

SHOPPING CENTERS

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Outparcels and leases: Avoiding surprises

Outparcels have become a staple of shopping center development and leasing. There is hardly a new shopping center that is not adorned with at least one or two outparcels sitting at the front or sides of the development. In fact, given the continued growth of pharmacies, banks and restaurants, coupled with the selectiveness of supermarkets and other anchors, many developers opt to develop their parcels exclusively as a "pad city."

Given the importance of outparcels to the modern-day shopping center, developers and tenants must take care in negotiating outparcel leases, as many of the issues raised by outparcel development are not addressed in a typical shopping center lease. Worse yet, when the players attempt to document an outparcel transaction using a typical shopping center lease, they find that the document has created many unintended results.

The first consideration in pad leasing is "what am I leasing?" Depending on the



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type of project, a landlord may believe it is leasing the entire outparcel to the tenant, meaning the building footprint and the associated parking. Although this may be the case, consider the implications.

From the landlord's standpoint, if the "premises" includes the parking areas, the tenant may have liberal construction and alteration rights over the "premises". Therefore, in leasing the premises, a landlord may inadvertently give the tenant the right to alter its

parking area, curbs, parking lot lighting and other site improvements. Although, in a condemnation, if one foot of roadway bordering the outparcel is condemned, and that roadway is within the boundaries of the premises, the tenant may now have termination rights or rights to share in the award for that taking.

From the tenant's perspective, if the "premises" includes the parking area, and the lease is not drafted properly, the tenant may now be responsible for constructing, maintaining, lighting or insuring the parking areas.

Another area of outparcel leases that is often passed over without proper attention is common area maintenance. Many outparcel transactions are ground leases. In a typical shopping center ground lease, the common area expenses shared by all parties includes expenses associated with tenant-buildings. However, since an outparcel tenant constructs its own building, it usually has the obligation to maintain that building. Therefore, if the tenant pays 100% of the cost to maintain its own building, and then a

For these reasons, and others, many landlords and tenants are moving to fixed payment CAM. In these arrangements, the tenant simply pays a negotiated CAM. This amount typically increases over time, either by CPI, the same increases as rent or some other pre-negotiated increase. Fixed CAM has the added benefit of reducing shopping center administration for the landlord. One downside, however, for landlords is how lenders view these payments. Whenever a lender sees that a lease may not be "triple net" in the pure sense, there may be resulting pricing adjustment on the loan to address the possibility that the fixed payment is not sufficient to pay all the CAM expenses, thereby requiring the developer to reach into its pocket to pay common area costs.

There are various other issues, like the few examples above, that simply do not translate when applying a shopping center lease to an outparcel deal. If the parties do not consider these items up front, before the deal is signed, they often discover many unpleasant surprises