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Seminar 11
The Active Ingredients in Grocery Store Leases
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by:

David J. Larsson
Larsson & Scheuritzel P.C.
Centre Square West, Suite 3510
1500 Market Street
Philadelphia, Pennsylvania 19102
dlarsson@larssonlaw.com

Eric Astrin
Director, Real Estate & Special Counsel
WeWork
1372 Peachtree Street NW
Atlanta, Georgia 30309
eric.astrin@wework.com
1. INTRODUCTION

This seminar will focus on the active ingredients in grocery store leases: key clauses (hereinafter, "Lotsaclauses®") that will launch stimulating discussion and provide attorneys and real estate stakeholders with useful tools for approaching (and sometimes even resolving) daunting issues in supermarket lease negotiations. Lotsaclauses® is ICSC-approved to treat both Pernicious Anchreatitis and Noxious Developatosis, diseases in which the ambitions of, respectively, a supermarket anchor tenant and a developer become inflamed. In the event of an unsigned deal that persists longer than 2 years or a painful individual negotiation session that persists longer than 8 hours, the attorney should seek immediate in-house counsel assistance and avoid telling the brokers about the delays.

2. WHAT ARE THE ACTIVE INGREDIENTS OF GROCERY STORE LEASES?

In our search for the "active ingredients" of grocery store leases, the presenters of this seminar canvassed several different persons with experience in negotiating grocery store leases. These persons include: a CEO of a supermarket retailer; a general counsel of a supermarket developer/owner; a person who spent decades in the business as a vice president of real estate and development for a supermarket retailer and then another decade as a consultant to supermarkets; both in-house and outside counsel to one of the world’s largest retailers; a director of real estate for a disruptor in the U.S. grocery market, a director of real estate with several years' experience with grocery stores in Europe, and several other people with unique and valuable insights on the supermarket business and where it's going: the presenters owe a substantial vote of thanks to each of these persons (sometimes referred to as our "participants") for their generous offerings of time and insight.

The open-ended questions that we asked our participants were:

• **What 3 supermarket lease clauses do you care about the most?**
• **What supermarket lease clauses do you think will change the most over the next decade?**
• **Will robots really come and eat all of our jobs? Or, more precisely, will robotic technologies render the big box supermarket a thing of the past?**

**What question did I not ask you that I ought to have?**

The presenters found this participatory process fun, enlightening, and, in many respects, quite surprising. One lesson we have surely drawn from this exercise is that the "active ingredients" of grocery store leases are not written in stone, and stand still for no woman or man: they constantly evolve and change: "The food marketplace is going to change more in the next 10 years than it has in the past 50." We who labor in the vineyards of supermarket shopping center leases need insight in order to help our clients produce lease documents (which typically affect our clients' fortunes for decades to come) that successfully navigate such a dynamic environment. In organizing these materials, we have looked back 50 years to the "Malaise Era" in order to show the past, present, and possible future of some key lease clauses identified by our participants. The ensuing discussion provides a sense of some of the dynamics that our participants and we believe can reasonably be expected to arise as these clauses continue to evolve over the next decade.
3. THE BUSINESS CONTEXT: SWEEPING NEW DEVELOPMENTS IN THE SALE OF GROCERIES

While the acquisition of Whole Foods by Amazon in 2017 shook the grocery industry and grabbed media attention, one of our senior management supermarket participants directed our attention to Ocado, which calls itself "the world's leading pure play online grocer." Ocado operates Customer Fulfillment Centers (CFCs), including an 18 acre (784,080 square feet) warehouse building in Andover, Hampshire, UK, containing "1,100 waist-high cuboid swarm robots, zipping along a grid system the size of several football pitches." Prior to a fire in February, the Andover CFC was processing 65,000 grocery orders per week. From the moment those 65,000 orders were placed online to the moment the orders arrived at their customers’ doors, there was no human intervention.

The same participant also directed our attention to the announcement in May 2019 that The Kroger Co. has entered into an exclusive partnership with Ocado to build three new automated warehouse facilities in the US in 2019, with the aim to identify up to 20 possible sites for US e-commerce facilities over the next three years. One retail analyst remarks, "Ocado’s current logistics and technical expertise in supporting online grocery fulfillment in Europe allows Kroger to potentially leapfrog both Walmart and Amazon in this space." Not only does the knowledge make Kroger better positioned to succeed in e-commerce, but Ocado has also illustrated the ability to operate profitably in the e-commerce space, something yet to be realized in the U.S. across any major grocery retailer (emphasis added). On-line videos of the Ocado Andover CFC are available at the URLs quoted in the Endnotes.

If the Kroger/Ocado partnership holds up, then Kroger may be able to enter whole new markets (e.g., the northeastern US) solely via CFCs -- i.e., without retail supermarket stores in shopping centers -- and achieve significant penetration in those new markets without having to bear the massive costs associated with acquisition, development, construction, and operation of new, conventionally-sized supermarket buildings.

This trend could have a deleterious effect on the cash flow of we who labor in the vineyards of supermarket shopping center leases!

The Kroger/Ocado exclusive arrangement may turn out to be the most important shopping center "exclusive" clause signed in 2019: after all, all of Kroger's competitors are, for now, locked out of using the Ocado e-commerce solution for grocery sales in the US.

SUPPORT FOR THE PROPOSITION, “YES, THE ROBOTS WILL REALLY COME AND EAT ALL OF OUR JOBS”

One of our senior management supermarket participants expects that the rise of profitable e-commerce competitors in the grocery sector -- over and above Walmart and Amazon -- will likely have a major economic impact on all sorts of clauses in existing and new supermarket leases. The supermarket tenant now needs to view every shopping center lease clause through the "filter" of competition with e-commerce -- even very basic clauses, such as term, store size, and rent and other occupancy costs may need to be revisited.

Several participants also noted that robotic technologies will also have site-specific effects on supermarket operations within shopping centers. One developer/landlord participant observes that robots will certainly take over more and more tasks associated with store cleaning, stocking of goods, and price checking.

Another participant (development consultant to a supermarket retailer) predicts that staple goods, such as paper, household items, detergent, and the like -- say, for example, aluminum foil and other goods listed on the
"Other Grocery Items Exhibit" encountered in paragraph 4 below -- are particularly susceptible to rule by our new robot overlords, due to the ease of ordering/restocking.

Another participant observes that pantry items (rice, boxed items) are all the same, so delivery is easier if the cost is right. If retailers (whether on-line or omni-channel) get customers to make that switch with robots/warehouses sending out orders with initial losses, and then slowly raise prices, "my personal opinion is that people will stick with it."

Yet another participant expects that very large-scale supermarkets will decrease over the next 10 years, with the trend toward more and more mid-size and smaller stores. Convenience and pricing (with appropriate selection) will win. Most store checker jobs will be eliminated within 10 years, with more self-checkout and "helpers" guiding customers through their own checkout process. "As a user of the self-checkout via hand-held computer carried around the store, I think that will make huge strides if stores are able to control inventory loss with that method."

One of our senior management supermarket participants notes that there are site-specific methods for competing with Customer Fulfillment Centers (CFCs), via so-called robotic micro-fulfillment centers (MFCs). For example, companies such as Takeoff and CommonSense Robotics deploy their MFC technology in underutilized space in existing supermarkets, thereby combining the proximity and convenience of the store with the efficiency of automated warehouse technology: "Ocado takes two years to open a facility, but we do it in three months."

Meanwhile, Walmart is deploying its own MFC technology, the Alphabot system, which works behind the scenes automatically to bring items from storage to associates who will consolidate the items in the customer order. The system is housed in a 20,000-square-foot extension connected to an existing supercenter store in Salem, New Hampshire; the extension also serves as a dedicated grocery pickup point with drive-thru lanes for customers.

SUPPORT FOR THE PROPOSITION, "NO, NOT REALLY"

The same development consultant who expects to see the robots take over the care and handling of the items on the "Other Grocery Items Exhibit" also opines that the sweeping statement, "Robotic technologies will render the big box supermarket a thing of the past" is not true: for example, on-line retailers are starting to realize the value of bricks and mortar stores, and vice versa. Supermarkets will continue to build on that value, and compete with e-commerce, by becoming more -- not less-- "human." Examples:

-- **In-Store Pharmacists**: Pharmacists (66%) rank just right behind nurses (84%) and doctors (67%) in public trustworthiness ratings of "very high" or "high. " This is one of the drivers of the increased prevalence of in-supermarket pharmacies: customers seeking the "human touch" are more likely to come into your supermarket if your supermarket has good pharmacists.

-- **In-Store Dieticians**: Using the same logic, supermarkets are actively expanding the use of dieticians to provide counsel to customers for even more "human touch."

A more junior participant believes there will always be a need for a supermarket because (i) people have immediate/emergency needs, (ii) some people do not have the access/means to utilize the robotic technologies (i.e. some people do not have bank accounts or credit cards and only make cash purchases), (iii) people like to be able to inspect their products before purchase -- especially produce, dairy, meat, fish, and poultry (another participant adds "bakery" to that list). The same participant believes that retailers are finding creative ways to
react to the robotic technologies and incorporate them into their business models. The retailers that embrace the
technologies, rather than fight against them, will remain so that we keep our jobs.

One of our senior management supermarket participants observes that the core of the supermarket
business in 2019 is now all about "meal occasions" and "snack occasions:" "It is a grocer’s fundamental purpose
to satisfy customer needs across all meal occasions for the family—that’s 27 meal occasions and 10 snacking
occasions per week on average." To that end, our participant expects to face even more intense competitive
pressure to add "grocerants" to supermarkets -- restaurant-style and take-out prepared food options -- a term that
is now old enough that the fourth annual Grocerant Solutions Summit occurred in October 2018.

4. TERM

Past:

A typical supermarket lease during the Malaise Era might have contained a "Term" clause that looked
like this:

\[
\text{The initial term shall commence on the date hereof and shall continue for a period of 20 years after the first day of the first month which commences on or after the commencement date of the initial term. At the expiration of the initial term of this lease, Tenant shall have the right or option to renew this lease for seven (7) additional terms of five (5) years each, upon the same terms and conditions as herein contained except that the rent shall be …}
\]

Present:

Fast forward to today: a typical supermarket lease in 2019 might contain a "Term" clause that looks like this:

\[
\text{Unless sooner terminated, the Term shall continue to and shall include the date (such date, or, if the Term is renewed, the date of expiration of the latest Renewal Period, as hereinafter defined, for which Tenant shall have exercised its option to renew, being hereinafter called the "Expiration Date") that is:}
\]

1. twenty-five (25) years following the day before the Rent Commencement Date if the Rent Commencement Date is the first day of a month, or

2. twenty-five (25) years following the last day of the month in which the Rent Commencement Date occurs if the Rent Commencement Date is not the first day of a month.

Provided that no Uncured Tenant Default exists at the time of the exercise of the applicable Renewal Period, Tenant shall have five (5) successive options to renew the Term from the dates upon which it would otherwise expire, for successive periods of five (5) years each (each such period, a "Renewal Period").
Discussion and Analysis: To date, not much has changed since the Malaise Era, except that some supermarket leases in the past few years contain a 25-year initial term in order to attract more favorable financing -- and therefore cheaper rent for the supermarket.

Future:
Given the rise of profitable e-commerce competitors in the grocery sector described in paragraph 3 above, will the at-least-20-year initial term supermarket lease soon become a shining artifact of the past? One senior management supermarket participant expects the initial term of supermarket leases to drop to 15 years or fewer: which, in and of itself, would be a marked departure from supermarket lease norms that have been in place since the Malaise Era. The same participant also wonders how this drop in initial term will affect the financing of supermarket-anchored shopping centers.

5. SUPERMARKET LEASED PREMISES

Past:
A typical supermarket lease during the Malaise Era might have identified the "Leased Premises" for the supermarket as:

Certain store premises containing approximately 55,268 square feet of gross
floor area of space built on a portion of the shopping center located at
[ADDRESS]

Present:
Fast forward to today: a typical supermarket lease in 2019 might identify the "Leased Premises" for the supermarket as:

a one (1) story building in the location and with the dimensions shown on the
Lease Site Plan and containing approximately 66,100 square feet of first floor
Gross Floor Area (plus Mezzanine and Vestibule).

Discussion and Analysis: The supermarket building grew by 20% from the Malaise Era to today: and, let's face it, that's just the number of square feet on which the supermarket is willing to pay rent! The "Present" language hints strongly that the supermarket will not be paying rent on the Mezzanine or the Vestibule, which could mean several thousand more square feet of building area per local zoning and building code definitions.

Future:
Median total supermarket store size, which was 35,100 square feet in 1994, peaked in 2006 at 48,750 square feet before settling down to 41,300 in 2015. The massive competition to sell stock keeping units (SKUs) of goods described in paragraph 3 above (with respect to the rise of profitable e-commerce "straight-up grocery" competitors in the grocery sector) and also described below in paragraph 6 below (with respect to other types of retailers that increasingly look to sell SKUs that are being sold in supermarkets) will put downward pressure on the size of supermarkets.

One supermarket-owner participant believes that e-commerce will definitely reduce the size of supermarkets as customers eventually make 20% to 25% of their food purchases via e-commerce. The
participant recalls a recent lease negotiation session during which the developer was pushing very hard for a longer supermarket operating covenant period, which caused the participant to muse, out loud, "Do you think I'm really going to need 65,000+ sf of space for this supermarket business 10 years from now?" Another participant in the same negotiation remembers that moment, and also remembers thinking, "Wow, Landlord, you'd better hope that Tenant doesn't start thinking too hard about that question and signs this Lease!"

6. RENT AND OTHER OCCUPANCY COSTS

**Past:**

A typical supermarket lease during the Malaise Era might have required Landlord to construct a new 55,000 sf supermarket building for Tenant in return for (i) Base Rent that began at $1.50 per square foot per annum (i.e., $82,500), plus (ii) Percentage Rent equal to 1% of the amount by which gross sales exceed the "natural breakpoint" of $8,250,000), plus (iii) Tenant's pro rata share of common area maintenance (all set forth in a single paragraph containing 3 short sentences, plus (iv) Tenant's pro rata share of real estate taxes (all set forth in 5 short paragraphs).

**Present:**

Fast forward to today: a typical supermarket lease in 2019 might (i) require Base Rent that begins at $18.00 per square foot or more per annum, and (ii) contain 3 full lease pages on Common Area Maintenance costs alone, another 4+ full lease pages on real estate taxes alone, and another paragraph on reimbursement of Landlord's insurance premiums. It will almost certainly not contain percentage rent.

**Future:**

One supermarket-owner participant believes that, given the e-commerce and other competitive pressures outlined above, the downward pressure on supermarket rents will be stronger than ever. From the owner's point of view, the amount of occupancy costs that are affordable for a given location are purely a function of the volume projections, and, as we have seen, store sales volumes are likely to shrink and the retail sales area of physical stores is likely to shrink, as well, due to the impact of e-commerce CFCs and MFCs, which means that the rents will likely have to reduce proportionately, as well. Supermarkets that can generate $1M to $2M per week in sales will likely become few and far between.

Another participant (development consultant to a supermarket retailer) counsels that supermarket operators will need to keep a careful eye out for (in order to limit, as much as possible) "mark-to-market" occupancy cost provisions in supermarket leases, examples of which include (i) percentage rent clauses, (ii) CLIs (cost of living increases), and (iii) any limitations or restrictions on the exercising of fixed-rent renewal options (e.g., provisions that say that only the "original tenant" is entitled to exercise any renewal options). The problem: (A) in a world of declining retail store volumes, rents that automatically "grow" will soon grow out-of-whack with store volumes that do not grow, and (B) the unit price of occupancy costs associated with competing e-commerce facilities, such as CFCs, are already inherently lower than the unit price of occupancy costs associated with retail stores, so each increase in retail occupancy costs will make the stores just that much more uncompetitive with the e-commerce alternatives.

7. EXCLUSIVE USES (SUPERMARKET RESTRICTIVE COVENANTS; RADIUS CLAUSES)

**Past:**
A typical supermarket lease during the Malaise Era might have contained a "supermarket restrictive covenant" clause that looked like this:

Landlord agrees not to use, let or sublet the use, letting or subletting of any other store in the Shopping Center or on any other ground owned, leased or controlled by Landlord within 3,000 feet of the boundary of the Shopping Center for the sale or storage of food, or for parking of motor vehicles in connection with the sale or storage of food, and Landlord agrees that this restriction will run with the land and be binding upon Landlord and Landlord's heirs, personal representatives, grantees, successors and assigns and shall be incorporated in any deed or deeds covering the sale or other disposition of said restricted premises by Landlord. This restriction shall not apply to the AAA rated department store (K-Mart) located in the Shopping Center. This restriction shall not apply to a luncheon counter, soda fountain, restaurant or of any eating place where the restricted items are consumed on the premises of such business, provided no drive-in restaurant shall be located in the shopping center without Tenant's written approval. This restriction shall not apply to the sale of food for off premises consumption by one drug store which devotes no more than 1,000 square feet to the sale and offering for sale of foods for off-premise consumption, and to parking in connection therewith.

Discussion and Analysis: Only "the sale and storage of food" is restricted! There's not a whisper of exclusives or restrictions re: non-food items such as pharmacy, health and beauty aids (HBA), pet food or pet items, or "other grocery items" such as paper goods or aluminum foil. Then again, the only "carve-outs" from this restrictive covenants are "a luncheon counter, soda fountain, restaurant or of any eating place where the restricted items are consumed on the premises of such business," a restriction that would not work very well for most eating places in 2019, very few of which restrict their customers solely to on-premises consumption.

Present:

A typical supermarket lease in 2019 might contain a "Restrictive Covenant" clause that looks more like this:

1. Landlord covenants and agrees that neither Landlord nor any Affiliate or Related Entity of Landlord (collectively, the "Landlord Parties"; each, singly, a "Landlord Party") shall, directly or indirectly, lease, rent, sell, or permit to be occupied:

   1.1. any premises within the "Restricted Area" (defined as the Shopping Center, together with any other premises owned, leased, controlled, or occupied by any Landlord Party within a radius of ___ (___) miles from the Shopping Center), as a drugstore, pharmacy, a super drugstore or super pharmacy, or combination drugstore or pharmacy and food mart (including CVS, Walgreen's and/or Rite Aid) (collectively, a "Pharmacy"), hyper market, supermarket, mini supermarket, convenience food, or grocery store (including Shaw's Supermarket,
Stop & Shop, Giant, Acme, Fresh Grocer, Aldi’s, Save-A-Lot, Bottom Dollar, Cumberland Farms, Wawa, and/or 7-11) (collectively, a “Supermarket/Grocery”), club store commonly known as warehouse club, membership club, and/or wholesale club (including BJ’s Wholesale Club, Sam’s, Costco, and/or Wholesale Depot) (collectively, a “Club Store”), combination discount department store/supermarket (including Wal-Mart Supercenter and/or Super KMart and/or Super Target) (collectively, a “Supercenter”), and/or any combination of the foregoing; or

1.2. any premises within the Shopping Center as a discount department store (including Wal-Mart, KMart, and/or Target) or unit price store, including what is commonly known as a dollar store or ninety-nine cent store or other store with a unit price lower than a dollar or ninety-nine cents (including Dollar General, $.99 Store and/or Dollar Express), and/or any combination of the foregoing.

2. Landlord covenants and agrees that, except as otherwise expressly provided in this Lease, Landlord shall not permit any occupant or occupants of the Shopping Center to sell, and Tenant shall have the exclusive right in the Shopping Center to sell:

2.1. prescription drugs (“Prescription Drug Items”); provided that the foregoing shall not prohibit any doctor, dentist, or other such professional, from providing medical, dental, or other such professional services to their patients;

2.2. all pet products, including cat food, dog food, cat litter, and other pet foods (“Supermarket Pet Items”);

2.3. human edibles for off-premises consumption (whether fresh, frozen, packaged, bottled, canned or otherwise), including fish, meat, produce, poultry, baked goods, dairy and egg products, deli and appetizing foods, non-alcoholic beverages (whether canned, bottled, frozen, powdered, or otherwise, including soda, juice, drinks, water, coffee and tea), beer, wines and all other types of alcoholic beverages (collectively, “Supermarket Food Items”), and the Other Grocery Items listed in the “Other Grocery Items Exhibit” (“Other Grocery Items;” the Supermarket Food Items and the Other Grocery Items, collectively, the “Supermarket Food and Other Grocery Items”); or

2.4. health and beauty aids and non-prescription drugs (collectively, “Supermarket HBA Items”).

The sale of Prescription Drug Items, Supermarket Pet Items, Supermarket Food and Other Grocery Items, and Supermarket HBA Items, as described in this Article 2, are herein collectively referred to as the “Competing Primary Uses.”
(a) Landlord may permit restaurants, sandwich shops, fast food restaurants, diners, and luncheonettes, other than a “Bakery” (defined below) (“Restaurants”); provided that:

(i) the aggregate Gross Floor Area of all Restaurants shall not exceed _______________ square feet;

(ii) no Restaurant may sell “Perishables” for off-premises consumption; provided, however, that:

(A) the sale by a Restaurant of any such item of Perishables as a component of a sandwich or other meal for on- or off-premises consumption shall be permitted (by way of example, and not of limitation, the sale of bread and tomato as part of a sandwich; the sale of cookies or fresh fruit as dessert items for on- or off-premises consumption; or the sale of sushi for on- or off-premises consumption);

(B) “Perishables” means produce, baked goods, or uncooked (fresh, frozen, or otherwise) meat, fish, or poultry, typical deli, appy, or other delicatessen foods or dairy products (i.e., milk, cheese, butter and yogurt, it being understood that a food item containing a dairy product as one of its ingredients [such as milk chocolate or pizza] shall not be deemed to be a dairy product for the purposes hereof), except for ice cream, frozen yogurt and individual servings of dairy drinks (i.e., a serving packaged in a container holding not more than sixteen (16) ounces); and

(iii) Landlord shall not permit any occupant or occupants of the Shopping Center to operate any retail sales establishment of any size that is identified or described in print, internet, television, radio, or other media as a bakery (collectively, a “Bakery”); provided that a bagel store (including, by way of example, Einstein’s Bagel, Bruegger’s Bagel Corp. and Manhattan Bagel Co.), a doughnut store (including, by way of example, a Dunkin’ Donuts), and a Restaurant operated and merchandized similar to a Panera Bread are permitted, and do not constitute a “Bakery” for purposes of this provision;

(b) Landlord may permit the sale of candy and/or nuts such as, by means of example and not of limitation, Loft’s, Godiva, or Fanny Farmer;

(c) Landlord may permit the sale of ice cream, frozen yogurt, smoothies, and other such frozen items, such as, by means of example and not of limitation, Baskin Robbins, Carvel, or Smoothie King; and

(d) Landlord may lease, rent, sell or permit to be occupied within the Shopping Center a single store by a single tenant for operation as a discount
merchandise store selling youth-oriented products such as those stores currently operated under the trade name “Five Below”, provided that (i) such store may not sell any Perishables, (ii) no more than 1,200 linear feet of shelf space, combined, of such store shall be used at any time for the sale or display of Supermarket Food and Other Grocery Items, Supermarket Pet Items, and Supermarket HBA Items, and (iii) the sale of any such Supermarket Food and Other Grocery Items, Supermarket Pet Items, and Supermarket HBA Items shall be incidental to the primary business of such store;

Other Grocery Items Exhibit
1. All paper goods typically carried in a supermarket, including paper napkins, paper towels, toilet paper, cups and plates. This does not include writing paper, greeting cards and other such paper goods typically carried in a stationery store.

2. All cleaning and freshening products typically carried in a supermarket, including detergents, soaps, drain/bowl cleaners, floor cleaners, laundry products, window, wall and counter cleaners, oven cleaners, furniture polish, air fresheners and related items such as, by way of example, but not limitation, scouring pads, sponges, mops, brooms and the like.

3. All packaging and other wrapping products typically carried in a supermarket, including aluminum foil, plastic wrap, food and sandwich bags, lawn/leaf/trash bags, sealable containers and the like.

4. All non food baby products typically carried in a supermarket, including diapers/training pants, wipes, and related accessories.

5. All herbs, spices, extracts, oils, powders and other items utilized in the preparation of food and typically carried in a supermarket.

Discussion and Analysis: No longer is the supermarket seeking a restriction only on the sale of food for off-premises consumption! Now, it's the “sale or display of Prescription Drug Items, Supermarket Pet Items, Supermarket Food and Other Grocery Items, and Supermarket HBA Items.” And a hard look at the Other Food Items Exhibit makes clear that, yes, if you try to sell a roll of aluminum foil, then the supermarket is coming for you!

While this is perhaps symptomatic of the painful inflammatory affliction previously defined as Pernicious Anchreatitis, it's also true that, for the 2019 supermarket operator, it's surely a jungle out there, and there are lots of stock keeping units (SKUs) of goods for the supermarket to protect. According to the Food Marketing Institute, the average number of items carried in a supermarket in 2017 was 30,098; that's actually down from 46,500 in 2013. SKUs per supermarket increased from 9,400 SKUs per store in 1980 to 35,000 SKUs per store in 2003.
There are lots of people other than traditional supermarkets out there in the jungle trying to sell you those SKUs:

**Limited Assortment Supermarkets – e.g. Aldi:** "In the past, it was common for [a discount supermarket Aldi (known for its low overhead, limited assortment, no-frills business model) store] to carry only 700 SKUs. In the last few years however, Aldi has been diversifying its private label offering. Each Aldi now carries an average of 1,400 high volume SKUs per store."  

**Dollar Stores – e.g., Dollar General:** The Food Marketing Institute defines a “Dollar Store” as “A small store format that traditionally sold staples and knickknacks, but now sales of food and consumable items at aggressive price points that account for at least 20%, and up to 66%, of their volume, e.g., Dollar General, Dollar Tree, and Family Dollar.” As to the SKUs sold in a typical Dollar General, “With 10,000 to 12,000 SKUs per store in a considerably smaller box compared to Aldi, Dollar General offers significantly more variety to its customers. While Aldi generally carries only one private label item of a particular product, Dollar General will most likely carry a number of national brands along with its own private label brand for that same product."  

**Drug Stores - e.g., CVS, Rite Aid, Walgreens:** In 2011, *Supermarket News* noted that food sales in drug stores were advancing faster than at grocery stores (especially in categories such as beer, frozen dinners, and dog food sales).  

**Other Food Competitors (e.g., Office Supply Stores, such as Staples):** Meanwhile, even as non-food retailers such as Staples and Bed Bath & Beyond are shrinking their retail stores and total SKUs per store (e.g., “... Staples ... is ... yanking from shelves about 1,200 poorly selling products and trying to shrink its remaining stores into 12,000 square-foot footprints—downsizing that will cut costs for employees, electricity, and a range of other overhead categories”), they (e.g., Staples, Bed Bath & Beyond) are increasing the amount of food SKUs per store.

Also, while the number of SKUs that are subject to the supermarket’s restrictive covenants continues to grow, it is evident from the "Present" language above that the "carve-outs" continue to grow, as well.

**Future:**  
There was broad consensus among our participants that we who labor in the vineyards with supermarket leases will continue to spend lots of time drafting and negotiating supermarket exclusives and restrictive covenants. After that observation, consensus tends to break down.

One supermarket participant notes that the supermarket industry is becoming more and more competitive, and retailers have to evolve in order to remain relevant. More retailers are expanding their business models to include additional services for the consumer. e.g., installing cafes/prepared meals/cafeterias, installing storage lockers, offering delivery services, offering wine/beer/alcohol tastings, cooking classes, etc. Supermarkets are also offering a larger variety of products beyond just basic grocery items. These clauses have already changed, and will also continue to change as retailers will want broader exclusives so that they can stay competitive.

Another supermarket participant predicts that landlords will eventually eliminate or whittle down supermarket exclusives and restrictive covenants significantly as landlords and their capital sources find that they hamper the ability to lease up a project.
Yet another participant (development consultant to a supermarket retailer) predicts that supermarkets will be pushing back against the presence in a shopping center of grocery staging areas, such as "Amazon Fresh," "Fresh Direct," and "Peapod," and even customer return centers, by prohibiting in the supermarket lease (via the Prohibited Uses clause or via the supermarket Exclusives and Restrictive Covenants clauses):

a space or store used primarily for staging, storing, holding for delivery, and processing Supermarket Food and Beverage Items, including Perishables, for off-premises consumption ("Grocery Staging Area") (including, by way of example, those Grocery Staging Areas similar to the those operated under the trade names "Amazon Fresh," "Fresh Direct," and "Peapod").

Still another participant (senior management of a supermarket retailer) predicts the opposite: the participant notes that all Kohl's stores will be accepting free, unpackaged returns for Amazon customers starting in July 2019, and sees no reason why supermarkets will not do the same: in fact, some already are. Practice point for those representing supermarkets: You'll want to make sure that your anti-storage locker/returns language doesn't inadvertently prohibit storage locker/returns activities that your client needs to put into the supermarket!

One developer/landlord participant observes that supermarkets always come into negotiations with a comprehensive "ask" for food exclusives. Since those supermarket negotiations almost always occur at the beginning of a project, it's difficult for a developer at that early stage of a project to tailor the exceptions that will be needed once the lease-up process continues. At that point, as a developer, you don't know yet (a) the identity of the retailers that you will be trying to co-locate with a supermarket, (b) what their food requirements will be (e.g., a partial aisle of food products in a Ross Dress for Less or a HomeGoods or HomeSense), or (c) how those food requirements may have evolved since the last deal the developer completed with that particular retailer.

8. PROHIBITED USES

Past:

A typical supermarket lease during the Malaise Era might have contained a "prohibited use" clause that looked like this:

Landlord shall have no right to construct a discount house, bowling alley, drive-in restaurant or a theatre in the area shown on Exhibit "A" until Tenant has previously consented in writing to the location and construction of such discount house, bowling alley, drive-in restaurant or theatre. (emphasis added)

Discussion and Analysis: Only 4 prohibited uses!

The first prohibited use, "discount house," refers to "any store which operates on a low expense, low markup basis and which emphasizes competitive pricing as a main attraction to win customers," according to a 1964 article in The New York Times, which also names E.J. Korvette and K-Mart as examples.

Interestingly, the same lease contains the following "inducement tenant" clause:

Landlord, to induce Tenant to enter into this Lease, covenants and warrants that it will construct and complete in the shopping center … one AAA rated
department store with a floor area of at least 55,532 square feet having a lease for initial term of 20 years, terminable only in case of default.

The presence of this "inducement tenant" clause supports the inference that, in 1977, supermarkets' concern with discount houses, bowling alleys, drive-in restaurants, and theatres arose principally from the fear of inadequate parking, which carried over into the 1970s from supermarkets' experiences with central business district (CBD) stores in earlier decades: "Many national chains and the local businesses had been plagued by inadequate parking in many of the central business districts and the shopping center concept with more plentiful parking was a great improvement. Customers could find parking any time at a shopping center without having to 'circle the block' several times as had been the case in the CBD."  

Present:

Fast forward to today: a typical supermarket lease in 2019 might contain a "prohibited use" clause that looks more like this:

1. Landlord covenants and agrees that Landlord shall not, without the prior written consent of Tenant, which such consent may be withheld in Tenant's sole and absolute discretion, lease, sell, or permit all or any portion of the Shopping Center to be occupied for any one or more of the following uses (the "Prohibited Uses"):

1.1. a use in violation of any then existing and applicable Law  

[PRESENTERS' NOTE: BRANDING CONCERN];

1.2. any residential (including hotels, living quarters, apartments or residences); industrial or manufacturing [PLEASE SEE DISCUSSION IN TEXT BELOW], assembling, distilling, refining, smelting, agricultural, mining or quarrying use, or warehouse or storage use [PLEASE SEE DISCUSSION IN TEXT BELOW] (other than such activities as are customary and ancillary to the operation of retail, entertainment, and/or service uses of the type permitted from time to time in comparable shopping centers);  

[PRESENTERS' NOTE: PARKING CONCERN]

1.3. "second-hand" store whose principal business is selling used merchandise, thrift shops, salvation army type stores, "goodwill" type stores, and similar businesses;  

[PRESENTERS' NOTE: BRANDING CONCERN]

1.4. "adult" book store or other establishment selling, renting, displaying or exhibiting pornographic materials or providing adult type entertainment or displays of a variety involving or depicting nudity or lewd acts;  

[PRESENTERS' NOTE: BRANDING CONCERN]

1.5. massage parlor;  

[PRESENTERS' NOTE: BRANDING CONCERN]

1.6. any bowling alley;  

[PRESENTERS' NOTE: PARKING CONCERN]
1.7. off-track betting establishment, carnival or amusement park;

[PRESENTERS' NOTE: PARKING CONCERN AND SOME BRANDING CONCERN]

1.8. mobile home park, trailer court, labor camp, junkyard or stock yard (except that this provision shall not prohibit the temporary use of construction trailers during any periods of construction, reconstruction, or maintenance)

[PRESENTERS' NOTE: BRANDING CONCERN];

1.9. dumping, disposing, incinerating, or reducing of garbage (exclusive of dumpsters for the temporary storage of garbage and any garbage compactors, in each case which are regularly emptied so as to minimize offensive odors);

[PRESENTERS' NOTE: BRANDING CONCERN]

1.10. fire, going out of business, relocation, bankruptcy or similar sales (unless pursuant to court order); [PRESENTERS' NOTE: BRANDING CONCERN]

1.11. bar, tavern, restaurant, [PLEASE SEE DISCUSSION IN TEXT BELOW] nightclub, discotheque or other establishment whose reasonably projected annual gross revenues from the sale of alcoholic beverages for on premises consumption exceeds fifty percent (50%) of the gross revenues of such business;

[PRESENTERS' NOTE: PARKING CONCERN AND SOME BRANDING CONCERN]

1.12. offices [PLEASE SEE DISCUSSION IN TEXT BELOW]; provided that (a) retail office use or (b) office space used by Tenant or any subtenant or other occupant of the Shopping Center for administrative purposes ancillary to Tenant's, subtenant's or such other occupant's retail use, and which is not open to the general public, shall not be considered "offices" for the purpose of this limitation; [PRESENTERS' NOTE: PARKING CONCERN]

1.13 auditorium, meeting hall or other place of public assembly;

[PRESENTERS' NOTE: PARKING CONCERN]

1.14. drug treatment, rehabilitation or methadone maintenance clinic or center; [PRESENTERS' NOTE: BRANDING CONCERN]

1.15. "adult" book store, massage parlor or other establishment selling, displaying or exhibiting pornographic materials or providing adult type entertainment, displays of a variety involving or depicting nudity or lewd acts, or any establishment providing nude or topless entertainment or wait staff (or provocative dressed wait staff inconsistent with a first-class shopping center), or any establishment selling or exhibiting pornographic materials (including, without limitation, adult books or videos), provided, however, that the foregoing shall not
prohibit the sale of books and videos commonly carried by national book and/or video retailers (such as Barnes and Noble or Borders) in the [APPLICABLE LOCALE OR METROPOLITAN AREA] [PRESENTERS' NOTE: BRANDING CONCERN];

1.16. the operation of a “head shop”, so-called, or other business devoted to the sale of articles or merchandise normally used or associated with illegal or unlawful activities, such as but not limited to the sale of paraphernalia used in connection with marijuana [PLEASE SEE DISCUSSION IN TEXT BELOW], cocaine or other controlled drugs or substances [PRESENTERS' NOTE: BRANDING CONCERN]; or

1.17. funeral parlor or mortuary [PRESENTERS' NOTE: BRANDING CONCERN AND PARKING CONCERN];

1.18. flea market [PRESENTERS' NOTE: BRANDING CONCERN AND PARKING CONCERN];

1.19. church, school, day care center or related religious or education facility [PLEASE SEE DISCUSSION IN TEXT BELOW]; [PRESENTERS' NOTE: PARKING CONCERN]

1.20. an on-premises dry cleaning plant or central laundry or Laundromat; provided, however, this restriction shall not apply to any dry cleaning facility providing on-site service oriented to pickup and delivery by the ultimate consumer, including nominal supporting facilities; [PRESENTERS' NOTE: ENVIRONMENTAL CONCERN, THEREFORE BRANDING AND COST CONCERN]

1.21. selling or leasing automobiles, trucks, trailers, or recreational vehicles; [PRESENTERS' NOTE: PARKING CONCERN; POSSIBLY SOME BRANDING CONCERN, AS WELL]

1.22. veterinary hospital or animal raising or boarding facilities; [PRESENTERS' NOTE: BRANDING CONCERN AND PARKING CONCERN];

1.23. car wash; [PRESENTERS' NOTE: BRANDING CONCERN AND PARKING CONCERN];

1.24. living quarters, sleeping apartments, or lodging rooms; [PLEASE SEE DISCUSSION IN TEXT BELOW]; [PRESENTERS' NOTE: BRANDING CONCERN AND PARKING CONCERN];

1.25. tattoo parlor; [PRESENTERS' NOTE: BRANDING CONCERN];
1.26. automotive service and repair; [PRESENTERS' NOTE: BRANDING CONCERN AND PARKING CONCERN];

1.27. cinema or movie theater [PLEASE SEE DISCUSSION IN TEXT BELOW]; [PRESENTERS' NOTE: PARKING CONCERN];

1.28. health club, health spa, or exercise facility; [PLEASE SEE DISCUSSION IN TEXT BELOW]; [PRESENTERS' NOTE: PARKING CONCERN]; and

1.29. medical/dental offices or health care facilities. [PLEASE SEE DISCUSSION IN TEXT BELOW] [PRESENTERS' NOTE: PARKING CONCERN AND POSSIBLY SOME BRANDING CONCERN, AS WELL];

Discussion and Analysis: At least 29 prohibited uses! Perhaps another example of painful Pernicious Anchreatitis.

Again, many of these 29 prohibited uses (e.g., the ones marked above as "PARKING CONCERN") reflect supermarkets' continued concern that the uses in question could result in inadequate parking for supermarket operations, especially if the uses are undertaken in close proximity to the supermarket. Others (e.g., the ones marked above as "BRANDING CONCERN") reflect supermarkets' concern with the branding and reputation of the shopping center in which the supermarket is located: the main questions may be, "Does this use help contribute to a warm, inviting, family-friendly retail environment?" and "Do customers associate our supermarket with a first-class shopping center environment? Or is our business at this location suffering because of the environment of this shopping center?"

Future:

Several of our participants were adamant that the "Prohibited Uses" clauses of supermarket leases are ripe for extensive change over the next decade:

Accordingly to one participant, as brick and mortar stores decrease, the need for vibrant centers will outweigh the perceived drawbacks associated with some of the traditional prohibited uses. More and more prohibited uses will be limited in size rather than subjected to outright prohibition. For example, stores that sell legal marijuana and marijuana derivatives are thriving in Scottsdale, Arizona, and other markets, and will continue to expand into the affluent centers. "Fancy" cannabis stores will move out of the run-down strip malls of yesterday and into the "first-class shopping centers" of tomorrow. Landlords will attempt to keep control via architectural and other subjective standards to protect their investment.

Another participant also predicts more "prohibited use" flexibility over the coming decade: As shopping centers evolve -- even traditional grocery-anchored community shopping centers -- many of the uses that have historically constituted "prohibited uses" under supermarket leases will need to be modified to meet current and future market conditions. Examples: see all of the underlined-bold-italics provisions noted in the above list of 29 Prohibited Uses, and particularly:

- restaurants: Although these have historically been viewed by supermarkets as parking hogs and also straight-up competition for supermarkets when it comes to prepared food sales, the reality is that restaurants
are one of the still-thriving elements of brick-and-mortar retail, and even one senior management supermarket participant conceded that it's simply not going to work for supermarkets to try to insist on hard limits on restaurant uses. **Practice point for those representing supermarkets:** You'll want to make sure that your anti-restaurant language doesn't inadvertently prohibit the "grocerants" that your client needs to put into the supermarket!

- **health/medical uses, including health clubs, medical office space, dispensing medicines and writing prescriptions:** Supermarkets have historically viewed these types of uses as parking intensive, and have generally tried to eliminate them entirely or limit them. This approach is unlikely to work as the decade goes on: the traditional "big box" retail of the past 2 decades will likely continue to stagnate and/or decline, and shopping center owners will need to move to accommodate more and more health providers who wish to push their business into brick-and-mortar retail for purposes of market penetration, so that there will be urgent care facilities and health clubs/exercise facilities in many, if not most, supermarket-anchored shopping centers;

- **office uses; theatre and other entertainment uses; residential uses:** Supermarket opposition to office uses and residential uses, usually due to parking concerns, will need to evolve and moderate to accommodate the needs of shopping center owners to convert their traditional purely retail facilities to mixed use projects that comprise retail, office, entertainment, and residential elements.

- **warehouse/storage uses:** Warehouse and storage uses, especially self-storage, have historically been viewed with disfavor by supermarkets who seek a warm, inviting retail environment for its customers. Developer/owners, in contrast, especially those who must contend with empty large anchor tenant vacancies in regional malls and shopping centers, need to find new space users who are eager to expand into available space. One such category of space users is self-storage providers. One result: the multi-site deal announced by mall owner CBL with Hickory Capital Group to convert empty large (i.e., 93,000 sf) former retail anchor spaces (e.g., Sears) to self-storage spaces.

9. **SUPERMARKET PERMITTED USES**

**Past:**

A typical supermarket lease during the Malaise Era might have contained a "permitted use" clause that looked like this:

> Landlord agrees that nothing in this lease shall be construed as compelling Tenant to keep the store in or upon the demised premises open for business, but Tenant shall have the privilege of closing said store at any time, provided Tenant shall continue to pay the minimum monthly rental as set forth in this lease and performs its other obligations under this lease. In the event after the commencement of the initial term, Tenant permanently closes its demised store for business, Landlord, at its option, may terminate this lease by written notice to Tenant provided that Tenant, at the time of receipt of said notice has not sublet all or any portion of the demised premises. Tenant shall not be deemed to have permanently closed its demised store for business when closed because of casualty damage, restoration of damage, repairs, alterations, strikes, or for any reason beyond the control of Tenant.
**Discussion and Analysis:** Aside from the Landlord "go dark" termination right, there is no limitation on the uses that can take place inside the supermarket. Note that there is no sign of "grocerants" or even the sale of prepared foods of any kind taking place inside the supermarket: in the words of one of our participants, "Compared to 22 years ago, supermarket prepared foods today are a dream!"

**Present:**

A typical supermarket lease in 2019 might contain a "permitted use" clause that looks more like this:

*The Demised Premises shall be used and occupied for the operation of a food supermarket and any one or more of the Incidental Supermarket Uses defined below (collectively, the “Permitted Supermarket Uses”), or, following the Mandatory Operating Period, for any other lawful retail use or purpose. The term “Incidental Supermarket Uses” means and includes any or all of the following uses that shall be incidental to Tenant’s use of the Demised Premises as a food supermarket: Gas Station; in-store pharmacy; health and beauty aids and non-prescription drugs (collectively, “Supermarket HBA Items”); store selling alcoholic beverages for off-premises consumption; in-store mini-bank with ATM; drop-off dry cleaner; in-store medical clinic; baby sitting and/or child care services; children’s nursery; florist; sale of videotapes; sale of donuts, bagels and other baked goods; health food store; in-store sit-down restaurants (including Supermarket Buffets) and franchises, such as Cinnabon and Rita’s Water Ice; the sale of merchandise, goods or services now or hereafter sold or rendered in food supermarkets in [STATE], including those operated by Tenant; and, if permitted by Law, the sale of beer and wines, liquor and all other types of alcoholic beverages. Anything to the contrary set forth herein notwithstanding, Tenant may enter into agreements to license, sublease, sublicense, grant concessions or otherwise permit the occupancy of portions of its food supermarket sales floor area for the Incidental Supermarket Uses. Tenant shall have the right, at all times throughout the Term, to operate within the Demised Premises one (1) Permitted Take Out Restaurant (it being the understanding that, subject to the limitations set forth below, Landlord shall have the exclusive right to operate or permit the operation of the remaining three (3) Permitted Take Out Restaurants currently permitted under applicable zoning law in the remainder of the Shopping Center outside of the Demised Premises). Notwithstanding anything contained in this Lease to the contrary, under no circumstances will Tenant use or permit the use of the Demised Premises for a Prohibited Use or a use in violation of any Exclusive granted by Landlord to another tenant in the Shopping Center during the initial lease-up of the Shopping Center (each, a “Future Exclusive”), provided that no Future Exclusive shall be binding upon Tenant, Tenant shall have no obligation to recognize any Future Exclusive, and Tenant may use the Demised Premises for a use in violation of such Future Exclusive in (a) any portion of the Demised Premises being used for the Permitted Supermarket Uses and/or (b) any portion of the Demised Premises.*
containing in excess of fifteen thousand (15,000) square feet of Gross Floor Area in which a use other than the Permitted Supermarket Uses is being operated (it being understood that each Future Exclusive shall bind Tenant, Tenant shall recognize each Future Exclusive and Tenant may not use the Demised Premises for a use in violation of each Future Exclusive in any portion of the Demised Premises containing less than fifteen thousand (15,000) square feet of Gross Floor Area that is not being used for the Permitted Supermarket Uses). Landlord shall give written notice to Tenant of each Future Exclusive.

Discussion and Analysis: This updated language certainly reflects many of the trends described in paragraph 3, especially the "grocerants" trend.

Future:

One supermarket participant emphasizes the importance of having a broad permitted use in order to have flexibility with the evolving supermarket business, especially with respect to what the supermarket can sell, and having flexibility with how the supermarket can advertise/promote at the location. Having a broadly defined permitted use is also important if the supermarket can assign the lease or sublet a portion of the space, so as to provide more flexibility for the operation of the supermarket business into the future.

A developer participant expects to see and more retailers seeking to add customer returns of on-line purchases as a free service that will drive more customer traffic into their stores. By way of example, all Kohl's stores will be accepting free, unpackaged returns for Amazon customers starting in July 2019.

One supermarket-owner participant notes that the trend toward even more "grocerants" now presents a new and unique challenge: making sure that the "grocerants" enjoy full-blown seating rights, which can sometimes be affected by zoning and planning laws and regulations, including parking requirements.

The same participants also observes that supermarkets are becoming more "experiential," more like a marketplace: more in-store grocerants and coffee/donut shops, in-store eye care, in-store medical clinics, in-store cleaners, in-store banks and financial services.

10. ASSIGNMENT AND SUBLETTING

Past:

A typical supermarket lease during the Malaise Era might have contained an "assignment and subletting" clause that looked like this:

Tenant shall not assign this lease except as set forth below without the written approval of Landlord, which approval shall not be unreasonably withheld by Landlord. Tenant shall have the right to sublet the whole or any part of the premises herein demised, along with appurtenant parking and access rights. Notwithstanding the foregoing, Tenant shall have the right to assign this Lease without Landlord's consent provided that the assignee assumes this Lease in writing, a copy of the assignment and the assumption of the Lease are delivered to Landlord, and the Tenant remains primarily liable for the full performance of this Lease. This Lease shall, without Landlord's consent, survive a merger or
Discussion and Analysis: This clause gives Tenant a fair amount of flexibility. Tenant appears to have a free right to sublet, and Tenant also appears to have a free right to assign the Lease via an affiliate transfer or via a merger or consolidation. What this clause doesn’t do is give Tenant the right to assign the Lease in connection with an asset sale or a stock sale that doesn’t constitute either a merger or a consolidation. This means that Landlord arguably has the right to block an asset sale or a stock sale, and no sophisticated multi-location tenant wants to hand its landlord for a single location the ability to block a transaction in this manner.

Present: A Landlord's initial draft of a supermarket lease today might look like this:

1. ASSIGNMENT AND SUBLETTING.

   1.1. Except as expressly set forth in this Article 1, Tenant may not assign its interest in this Lease, sublet the whole or any part of the Demised Premises, or permit any subtenant to further sublet any part of the Demised Premises without Landlord's consent, which consent shall not be unreasonably withheld, delayed or conditioned, but in all events any such assignment or sublease shall be subject to all of the terms and conditions of this Lease, including the provisions and limitations contained in this Article 1. For purposes of this Article 1, any transfer of ownership interests in Tenant and any assignment by operation of law shall constitute an "assignment" of the Lease that requires Landlord's consent.

   1.2. Subject to the provisions and limitations contained in this Article 1, Tenant may assign this Lease (but only after the expiration of the Mandatory Operating Period), and sublet, grant concessions or license the whole or any portion of the Demised Premises for any retail use not prohibited by the terms of this Lease; provided, however, that (a) Tenant shall remain liable under the terms of this Lease, and (b) Tenant shall forward a copy of all relevant assignment documents to Landlord within a reasonable time thereafter. Notwithstanding the foregoing, Tenant shall have the right to make a Permitted Assignment and a Permitted Sublease (both hereinafter defined) without Landlord's consent. Any assignment made a part of a sale or transfer to a purchaser of fewer than five (5) of the stores then being operated as a “TRADE NAME” shall require Landlord's prior consent, which consent may be withheld in Landlord's sole and absolute discretion, and, if Landlord consents, then any consideration paid to Tenant by such purchaser shall be due and payable immediately by Tenant to Landlord upon Tenant's receipt of such consideration.

   1.3. As to each assignment and assumption of this Lease: (a) a copy of such assignment shall be submitted to Landlord at least thirty (30) days before the effective date thereof, other than if the assignment by Tenant is a Permitted Assignment, in which event notice of such transfer and a copy of the assignment shall be submitted to Landlord not less than ten (10) days after the effective date thereof, (b) each assignee shall assume the obligations of this Lease by
executing, acknowledging and delivering to Landlord a written assumption agreement; (c) any such assignment shall be subject to all terms and conditions of this Lease, and (d) any consideration paid to Tenant by such assignee shall be due and payable immediately by Tenant to Landlord upon Tenant's receipt of such consideration.

1.4. At any time during the Term, Tenant, without Landlord’s consent, shall have the right to make an assignment (a) made a part of a sale or transfer to a purchaser of at least five (5) of the stores then being operated as a “TRADE NAME” or, (b) to any corporation or entity controlling, controlled by, or under common control with Tenant or another corporation or entity into or with which Tenant is merged or consolidated (each a “Permitted Assignment”).

1.5. Tenant, without Landlord’s consent, may sublet portions of the Demised Premises (each such sublease being hereinafter referred to as a “Subletting”, any party Subletting from Tenant being hereinafter referred to as “Subtenant”), provided that:

1.5.1. except as specifically set forth below, absent Landlord’s consent, which consent shall not be unreasonably withheld, delayed or conditioned, in no event shall Tenant enter into more that four (4) Sublettings at any one time;

1.5.2. each Subtenant shall agree, prior to the effective date of the Subletting (which agreement may be contained in the sublease), to attorn to Landlord, at Landlord’s option, in the event this Lease is terminated or surrendered by Tenant or is terminated by Landlord; subject to any right reserved by Subtenant to terminate its sublease if Tenant discontinues the operation of a supermarket in the Demised Premises;

1.5.3. any Subletting shall be subject to all the terms and conditions of this Lease including the provisions respecting Prohibited Uses, Exclusive Uses and Future Exclusive Uses; and

1.5.4. Tenant shall give Landlord at least ten (10) days' prior notice of the Subletting.

1.6. Notwithstanding the provisions of Article 1.5, Tenant shall have the right to sublet all or substantially all of the Demised Premises without Landlord’s consent if such subletting is (a) made a part of a sale or transfer to a purchaser of at least five (5) of the stores then being operated as “TRADE NAME”, or (b) to any corporation or entity controlling, controlled by, or under common control with Tenant or another corporation or entity into or with which Tenant is merged or consolidated (each, a “Permitted Sublease”). Any subletting pursuant to the
foregoing clauses (a) and (b) of this Article 1.6 shall not require any notice to Landlord.

1.7. If this Lease is assigned, Tenant agrees that Landlord, in the exercise of its rights under this Lease, may proceed against Tenant separately, or jointly, before, after or simultaneously with any proceeding against any successors or assigns of Tenant.

1.8. If Tenant elects to assign this Lease or sublet all or substantially all of the Demised Premises for all or substantially all of the remaining Term (a “Total Sublease”), other than pursuant to a Permitted Assignment or a Permitted Sublease, Tenant shall give to Landlord not less than thirty (30) days prior notice of the intended assignment or Total Sublease, and Tenant shall be required to obtain Landlord’s prior consent thereto, which consent shall not be unreasonably denied, withheld, delayed or conditioned. Each notice and request for consent given by Tenant to Landlord shall be accompanied by a statement containing the name and address of the proposed assignee or subtenant and the nature and character of the business to be conducted by the proposed assignee or subtenant. With respect to any assignment which is not a Permitted Assignment or a Total Sublease which is not a Permitted Sublease, Landlord, at its option, shall have the right to cancel this Lease (with the same force and effect as if the entire Term had expired by lapse of time) by giving notice to Tenant (“Transfer Cancellation Notice”) within thirty (30) days after Landlord’s receipt of a copy of the assignment or Total Sublease and the notice and request for consent to such assignment of this Lease or Total Sublease, and by paying to Tenant the Recapture Payment. If Landlord elects to cancel this Lease, and the payment to Tenant of the Recapture Payment, the Term shall fully cease and expire on a date (“Transfer Recapture Date”) selected by Landlord in its Transfer Cancellation Notice, which date shall not be less than fifteen (15) nor more than thirty (30) days after the intended effective date of such assignment or Total Sublease.

Discussion and Analysis: This clause does not give Tenant sufficient flexibility, and is a prime example of the alarming inflammatory affliction previously referred to as Noxious Developatosis. Consider the context: Tenant has successfully done the hard work of building up its supermarket business in the Landlord’s shopping center, heroically fending off daunting e-commerce competitive threats and the other shopping center occupants who are always trying to grab a little bit more of Tenant's profit margin, all the while paying a substantial portion, if not all, of Landlord's debt service via Tenant's base rent payment, along with the shopping center's CAM, real estate taxes, and insurance costs. Now that Tenant finally has an opportunity to enjoy some fruits of its labor via a capital event (e.g., store sale, merger, acquisition, stock sale, asset sale), Landlord points to this clause and asserts a right to inject itself into the middle of that capital event. This is not a clause that a supermarket anchor
tenant can accept, and it will become even more unacceptable as the industry continues to evolve in the manner described above.

**Future:**

More than one of our participants observed that the future is likely to bring more consolidation within the supermarket industry. A large part of the growth of the supermarket industry over the past few years has been acquiring and redeveloping existing boxes rather than building new stores from the ground up. This will continue to be the case. The benefits include:

- More predictable (and favorable) zoning/land use/entitlements environment;
- More predictable (and favorable) construction cost profile;
- More opportunities: Many supermarket sites that enjoy good real estate attributes failed as supermarkets mostly due to poor management performance by prior operators. A good operator can come into many existing sites and turn them into performing stores.

Another participant notes that, in the current increasingly competitive environment, it is more important than ever that supermarkets have the ability to sublease/assign (without Landlord consent or with just prior notice) if the location is no longer profitable, or if there is a need to assign or sublet for some other reason.

11. **CONCLUSION**

We offer the parting reflections of 2 of our participants:

- "Big box leases continue to become more complicated. Although both Landlord and Tenant want to protect against every circumstance; I do not feel this is sustainable. I think it’s important for a discussion to be had about how :Landlord/Tenant disputes can be handled more efficiently once they occur, rather than trying to cover every circumstance ahead of time in each lease. This slows down deals. This is and always will be necessary to an extent but I feel that having more of an understanding between Landlord and Tenant about how each will respond to situations as they arise will allow for the leases to become simpler. Maybe the solution lies in creating more of a regionally accepted lease form (similar to the residential market). This will ultimately put all parties in a better position."

- Are longer leasing negotiations for the grocery store leases worth it? I believe definitely “yes.” As Developers/Owners feel the crunch of softer leasing markets on their grocery store centers and their other centers, developers and owners will always look for ways to increase value/earnings. Sometimes, those ways will increase traffic flow and complement the grocery store business; however, sometimes they will detrimentally affect the grocery store use. As such, the more control the grocery store has in the property’s uses, the more the grocery store can protect their significant investment. However, it is a balancing act and full of judgment calls – there must be concessions and cooperation on both sides to protect the business deal. But as grocery stores have become more important tenants of more varieties of retail locations (not just traditional strip malls), grocery stores should attempt to protect themselves as best they can for the expected changes that are coming as well as the “unforeseeables” in the future.

ENDNOTES:


5 Ibid.


10 https://news.gallup.com/poll/245597/nurses-again-outpace-professions-honesty%20-ethics.aspx, accessed 24 May 2019. While lawyers don’t quite enjoy comparable esteem in the public eye, you’ll be heartened to learn that we do still outpace telemarketers, car salespeople, and members of Congress.


19 Ibid., Note 17.


26 “Planet 13 Holdings is a vertically integrated dispensary operator [whose] approach is completely unique. The company’s off-strip SuperStore in Las Vegas, Nevada, is already the largest cannabis store in the country, and will grow even further by the time it’s fully built out. Currently spanning 16,200 square feet, the Planet 13 SuperStore will eventually feature a coffee shop, pizzeria bistro, events center, and consumer-facing production facility with about a dozen windows for viewing, all of which should be complete by the third quarter of this year. When fully complete, Planet 13’s flagship store will span 112,000 square feet. For added context, the average Walmart spans 105,000 square feet.” “The Disneyland of Cannabis Stores Is Set to Open... Near Disneyland,” Sean Williams, June 11, 2019 (https://www.fool.com/investing/2019/06/11/the-disneyland-of-cannabis-stores-is-set-to-open-n.aspx, accessed June 11, 2019).
