

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

Nothing is simple anymore, right? What could be a basic transaction -- developer purchases land, builds building and parking, leases on a long term basis to credit national tenant, closes on favorable long term financing -- becomes a tricky minefield when we introduce one new factor: Ground Lease.

Owner of a choice parcel won't sell to Developer. Instead, Developer ground leases the land for 20 years with options to renew for an additional 40 years. The Ground Lease is triple net so Owner only collects rent.

Next, Developer enters into a lease for 60 years with early termination rights starting in year 20 with a credit national Tenant. The Developer-Tenant lease term matches with the term of the Ground Lease; Tenant pays all taxes and virtually all maintenance and repair costs. At this stage, we have an easy deal.

Developer arranges for leasehold construction financing with Bank, and a commitment for permanent financing from a pension fund. Tenant and Bank previously negotiated a form subordination, non disturbance and attornment agreement (SNDA) that both can live with. The permanent lender is satisfied with the SNDA Bank uses and agrees to use that form.

So far so good. Now, Tenant wants Developer to arrange a SNDA-like agreement with Owner. After all, if Developer defaults under the Ground Lease, Tenant will lose its lease plus its leasehold improvements, not to mention its competitive advantage by being at that location. Tenant wants Owner to agree that if Developer defaults under the Ground Lease, but Tenant is not in default under its lease, Owner will not disturb Tenant's possession or rights under the Lease and will simply step into the shoes of Developer under the Developer-Tenant lease. Owner agrees.

However, Bank enters the picture with its perspective. If Owner terminates the Ground Lease and steps into Developer's shoes under the Developer-Tenant Lease, the Bank no longer gets the income stream to pay back the loan. In addition, since Bank's lien is only on the leasehold, if the Ground Lease is terminated, its mortgage is terminated! This Bank is now angry.

Bank tells Developer that as a condition of funding the construction loan, Owner must agree with Bank that in the event of a default by Developer under the Ground Lease, Owner must give Bank notice and an opportunity to cure the default. If the default can not be cured easily or at all, Owner must wait while the Bank forecloses its mortgage on the leasehold interest under the Ground Lease, steps into the shoes of Developer and then cures the default, or Owner agrees that once Bank is in the place of Developer, Owner will "waive" the default and allow Bank to operate as the tenant under the Ground Lease.

Now we introduce the next level of complication: the Owner's original lender -- the Fee Lender. For that creative solution, call or e-mail the author.

Glen Cornblath is a partner in the Chicago law firm of Krasnow Saunders Cornblath, LLP, (312) 755-5700. His practice involves all aspects of real estate, including acquisition of undeveloped land, development of retail, office and industrial facilities, financing, leasing for both anchors and in-line tenants and sale of developed property.