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Workshop 10

Work Letters: The Construction Contract Hiding in Your Lease

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I. Completion Delay Issues

A. Relocation Ramifications
1. Tenant Concerns
   a. Coordination
   b. Contingency Plan
   c. Milestone Schedule
2. Landlord Concerns
   a. Allocation of Business Risk
   b. Pandemic/COVID-19 Risks
   c. Further Limitation of Landlord's Liability
   d. Schedule Exposure Deflection

B. Damages and Losses
1. Tenant Concerns with Landlord Work Delay
   a. Lost Revenue/Operations
   b. Third Party Contract Defaults
   c. Additional Carry Costs
   d. Increased Construction Costs
   e. Seasonal Losses
2. Landlord Concerns with TI Completion Delay
   a. Adverse Effects on the Shopping Center
   b. Co-Tenancy
   c. Loss of Percentage Rent
   d. Lender Issues

II. Remedy Considerations

A. Liquidated Damages
1. Tenant Concerns
   a. Generally
   b. Amount
   c. Target Completion Date
   d. Remedy Election Issues
   e. Narrowly Tailored
   f. Other Requirements

2. Landlord Concerns
    a. Alternative Liquidated Damages Perspective
    b. Passing the Buck
    c. Completion Date
    d. Grace Period
    e. Excused Delay
    f. Liquidated Damages Cap
3. Sample Liquidated Damages Provision - Tenant Favorable

B. Takeover Rights
    1. Tenant Concerns
    2. Landlord Concerns
        a. Loss of Control over Work
        b. Loss of Control of Completion; Potential Delay Implication
        c. Potential Cost Overruns

C. Lease Termination Rights
    1. Tenant Concerns
    2. Landlord Concerns

D. Other Possibilities to Consider
    1. Delayed Rent Commencement
    2. Rent Offset

III. Tenant Improvement Allowance Issues

A. Securing the Tenant Improvement Allowance
    1. Landlord Concerns
        a. Cash Escrow vs. Letter of Credit
    2. Tenant Concerns
        a. Cash Escrow vs. Letter of Credit

B. Disbursing Complexities
    1. Landlord Concerns
        a. Tenant Improvement Payment Timing; Disbursement Conditions
        b. TI Amount and Additional Considerations
    2. Tenant Concerns
        a. TI Allowance Timing and Preferably (Lack of) Conditions

C. Tenant Equity Contributions

IV. Third Party Entanglements

A. Landlord Concerns
    1. Existing REAs and Leases
    2. Quiet Enjoyment
    3. Lease Space Subject to Existing Restrictions and Encumbrances

B. Tenant Concerns
    1. Compliance Assurances
    2. Landlord Reps and Warranties
    3. Sunset Provision
    4. No New Agreements

V. Scope of Work Considerations

A. Qualified Expenditures for Tenant Improvement Allowance
   1. Tenant Concerns
   2. Landlord Concerns

B. Clarification and Coordination of Landlord's Work vs. Tenant's Work
   1. Mutual Concerns
   2. Tenant Concerns
   3. Landlord Concerns

Discussion Hypothetical:

Pumps Plus (or "PP") is a growing company with a popular, recently developed concept, which borrows from numerous other successful ventures, including coffee shops, fast casual restaurants, convenience stores, electric vehicle charging stations and fueling stations, to create a comprehensive shopping experience for people on the go, marketing to a customer base including all ages and socio-economic levels. The idea is to move beyond the traditional boundaries of a gas station and create a pleasant one-stop destination for all of these products and more. PP has expanded rapidly based on the success it has enjoyed and now has over 900 stores on the East Coast of the United States. The standalone facilities on average consist of two acre sites improved with a 4,000 square foot building, curbing, pavement, driveways, machinery, underground storage tanks, a canopy, and motor fuel dispensing equipment.

With the current trends big box shopping centers are experiencing, particularly post-COVID, the PP executive team believes a brief window of opportunity exists to capitalize on the availability of certain prime suburban locations and to redevelop some existing sites in certain high traffic locations to expand its concept. Not surprisingly, many power center landlords have expressed great interest in PP, particularly given the promise of the strong rental rates PP pays coupled with the volume of traffic customers will bring to the center.

From its inception, Pumps Plus has employed a highly leveraged strategic plan. PP leases its entire portfolio of convenience stores and aggressively negotiates for extensive base landlord improvements and eye-popping TI allowances. PP, in turn, generally has been willing to pay above-market base rent to effectively finance its unique build-outs, which it views as indispensable to its brand.

As part of its East Coast expansion plan, PP has identified a seemingly ideal site in the Staples Mill retail corridor ("SMC"), a venerable 60-year-old big box and small shop shopping center located in an affluent suburb 8 miles west of Washington, DC. SMC has been an iconic destination since its opening, but in recent years has lost two of its four anchor tenants and experienced never-before-seen levels of vacancy. SMC sees the PP opportunity as a chance to positively alter the trajectory of its flagging property in a single transaction and hopes to replicate this model with PP at several other sites it owns up and down the East Coast. PP has a successful, but undersized store located only four miles from SMC and believes that relocating to SMC would immediately result in a net increase in annual revenue of 35%.

PP has proposed taking just over two acres of the shopping center requiring demolition of one of the vacated anchor buildings and several shop spaces located in between the two anchors, some of which are still in operation. This will require SMC to relocate several existing tenants and deliver to PP a pad-ready, re-zoned site subdivided from the remainder of the shopping center and consisting of a new separate tax parcel. SMC would be obligated to deliver the pad in accordance with detailed specifications on or before an outside date of 365 days to allow PP to commence and complete its TI construction in accordance with its expansion roll out schedule. PP's current lease for the location it will be relocating expires in 18 months, and it has no ability to extend its current lease beyond that date. The tenant improvements will include the convenience store building and all interior finishes, fuel pumps and other fueling station equipment, landscaping, lighting and other site work.

We will use the above hypothetical to illustrate and analyze the following issues related to construction in the landlord-tenant context.