopping center, and the permitted uses of those tenants. Further, the impact of exclusives and use restrictions negotiated by other tenants at the center must be considered in conjunction with a potential change in use that may occur upon assignment or subletting.

## Make Other Rights Personal to Tenant

It is common for landlords to offer highly sought-after tenants extra perks, such as expansion rights, options to extend and rights of first refusal/rights of first offer, to entice them to take space at their shopping center. In doing so, landlords should also consider the impact of an assignment or sublease on these rights, and whether any such rights should terminate upon assignment or sublease.

## Seek to Share in Excess Rent

In instances where a tenant assigns its lease or subleases its premises, it may be paid an amount that exceeds the amount the tenant is obligated to pay the landlord under the lease. If the assignment or sublease had not been entered into, then in theory, those same financial accommodations (i.e. higher monthly rent payments) would have been available to the landlord if it had leased directly to the assignee or subtenant. Accordingly, a landlord should seek the right to share in this excess financial consideration along with the tenant, or, if it has the leverage, to obtain 100 percent of such excess.

The aforementioned issues are just a sampling of what a landlord should consider when negotiating assignment and subletting provisions with a prospective tenant. Of course, the landlord should always seek to impose provisions in the lease requiring that landlord approve, in the landlord's sole and absolute discretion, any assignment or sublease. If a tenant has sufficient leverage to push back on this point, then the landlord would be remiss to not consider the foregoing issues and should attempt to address these issues, either in the letter of intent stage, or in the lease itself.

Scott Timpe, Associate, Cox, Castle & Nicholson in Los Angeles



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