

Creative Solutions is a bi-monthly column offering creative solutions to unusual problems in drafting leases for retail space. Please email your questions or problems you are encountering and your Creative Solutions to Glen Cornblath, gcornblath@ksc-law.com.

Casualty. Usually not a big surprise, right? A landlord can't terminate a tenant's lease if the destruction is "small" enough and can terminate the lease if the casualty is "too big." Landlords and tenants negotiate how they define small or too big but the general concept doesn't change. Of course, landlords and tenants also negotiate time periods and other conditions for rebuilding, like receipt of proceeds, but we're not going to look at those issues in this column.

Let's quickly review the competing interests. The landlord wants to retain flexibility in the event of a casualty. If enough of the center is destroyed, razing the building and starting over may give the landlord a better return on its investment. Either way, the landlord does not want one tenant, particularly a small tenant, dictating what happens to its real estate.

The tenant wants the assurance that it will not lose a good location or favorable economics because some portion of the center burns down. A fire that does not affect a specific tenant should not give the landlord the right to "revisit" the lease terms for that tenant by canceling the lease, or threatening to cancel unless the tenant agrees to new economics.

But here is the twist: A relatively small tenant, say 1,500 sq. ft., takes an end-cap space in a community center. The tenant's use is a destination use and the tenant does not see itself as dependent on the other tenants in the center. This tenant is a credit tenant that will enhance the landlord's center and the bottom line. The tenant does not want the landlord to be able to terminate, and ideally wants the landlord to rebuild regardless of how much of the center is destroyed in the casualty.

One solution is for the landlord to agree that if there is a casualty and the landlord wants to terminate this tenant's lease, the landlord must also terminate the leases of the other tenants in the shopping center. That way the tenant knows the landlord is not singling out this tenant for termination and using the casualty as an excuse.

The landlord may find this a viable solution because it preserves the landlord's ability to redevelop the property in case of a total or near total casualty. The landlord would need to terminate all the leases anyway in order to rebuild a new concept, so this extra requirement is really not burdensome.

In addition, the tenant may require the landlord to re-lease the space it had prior to the casualty, on the original lease terms. A two year time frame, or another time negotiated by the parties, may be the appropriate time in which the landlord remains obligated to re-lease the space to the original tenant. This solution prevents the landlord from using the casualty as an excuse either to dump the tenant in question or to increase the economic terms of the lease, while also not unfairly requiring the landlord to build a shopping center when an office building is now a better use.

What else might the tenant want/landlord offer? The tenant might want an option to be in the first floor retail of any new development the landlord may build on the site. If the use is appropriate, the tenant may view the first floor of an office building or condominium tower as a great location. While it would be difficult to agree upon economic terms in advance due to different construction costs for a new use, the landlord and tenant may negotiate a “market” based option in which the tenant can elect to take space in the new use, provided there will be retail users. The landlord may find this beneficial if lenders want to see pre-leasing activity.

The landlord may also agree to build the tenant an outlot building on a portion of the property while the remaining property is put to a new use. Depending on the configuration of the property, and the new use, an outlot building for a bank or convenience store or video store may be to everyone’s advantage.

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