ROUNDTABLE

WHAT MAKES RESTAURANT LEASING DIFFERENT THAN RETAIL LEASING?

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When negotiating restaurant leases there are a couple of concepts that do not typically appear in traditional retail leases, or have unique issues related to restaurants that should be contemplated.

Hours of Operations: Many restaurants operate later than those of a traditional retailer. In addition, restaurants not serving breakfast may not want to open prior to 10 AM or noon. Extended Holiday Hours During the holiday season, restaurants may not want to participate in days like "Black Friday" and other seasonal events because such early morning, seasonal events do not play a role in the tenant's use. Notwithstanding the foregoing, Tenant shall not be required to open and operate on federal or state holidays."

For late operating tenants, special concerns such as Common Area lighting, noise at late hours, and other safety concerns should be considered. The requirement to light the Common Areas for some period of time following the tenant's nightly closure is not typically controversial, but who pays for the extra lighting is a point of negotiation. The same goes for late night housekeeping and security. In addition to safety and security, if the late-night tenant is in an enclosed mall, then access to the Premises remains open within portions of the enclosed mall and parking areas is critical. Late night use of Patio Areas and Outdoor Operations is another concern for the parties, especially if the project is in a mixed-use development with a residential component.

Parking/Valet/Take Out/Delivery Service: Typically, the parking ratio at a center complies with applicable code requirements, and may also be subject to a more stringent parking ratio requirements set forth under an REA, each which may provide that only parking spaces available for nonexclusive use can be included toward satisfaction the parking requirements.

Short-Term Parking: Some restaurants will want dedicated spaces for take-out or pick-up parking. Tenants will want signs to specifically identify the tenant. Landlord concerns: If Landlord starts offering tenant-specific take-out parking to one tenant, then other tenants will want their own take-out spaces too. Tenant concerns: Much of its sales are carry-out orders. Tenant's customers will want to be able to park close to the store and get in and out within a few minutes. If they have to drive around the parking lot looking for an empty space, located further away from our store, they're more likely to opt for a competitor, especially one with a drive thru. Potential compromise: Offer to designate a couple of spaces as non-exclusive short-term parking. Note that Landlord will not want to enforce these areas.

Protected Parking: Tenant may request that a certain number of non-exclusive spaces be maintained in the proximity of the restaurant. The spaces will remain available on a non-exclusive basis for use by Tenant's customers (and customers of other tenants).

Valet Parking: Some restaurants, particularly white tablecloth or "sophisticated" restaurants, may require valet. Landlord may operate, or cause to be operated, a valet parking service at the center for the benefit of all customers of the center who elect to use it, normally for a fee. For Tenant operated valet, the tenant will want to (i) have the right to operate a valet, (ii) designate and protect parking spaces for the valet's use, and (iii) have the right to drop off and stacking locations, including the ability to put out a sign indicating such valet parking is available. Landlords need to verify a tenant operated valet is not prohibited by any of its other leases or any REA or Declaration.

Gross Sales: There are some examples of "sales" that restaurant tenants do not want when calculating percentage rent, such as tips or gratuities actually paid to tenant's employees and not retained by tenant, free or discounted employee meals, transactions where the patron left without paying, complementary meals offered for promotional purposes, delivery charges paid to third party providers (see below) without profit to Tenant. Landlords will want to limit these exclusions to not more than a certain amount or percentage of a tenant's aggregate gross sales. Catering or off-premises operations involving items prepared and served off-Premises, including all deposits for such off-Premises catering not refunded to purchasers are another point to be addressed. Catering sales from the Premises can be a point of contention for restaurants as these orders have less of a nexus to the Premises if they are being delivered off-site. Landlords will want to include sales from all takeout and delivery business generated from the Premises.

Third-Party Apps: The use of third-party delivery apps such as Uber Eats, Postmates and Door Dash has dramatically increased over the last few years. Pricing on these apps may not match the pricing offered by tenant within the restaurant. Additionally, the apps may divert orders to different restaurants without tenant control. The apps also charge fees, some of which are paid to the restaurant, some of which are paid to the app provider, and some of which are split between the app provider and the restaurant. Depending on the restaurant and its structure, these sales may or may not be counted as sales from the restaurant.

Alcohol Sales. If the tenant is obligated to pay percentage rent one must determine whether the state prohibits the inclusion of alcohol sales in gross sales for purposes of percentage rent, or if including such sales in gross sales makes the landlord a responsible party under the liquor law, or even require the landlord to be a party to the liquor license.

Exclusives: Restaurant tenants are by their very nature territorial. Exclusives are critical in determining the types of uses tenants can and cannot do in their leased space as well as defining what landlords cannot do (or allow others to do) in the rest of the shopping center. If there is an exclusive discussion, Landlords will endeavor to make the exclusive as specific as possible so that Landlord retains the ability to lease other spaces within the shopping center as freely as possible. A tenant will often want to prevent the landlord from leasing a space to another similar restaurant focusing on their same use. The landlord will be concerned that granting this exclusive would prevent other tenants from having similar items, even if ancillary to their primary menu.

PITFALL EXAMPLES: Coffee. The overall coffee exclusive granted to a national coffee chain might not apply to the major grocer, since landlord carved out major tenants from the exclusive. However, landlord might have a hard time attracting a mini-mart that is a part of gas station, and landlord might not be able to lease to any restaurant. Landlord might differentiate between beans, fresh-brewed, and bottled/canned coffee, and should pay attention to the right to allow restaurants in the center.

Pizza: A restaurant tenant may want to ensure it is the only pizza parlor in the center. However, a pizza exclusive could preclude an upscale Italian restaurant from selling artisanal pizza as one of many entrees. Some ways to maintain flexibility while providing tenant protection are landlord differentiating

by menu selections (e.g., more than 50% Italian entrees), table service, table clothes, average entrée price, average per person charge.

Donut: A donut store may want a donut or pastry exclusive but the landlord will need to account for: (i) A Mexican restaurant that wants to sell churros; (ii) The Chinese place selling dim sum pastries in the morning; (iii) A convenience store selling prepackages donuts and snack cakes; (iv) The caterer who bakes wedding cakes and holds tastings at the center.

Is a burrito a sandwich? In White City Shopping Center, LP v. PR Restaurants, LLC, 2006 WL 3292641 (Mass. Super. Ct. Oct. 31, 2006), Panera Bread had an exclusive on selling sandwiches and soups. The exclusive prohibited the operation of a bakery or restaurant reasonably expected to have annual sales of sandwiches greater than 10% of its total sales or primarily for the sale of high-quality coffees or teas, such as, but not limited to, Starbucks, Tea-Luxe, Pete's Coffee and Tea, and Finagle a Bagel. The lease did not definition "sandwich" and only listed several chain restaurants prohibited by the exclusive. Qdoba, a Mexican-themed fast food restaurant selling burritos, tacos, and quesadillas leased space at the shopping center, the landlord sought a declaratory judgment stating that the sale of those items did not violate Panera's exclusive. Panera sought a preliminary injunction to block Qdoba's operations. The Court denied Panera's motion and found the exclusive was not violated by Qdoba. The court stated that the ordinary meaning, undefined by the parties, was the dictionary definition of a sandwich: "two thin pieces of bread, usually buttered, with a thin layer (as of meat, cheese, or savory mixture) spread between them." (citing The New Webster Third International Dictionary, 2002). Burritos and tacos did not meet the requirements of this definition.

Nuisances/Noise/Odors: Nuisance is generally defined as an unreasonable or wrongful use of land that interferes with another's use and enjoyment of its land. At common law, nuisance law is divided into two torts: a public nuisance and a private nuisance. A private nuisance is a substantial invasion of another's interest in the use and enjoyment of its land. Private nuisances do not necessarily involve a physical trespass but still interfere with the reasonable use and enjoyment of one's property. A private nuisance can be categorized as either intentional nuisances or an unintentional nuisance. Situations that give rise to nuisance allegations involve interference with use of land from activities such as pollution, noise, orders, vibrations, excessive light, etc. Conversely, a public nuisance is one that unreasonably interferes with a common right that the general public shares. Circumstances that influence the issue of unreasonableness are: whether the conduct significantly interferes with public health, safety, peace, comfort, or convenience; whether the conduct is proscribed by statue or ordinance; whether the conduct is of a continuing nature or has produced a permanent or long-lasting effect. Examples of public nuisances include pollution of public waters, creation of public health hazards, drug activity, and storage of explosives. Noises: Courts have determined that certain noise sources are not a nuisance as a matter of law. For example, dogs barking, children frolicking, and the discordant sounds of music and outdoor summer life do not, as a matter of law, rise to the level of substantial and unreasonable interference with the plaintiffs' use of their own property. Odors: An unpleasant odor which is distinct from the background odor and identify a specific source causing the odor can be a nuisance provided the plaintiff can show its duration is long enough to substantially and unreasonably interfere with the use and enjoyment of land. Quiet enjoyment: Tenants are also generally entitled to

quietly have, hold and enjoy its leased Premises during the lease term. Most commercial leases contain a clear covenant of quiet enjoy, and in most states, there is an implied covenant of quiet enjoyment.

Patio Area: Landlords understand that some restaurants want to have a patio area, but landlords need to ensure the patio does not create issues for itself or other tenants or neighbors. Tenant perspective: One of the draws of the restaurant concept is space design which features roll-up garage doors that open to a patio area. This creates good energy for the space and center. As for Base Rent and extras, tenants often do not want to include the square footage of a patio area into the occupancy costs calculation, but all of the other lease obligations would apply (e.g., maintenance, insurance, indemnity obligations) to the Patio Area. The parties need to understand and establish rules related to the use of the Patio. For instance, tenants may want to keep the Patio open until close which could be after midnight, with live music (with uncensored lyrics), sports broadcasts, or large (and noise) gatherings. The Patio may host cigar nights (or weed nights depending on the jurisdiction). These may cause issues for surrounding tenants and neighboring properties, especially for office and residential tenants. The parties should check any operating agreement between the retail, office, and residential components as they may prohibits noise during business hours, and after a certain hour.

Liquor License: Many restaurant tenants serve alcohol. Landlords and tenants need to consider items, such as permits, licenses, and insurance, during lease negotiations. Tenants cannot be allowed to serve alcohol within a space prior to receiving permits and licenses to do so. Landlord will also want the tenant to maintain liquor liability insurance while serving alcohol. In some states a liquor license is treated as a commodity. If a landlord already owns a liquor license, which license can be sold to tenant and then later repurchased by landlord upon expiration of the lease, the parties should carefully outline the agreement in the lease or other writing. In other jurisdictions, liquor license may be issued directly from the governmental authority or purchased from an existing holder. License availability may be a concern as sometimes the total number of licenses is limited. Liquor licenses come is all shapes and sizes, some allow only beer and wine, some allows service of all alcohol and some allow carry-out.

Special Permits: In addition to liquor licenses, certain uses may have specific licenses and approvals which must be obtained to be able to operate, including licenses for games, assembly, valet parking, etc. Restaurant tenants may also want an exterior storefront or signage that may require governmental approval (and have REA implications). Restaurants developed on outparcels are subject to certain height restrictions, as well as restrictions on the size of signage and architectural features.

Franchise: Occasionally the Tenant will be a franchisee of a franchised concept. The Tenant/Franchisee will be required to include certain provisions in the Lease on behalf of the Franchisor. The Franchisor terms are typically either incorporated into the Lease itself or included as an Exhibit/Rider to the Lease. It is not unusual for the Franchisor terms to include, at a minimum, the following: (i) the ability for Franchisor to take over the Lease from Tenant (either unilaterally or in conjunction with Tenant), (ii) Landlord notice to Franchisor of any Tenant defaults and the ability for Franchisor to cure them, and (iii) the ability of Franchisor to "de-brand" the Premises at the end of the term.