

Thursday, October 27, 2022
2:15 PM – 3:30 PM

Seminar #16

**ICSC's New Model Retail Lease; Staying Current with the New Reality:
The Threshold Moment has arrived.**

Presented to

2022 ICSC+U.S. LAW
JW Marriott Grande Lakes, Orlando, Florida
October 26-28, 2022

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The following materials have been prepared in conjunction with the presentation by the speakers at this seminar.

Introduction

As a consequence of the proliferation of e-commerce sales, technological advances in the tracking and reporting of sales of goods and the impact of the COVID-19 pandemic on retailing, landlords and tenants have had to rethink their brick and mortar leases. In 2020, a panel of distinguished ICSC leasing professionals formed a task force for the purposes of reviewing and updating the existing retail model lease that had been drafted in the past.

This seminar will focus on some of the important provisions found in the new ICSC retail model lease that was developed by a team of legal and leasing experts, including changes in the formula for gross sales and percentage rent calculations, operating expenses clauses including caps and exclusions, radius restriction clauses, maintenance and repair obligations, and force majeure clauses and their impact on continuous operating requirements and rent abatement in light of the COVID-19 pandemic.

I. Percentage Rent Clauses

- a. **Gross Sales Definition** - From a landlord's perspective, the definition of gross sales should be as expansive as possible. On the contrary, tenants seek to narrow the definition of gross sales to minimize the effect of the percentage rental provisions.

If the tenant achieves a certain volume of Gross Sales in a given period (commonly referred to as the "Breakpoint"), then the tenant will pay the landlord, as additional rent, a percentage of gross sales that

exceeds the Breakpoint. For example, if Gross Sales during a year exceeded \$3 million, then the tenant might be obligated to pay 7% of the excess amount as percentage rent.

The following is a typical gross sales provision found in retail marketplaces (shopping center) leases:

The term "Gross Sales" as used herein shall be construed to include the entire amount of the sales price, whether for cash, credit, trade-ins or otherwise, of all sales and leases of merchandise (including gift and merchandise certificates), food, beverages, services and other receipts whatsoever of all business conducted at, in or from the Demised Premises, including, without limitation, orders (whether by mail or telephone or by electronic or other means of communication) taken, received or filled at the Demised Premises, deposits not refunded to purchasers, orders taken or received, although said orders may be filled elsewhere, catalogue sales, sales to employees, sales through vending machines or other devices, sales by any sublessee, concessionaire or licensee or otherwise in said premises, and insurance proceeds and/or condemnation awards received for loss of sales, profits or business. Each sale upon installment or credit shall be treated as a sale for the full price in the month during which such sale is made, irrespective of the time when Tenant shall receive payment from its customer. Each lease shall be treated as a sale in the month during which such lease is made in an amount equal to the total rent or other consideration payable during the term thereof, irrespective of the time when Tenant shall receive payment from its customer. No deduction shall be allowed for uncollected or uncollectible credit accounts. Notwithstanding the foregoing, however, Gross Sales shall not include (and there shall be deducted from Gross Sales only to the extent previously included in Gross Sales) the following: (Items below to be negotiated on a lease by lease basis)

- i. any sums collected and paid out for any sales, use, luxury or excise tax imposed by any duly constituted governmental authority where the amount of such tax is separately charged to the customer and paid directly by Tenant to the taxing authority,
- ii. the exchange of merchandise between the stores of Tenant or transfers to a warehouse, if any, where such exchanges or transfers of goods or merchandise are made solely for the convenient operation of the business of Tenant and not for the purpose of consummating a sale which has theretofore been made at, in or from the Demised Premises and/or for the purpose of depriving Landlord of the benefit of a sale which otherwise would be made at, in or from the Demised Premises,
- iii. the amount of returns to shippers, wholesalers or manufacturers, for credit,
- iv. the amount of any cash or credit refund made upon any sale previously reported from the Demised Premises where the merchandise sold, or some part thereof, is thereafter returned by purchaser and accepted by Tenant,
- v. sales of Tenant's fixtures and equipment which are not part of Tenant's stock in trade and where such sales are not in the ordinary course of business,
- vi. bona fide sales, at a discount off the regular retail price, to Tenant's store employees or employees of Tenant's affiliated companies to the extent that such sales do not exceed, in any calendar year, two percent (2%) of Gross Sales (excluding such sales) for such calendar year,
- vii. bad debts on credit sales, bad checks and credit card charges on sales previously included in Gross Sales which are uncollectible accounts to the extent that the same do not exceed, in any calendar year, two percent (2%) of Gross Sales for such calendar year (excluding such accounts) subject however to inclusion in Gross Sales if such accounts are subsequently collected,
- viii. bona fide service or sales carrying charges charged by Tenant to its customers for the extension of credit on the sale of merchandise from the Demised

Premises if Tenant in billing its customers itemizes such charges separately from the cash purchase price of the merchandise sold,

ix. bulk sales of obsolete, discontinued or damaged merchandise to non-consumer purchasers,

x. receipts from public telephones, stamp machines or vending machines installed in non-sales areas of the Demised Premises for the exclusive use of Tenant's employees,

xi. charges for gift wrapping, check cashing, repairs and alterations, delivery charges and similar minor auxiliary services rendered at no gross profit, where such charges are separately stated from the purchase price of the merchandise sold and to the extent that the aggregate of such excluded charges does not exceed, in any calendar year, one percent (1%) of Gross Sales (excluding such items) for such calendar year,

xii. internet or mail order sales or sales from Tenant's catalog where the order for any such sale is not placed at the Demised Premises nor filled nor picked up from the Demised Premises, and

xiii. sums received as partial payment for merchandise sold upon the "lay-away" or "will call" basis, provided all receipts and revenue in respect of such "lay-away" or "will call" sales shall be included in Gross Sales upon the first to occur of the date the applicable merchandise is delivered to or otherwise received by the customer, or the date any such "lay-away" or "will call" sale is abandoned and the deposit and any other sums received on account thereof are forfeited to Tenant, or one year after the initiation of any such "lay-away" or "will call" sale.

Notwithstanding anything to the contrary set forth above in this Section, the amount of any gift card or merchandise certificate shall be included in Gross Sales only if and to the extent such cards or certificates are redeemed (except to the extent otherwise excludible from Gross Sales under this lease), so long as such certificates are similarly treated in all other stores under common ownership and control with Tenant's store in the Demised Premises.

From a tenant's standpoint, what is missing from the first sentence of the above definition is the limiting language that gross sales will only include the sales price actually received. As a result, this may allow the landlord to include the amount of all sales (whether or not money is actually received by tenant) in the calculation of gross sales which is then subject to percentage rent.

b. **Exclusions vs. Deductions.** It is important to correctly categorize a transaction description as an exclusion or a deduction. Exclusions are revenue items that are never even included in the tenant's calculation of gross sales. On the other hand, deductions are subtracted from total gross sales after having been initially included in gross sales.

Common exclusions from "Gross Sales" are:

Exchanges of merchandise between stores of tenant.

Returns of goods or merchandise to shippers or manufacturers.

Exchanges of merchandise by customers, but only to the extent of the value of the merchandise returned for exchange.

Amounts received from claims for loss or damage to merchandise.

Sales of tenant's furniture, fixtures and equipment.

The amount of sales taxes or any excise or other tax collected by tenant from customers and paid by tenant to any governmental agency. (It should be noted that if the sales price already includes the amount of such tax, the amount of the tax that was included in the sales price would instead be

considered a deduction and therefore subtracted from gross sales).

The amount of sales to only store employees. (Landlords will often include a provision stating that discounts to only store employees may be excluded to the extent the discounts do not exceed a certain percentage of the gross sales, with 1% - 3% of gross sales being a common range for such cap).

Insurance and condemnation proceeds.

Bulk sales not in the ordinary course of business.

The sale, transfer, or exchange of the entire business of tenant.

Rent paid to tenant by a subtenant, licensee or concessionaire, provided, however, any sales by such subtenant, licensee or concessionaire at the Premises should be included in the gross sales calculation).

Delivery and shipping charges to customers paid in connection with a sale, provided Tenant receives no gross profit therefrom.

Interest, finance and carrying charges on a credit sales transactions, provided, however, said exclusion shall not exceed one percent (1%) of Gross Sales per annum.

Receipts from vending machines installed solely for the use of tenant's employees

Tips or gratuities actually paid to employees and not retained by tenant.

Sales of promotional items at cost.

Common deductions from "Gross Sales":

- The amount of any actual refunds or credits made by tenant to a customer or purchaser for returned merchandise, the sale of which was previously included in gross sales of the store.
- The amount of any sales, luxury or excise tax on sales which is both added to the selling price and paid directly to the taxing authority by tenant.
- Bad debts, provided however, in the event the amount of bad debt is later collected, the amount shall be added to Gross Sales for the lease year in which such bad debt is collected.
- Credit card fees and fees paid by tenant to banks in connection with acceptance of customers' ATM, debit cards, e-Wallets, loyalty payments, mobile payments, etc. (What used to be "credit card fees" should be broadened to include all merchant fees and fees charged by payment processors or card issuers. PayPal, Square, SMS (Short Message Service) and Apple Pay are payment processors because a debit/credit card/bank account on file with them is the source of the payment. PayPal issues its own consumer credit products, too)

From a landlord's perspective, the lease should state that, other than sales tax included in the sales price, taxes imposed on the tenant (e.g., franchise tax, capital stock tax, income tax or tax based upon tenant's income, capital structure, or profits) are not deductions from gross sales.

c. Omni-Channel Hot Button Issues:

Below is the current definition of the what cutting-edge omnichannel retail is, according to Total Retail's 2018 Top 100 Omnichannel Retailers. During the first quarter of 2018, Total Retail measured publicly traded retail companies and judged them on the following seven omnichannel criteria (© 2018 NAPCO Media, <https://www.mytotalretail.com/resource/total-retails-2018-top-100-omnichannel-retailers>):

1. does it offer buy online, pick up in-store (**BOPIS**)
2. does it offer the ability to search for in-store products on its website, including access to stock availability;

3. does it offer a shared cart across channels (e.g., mobile to desktop);
4. can loyalty points be earned and redeemed across channels;
5. can products be returned across channels (e.g., return online purchases in-store);
6. does it offer five or more channels for customers to engage customer service staff; and
7. is product pricing consistent across channels.

Real estate professionals and their attorneys must engage in the discussion of each element of the retail transaction. What customer interactions with the physical store location will result in a transaction being included in gross sales? What customer interactions with the physical store location will result in a transaction not being included? A transaction being excluded? Inclusion language should be as broad as possible and not limited in scope based on the current tenant's business model. Services and experiences are under constant consideration by apparel retailers. Food & beverage tenants are offering delivery and order-online-for-carryout. Grocery tenants are offering click-and-collect and meal subscription services. Even some service providers are agreeing to report Sales to landlords. For example, medical services, like urgent care centers, eye care / vision centers and dental. For other professional services sales reporting is still uncommon, but it can happen.

d. **Lease Requirements** (Registration, Recording, Reporting, Record Keeping) and Audit Rights

- i. **Record Keeping & Auditing:** (Three (3) year retention and maintenance of records from end of each lease year. Right to audit for a three (3) year period.

(1) Basic records. The tenant are customarily obligated to keep basic financial records relating to the location's performance for a period of three lease years. These include:

- POS transactional level data
- POS Summary reports (day/week/month)
- Monthly sales summary reports (Sales Journal, General Ledger)
- Bank Statements including deposit slips
- Chart of accounts
- Revenue line items from a store operating statement
- Sales tax report at store level. Taxable and non-taxable transactions in certain states have different components. Varies by jurisdictions.
- Federal income tax returns (Independent, local, franchisee, etc.)

(2) Worksheet for the individual location for the time period covered showing the formula utilized and the Gross Sales calculations in accordance with the formula.

(3) Supporting documents, when requested, can include merchant statements or GL entries showing the deductions or exclusions to trace actual values.

- ii. **Audit Rights.** Elements to be negotiated may include:

1. Specific information or reporting detail around returns and internet transactions detail, where available.
2. Specific enforcement or escalation remedies if tenant is chronically failing to report or respond to support requests.
3. Look back period from the end of a lease year

ICSC Model Retail Lease Provisions for Percentage Rent

SECTION 3.02. Percentage Rent.

From and after the Rent Commencement Date, and in addition to Fixed Minimum Rent payable by Tenant hereunder, Tenant shall pay Percentage Rent to Landlord. Percentage Rent shall be payable monthly in arrears

in the first calendar month in which the Gross Sales of Tenant exceed the Percentage Rent Breakpoint for such Lease Year, and thereafter within fifteen (15) days after the end of each calendar month during such Lease Year. On or before the tenth (10th) day of each calendar month during the Term hereof, Tenant shall furnish Landlord with a written statement certified by Tenant to be correct showing the amount of Gross Sales for the Premises from the beginning of the Lease Year to the end of the previous calendar month or portion thereof. For purposes of this Lease, the "Percentage Rent Breakpoint" for each Lease Year shall be determined by dividing the annual Fixed Minimum Rent for such Lease Year by the Percentage Rent Rate. At the end of each Lease Year, adjustments for any overpayment or underpayment made during such Lease Year shall be made as set forth in this Section 3.02. If Fixed Minimum Rent during any Lease Year is reduced pursuant to a provision in this Lease or by express written agreement between Landlord and Tenant, then the Percentage Rent Breakpoint and Monthly Breakpoint, as may be applicable, shall likewise be reduced by a percentage equal to the percentage decrease in the Fixed Minimum Rent payable for the period during which the change in Fixed Minimum Rent is in effect. The Percentage Rent Breakpoint for each Lease Year shall be determined by dividing the annual Fixed Minimum Rent due for such Lease Year by the Percentage Rent Rate.

SECTION 3.03. Gross Sales Defined.

(a) *The term "Gross Sales" as used herein shall mean the aggregate dollar amount of gross sales, income, receipts, revenues, membership fees, charges, monies or other things of value received and accepted by Tenant, of, in connection with and for all merchandise, services or other operations or business sold, leased, licensed or rendered at, in, on, from or arising or attributed to the Premises by Tenant or any subtenants, concessionaire or licensees, whether at retail or wholesale, and whether evidenced by cash, check, coupon, credit card, charge account, debit card, cryptocurrency, exchange or otherwise and regardless of the amount, or profit realized. Gross Sales shall include, without limitation, the amounts received from the sale of goods, wares and merchandise, whether such sales be made by means of merchandise, vending devices, coin operated machines, electronic games or devices, rentals and for services performed in, on or from the Premises, including without limitation, all display fees, slotting allowances, promotional considerations, rebates or other payments received by Tenant to stock, promote or advertise any product, the amount of all orders taken, received, including mail, catalog, telephone, telegraph, electronic communication (including without limitation orders received through the internet), video, computer, cell phone, smart phone, iPad, tablets, mobile technology, or other technology-based system whether existing now or developed in the future, that are taken at or made from the Premises or other orders received at the Premises, whether such orders are picked-up or filled from the Premises or elsewhere which Tenant in the normal and customary course of its operations would credit or attribute to its business upon the Premises, or any part or parts thereof, as well as any business interruption or loss of income insurance proceeds attributable to lost sales revenue received by Tenant. All sales originating at the Premises shall be considered made and completed from the Premises even though bookkeeping or payment of the account is transferred to another location for collection or filling of the order and actual delivery of the merchandise is made from another location. Gross Sales shall also include all (i) deposits not refunded to purchasers and all service charges for layaway sales; (ii) lottery ticket sales or other tickets sold by Tenant for the full amount of the ticket price, but not the commission income earned by Tenant, and (iii) all moneys or other things of value received by Tenant from its operations at, in, on or from the Premises which are not expressly excluded from gross sales by the other provisions of this definition.*

(b) *Notwithstanding the foregoing provisions, for purposes of calculating Percentage Rent only, the following amounts shall be expressly excluded (or to the extent applicable and included or previously included or includable in Gross Sales, deducted) from the definition of Gross Sales: (i) Cash or credit refunds made upon transactions included within gross sales, not exceeding the selling price of merchandise returned by the purchaser and accepted by Tenant which were previously reported to Landlord, (except that Tenant shall not deduct from Gross Sales any refund credit for merchandise returned by customers who did not originally purchase the merchandise from an actual brick and mortar retail location, including, but not limited to, refund credits for sales that originated from catalog, mail order, internet sales or electronic communication); (ii) Sales taxes, excise taxes or gross receipts taxes imposed by the government upon the sale of merchandise or services, but only if collected from customers separately from the selling price and paid directly by Tenant to the taxing authority; and (iii) sales of gift certificates ("Gift Cards") at the Premises until they are redeemed for merchandise, provided, however, Gift Cards purchased elsewhere and redeemed at the Premises shall be included in Gross Sales and the amount of any discount on sales to employees of the Premises (hereinafter "Exclusions from Gross Sales"). Tenant agrees to provide Landlord with complete, accurate and separate records as to those items that constitute Exclusions from Gross Sales.*

II. Operating Expense Clauses

a. Definition of Common Area Costs - In addition to the payment of fixed rent, most shopping center leases include a requirement that the tenant pay its fair share of the expenses incurred by the landlord in maintaining the "Common Areas" of the center ("Common Area Costs" or "Operating Costs"). The definition of Common Areas generally means those areas of the shopping center, as they may exist from time to time, which are exclusive of gross leasable area as well as other areas which are set aside as the exclusive use of the landlord. These areas include, without limitation, the parking areas, roadways, pedestrian sidewalks, roofs, loading docks, delivery areas, landscaped areas, and all other areas or improvements which may be provided by landlords for the general use of tenants of the shopping center and their agents, employees, and customers whether within or without the shopping center.

b. Inclusions/Exclusions - The battle ground between landlords and tenants is what constitutes "Common Area Costs" under the Lease. Landlords want as broad a definition as possible. Tenant try to narrow that definition so that its obligation to pay Common Area Costs does not become a profit center for the landlord.

A typical landlord-oriented Operating Costs definition might be as follows:

"Operating Costs" shall mean all costs and expenses incurred by Landlord in connection with ownership, maintenance, operation, repair, replacement, protection, policing, managing, equipping, lighting, painting, water, sewage, landscaping, grading, resurfacing, striping, exterminating, inspecting, insuring and cleaning the Common Areas and all other portions of the Center which may be incurred by Landlord in its discretion, including without limitation all on or off-site facilities and utilities currently existing or hereinafter constructed serving the Center or required to be maintained with the operation of the Center, and all costs and expenses relating to: (a) parking areas (whether on-site or off-site), sidewalks and utility facilities; (b) insurance, including without limitation, property insurance, liability insurance, workers compensation insurance, rent loss insurance and all other types of insurance carried by Landlord from time to time, in its sole discretion, including costs of deductibles or self-insured retentions; (c) water and sewer facilities; (d) storm water drainage; (e) marketing costs and expenses; (f) property owners association or similar types of associations; (g) lighting; (h) air conditioning, heating, fire protection and ventilation of the Common Areas, facilities and equipment, (i) trash removal, trash compactors (if subsequently installed); (j) security, if any; (k) utilities; (l) roof maintenance, repair and replacement for improvements and buildings at or on the Center; (m) reasonable reserves; (n) holiday or seasonal decorations; (o) snow and ice removal; (p) marketing costs and expenses; (q) pest control; (r) landscaping, sprinkler and irrigation systems; (s) rental expenses and depreciation applicable to owned equipment or machinery used in maintenance or operation of the Shopping Center; (t) taxes, fees or assessments applicable to any pylons, signage, equipment or other facilities; (u) Center signage, including without limitation, related electricity costs; and (v) salaries, insurance, unemployment and social security taxes for personnel managing, maintaining, operating or providing services for or relating to the Center and (w) administrative fee in the amount of fifteen percent (15%) of the total Operating Costs.

Tenants may want to expressly exclude the following from the definition of Operating Costs to limit their liability:

- Costs or expenses of leasehold improvements, leasing commissions, lease negotiations, advertising, brokerage commissions, architectural or engineering services;
- Costs or expenses related to any leasable area in the shopping center, including without limitation, relating to any maintenance or repair, renovations, remodeling or costs incurred in obtaining new tenants or keeping existing tenants;
- Capital expenditures;
- The cost of, or any related amortization or depreciation of acquiring, constructing, remodeling, refurbishing or expanding the Center or any portion thereof, including without limitation buildings, improvements, common areas, parking areas or any related facilities or services;
- Costs or expenses payable by any tenants or occupants directly to third parties;
- Any excess premiums for insurance coverage arising or resulting from extra-hazardous activities of any tenant or occupant of the Center, or their agents, employees or contractors, other than Tenant;

- Costs or expenses arising from the failure by the Landlord to timely pay bills or other obligations, including without limitation, any late charges, penalties or interest relating thereto, except to the extent arising from default of Tenant;
- Except for the payment of Taxes due under the Lease, all other governmental charges, taxes, assessments of any kind or any income taxes;
- Costs or expenses arising from any bad debt of Landlord;
- Reserves of any kind or nature;
- Costs or expenses relating to any loan, lien or mortgage encumbering all or any portion of the ng Center;
- Costs or expenses of compliance with any court orders, judgments, court decrees, governmental laws, rules, regulations, codes or other governmental requirements, including without limitation, "The Americans with Disabilities Act;"
- Costs of clean-up, removal, testing, monitoring, abatement or other remediation of any Hazardous Substances located on or about the Center;
- Any amounts reimbursable by eminent domain proceeds or settlements, insurance proceeds or settlements;
- Costs or fees relating to any merchants' associations or similar types of associations;
- Salaries or benefits of any employees or officers of Landlord of higher rank than manager of the Shopping Center, or the costs of employees not located on-site or overhead expenses not directly related to the Center;
- Any costs or expenses arising from violations by Landlord or any other party other than Tenant of any governmental ordinance, law, rule, regulation or requirement, including without limitation, any penalties, fees, interest or fines arising from such violation(s);
- Costs, rent or other payment amounts due or arising under any ground lease, master lease or sale/leaseback transaction;
- Costs or expenses arising from or related to any audits except to the extent incurred in connection with generation of Operating Costs statements;
- Costs or expenses arising as a result of improper or faulty construction, defective workmanship, defective components or equipment, design defects, or latent defects, including any maintenance, repairs or replacements relating thereto;
- Costs of insurance for liability or personal property covering or insuring any leasable space, other than the Premises, whether or not such leasable space is occupied;
- Costs or expenses of enforcing, amending, terminating or extending any leases or occupancy agreements, or any obligations of any tenants or occupants under leases or occupancy agreements, including without limitation, attorneys' fees or court costs relating thereto; and
- Management fees, administrative charges, or similar charges.

c. Tenant's Proportionate Share - From the landlord's perspective "Tenant's Proportionate Share" normally means a fraction, the numerator of which is the gross leasable area of the premises and the denominator of which is the gross leasable area of the shopping center which is occupied and open for business from time to time, in each case as reasonably determined by the landlord. Some landlords require a provision in the lease that in no event will the percentage of gross leasable area to be used in the denominator be less than

eighty percent (80%) of the gross leasable area of the shopping center. In addition, landlords often exclude the gross leasable area of anchor stores such as big box stores having gross leasable areas in excess of 25,000 square feet from the denominator. Tenants should be careful in negotiating the definition of Tenant's Proportionate Share to include the largest denominator possible, regardless of occupancy levels at the Shopping Center or leases to anchor tenants.

d. Annual Caps on Increases - It is highly desirable from a Tenants standpoint to obtain a cap on the annual increases of Operating Costs which will allow a tenant the ability to better quantify its annual leasing costs. Additionally, a cap serves to encourage landlords to keep the Common Area Costs below the cap, since landlord will absorb Common Area Costs exceeding the applicable cap. Caps can take several forms but are generally either (i) noncumulative or (ii) cumulative.

- i. Non-Cumulative Caps.* A noncumulative cap provides that the annual amount the tenant is required to pay for Operating Costs will not exceed a certain percentage, e.g. 5%, of the amount paid by the tenant for the immediately prior Lease Year. By way of example, Tenant's Proportionate Share of Operating Costs for any Lease Year following the first full Lease Year of the Term shall not exceed one hundred five percent (105%), on a non-cumulative basis, of Tenant's Proportionate Share of Operating Costs payable by Tenant for the immediately prior Lease Year.
- ii. Cumulative Caps.* A cumulative cap allows the landlord to recapture amounts of the Operating Costs incurred for an applicable year, and if such amount does not reach the percentage capped amount, then the landlord can recover the amount by which the Operating Costs exceeded the required capped amount for prior years, up to the percentage capped amount for the applicable year. If Operating Costs only increased by 4% in the current year, with a 5% cap, the landlord can increase the Operating Costs to 5% in order to recapture up to 1% overage from prior years. By way of example, Tenant's Proportionate Share of Operating Costs for any Lease Year following the first full Lease Year of the Term shall not exceed one hundred five percent (105%), on a cumulative basis, of Tenant's Proportionate Share of Operating Costs payable by Tenant for the immediately prior Lease Year.

e. Audit Rights - Unless Operating Costs are fixed, tenants should obtain the right to audit the landlord's books and records to confirm that the Common Area Costs being passed through are costs permitted under the terms of the applicable lease. Most Landlord form leases typically omit this provision in its entirety. Consequently, the tenant has no right to audit unless the tenant expressly requests and obtains an audit right during lease negotiations. Landlords often take the position that there will be no audit rights for tenants who lease small portions of the total square footage of the shopping center and grant audit rights to tenants who lease larger spaces and possess stronger bargaining power.

ICSC Model Retail Lease Provisions for Operating Expenses

SECTION 4.01 Operating Costs

(a) During each month of the Lease Term, Tenant shall pay to Landlord, along with the monthly installment of Fixed Minimum Rent, without demand, deduction or setoff, as Additional Rent, Tenant's Proportionate Share, as such term is defined herein, of Landlord's total costs (including appropriate reserves) for operating, managing, administering, maintaining, repairing, replacing or improving the portions of the Shopping Center that are the responsibility of Landlord hereunder and Landlord's total costs for all insurance covering the Shopping Center, the cost of all deductibles paid by Landlord, and Landlord's cost for furnishing heating, ventilating and air-conditioning in connection with all or any part of the Shopping Center (collectively "Operating Costs"). Operating Costs shall include, but not be limited to, the following costs of Landlord: (i) premiums for insurance policies whether under master or blanket policies or separate policies, unless paid pursuant to Article IX, including commercial general liability insurance personal injury and property damage; all risk (special form) insurance; business interruption insurance; workers' compensation insurance; and fidelity bonds for personnel; (ii) lighting, (iii) cleaning, (iv) snow and ice removal, (v) landscaping and paving, (vi) painting, (vii) policing and providing security (if Landlord shall so elect), (viii) fire protection, (ix) drainage, (x) heating, ventilating, and air-conditioning; (xi) depreciation of machinery and equipment used in connection with the Shopping Center and the maintenance thereof, (xii) repairs, maintenance and replacement of the roof of the enclosed mall and the

enclosed mall building, and other portions of the Shopping Center, (xiii) the maintenance and operation of the sprinkler system installed in the Shopping Center; (xiv) costs incurred in complying with applicable governmental laws, ordinances, rules and regulations together with Landlord's expenses in determining the amount of any charges or assessments levied on the Shopping Center; and (xv) all on-site costs and personnel expenses incurred by Landlord in managing the Shopping Center (including all contributions and payments required to be paid by the employer and all fringe benefits) plus an amount for administration equal to fifteen percent (15%) of the total of all Operating Costs.

(b) The net amount of Operating Costs paid to Landlord by any "Anchor Stores" (defined for purposes of this Lease as stores occupying..... square feet or more of the Gross Leasable Area of the Shopping Center, as such term is defined herein) or tenants of freestanding buildings in the Shopping Center shall be deducted from Operating Costs prior to computing Tenant's Proportionate Share of Operating Costs (collectively "Operating Cost Deductions"). Tenant's Proportionate Share of Operating Costs, as adjusted for Operating Cost Deductions, shall be computed by multiplying Operating Costs by Tenant's Proportionate Share, as such term is defined herein. Tenant shall pay Tenant's Proportionate Share of Operating Costs monthly in advance based on estimates ("Estimated Operating Costs") made by Landlord from time to time. Estimated Operating Costs shall be revised annually on the basis of actual Operating Costs for the preceding calendar year of operations. Should Estimated Operating Costs be underestimated, Tenant shall pay any deficiency together with the payment of the next installment of Fixed Minimum Rent and, thereafter, shall pay Tenant's Proportionate Share of Operating Costs, as adjusted, in equal monthly installments as herein provided. Any excess payments of Estimated Operating Costs shall be credited against the payment of Operating Costs next due and owing hereunder. The Tenant shall have the right during regular business hours to audit and otherwise examine Landlord's books and records related to Tenant's Proportionate Share of Operating Costs charged pursuant to this Section 4.01.

(c) For the purposes of this Lease the terms (i) "Gross Leasable Area" shall mean the area computed by measurements of the ground floor (and any additional floor or mezzanine if and to the extent used for the display or sale of retail goods) made to and from the center of party walls and the outside of exterior walls (but not including therein any decorative facade, fascia or architectural treatment, or any overhang such as canopies or non-occupiable extensions of the building or extensions to the loading dock receiving area), plus the area of any exterior portion of the Shopping Center that is subject to the exclusive use of any tenant or group of tenants for the sale or display of merchandise but excluding any exterior loading docks, loading zones or delivery areas, exterior trash enclosures or pallet area, exterior utility rooms and exterior vestibules that are not used for the sale or storage of retail goods; (ii) "Gross Leasable Area of the Shopping Center" shall mean shall mean the area computed by measurements of the ground floor (and any additional floor or mezzanine if and to the extent used for the display or sale of retail goods) made to and from the center of party walls and the outside of exterior walls (but not including therein any decorative facade, fascia or architectural treatment, or any overhang such as canopies or non-usable extensions of the building or extensions to the loading dock receiving area), plus the area of any exterior portion of the Shopping Center which is subject to the exclusive use of any tenant or group of tenants for the sale or display of merchandise but excluding any exterior loading docks, loading zones or delivery areas, exterior trash enclosures or pallet area, exterior utility rooms and exterior vestibules which are not used for the sale or storage of retail goods, and (iii) "Tenant's Proportionate Share" shall mean a fraction, the numerator of which shall be the number of square feet of floor area of the Premises and the denominator of which shall be the number of square feet of Gross Leasable Area of the Shopping Center.

[Alternative Provision Where Fixed Operating Charge is Used]

SECTION 4.01. Fixed Operating Charge.

Landlord will operate, manage, maintain and repair or cause to be operated, managed, maintained or repaired the Shopping Center. In consideration of Landlord's operation, management, maintenance and repair of the Shopping Center as provided herein, Tenant shall pay to Landlord the Fixed Operating Charge for and with respect to each and every calendar year during the term of this Lease (prorated for any partial calendar year), in equal monthly installments due and payable in advance on the first day of each and every month during the Term of this Lease commencing with the Rent Commencement Date. Tenant acknowledges and agrees that, because the Fixed Operating Charge is an amount agreed to by the parties, Tenant shall have no right to audit Landlord's books and records concerning the Fixed Operating Charge. The "Fixed Operating Charge" for the calendar year 20__ (the

"Base Year") shall be: _____ Dollars (\$____) per square foot of Gross Leasable Area per annum (computed on an annualized basis for any partial calendar year), subject to adjustment as set forth herein. For and with respect to each and every calendar year or partial calendar year after the Base Year, the annual Fixed Operating Charge shall be increased on the first day of each such calendar year or partial calendar year by an annual amount equal to ____ percent (____%) of the Fixed Operating Charge in effect hereunder for the immediately preceding calendar year (computed on an annualized basis for any partial calendar year). The term "Gross Leasable Area" shall mean the area computed by measurements of the ground floor (and any additional floor or mezzanine if and to the extent used for the display or sale of retail goods) made to and from the center of party walls and the outside of exterior walls (but not including therein any decorative facade, fascia or architectural treatment, or any overhang such as canopies or non-usable extensions of the building or extensions to the loading dock receiving area), plus the area of any exterior portion of the Shopping Center which is subject to the exclusive use of any tenant or group of tenants for the sale or display of merchandise but excluding any exterior loading docks, loading zones or delivery areas, exterior trash enclosures or pallet area, exterior utility rooms and exterior vestibules which are not used for the sale or storage of retail goods.

III Radius Restrictions

a. **When should they be used in a lease** - Retail leases often include radius restriction clauses that prohibit a tenant from opening and/or operating a similar business within a certain radius of the retail store premises in an effort to protect the landlord's percentage rental income generated by the tenant. The logic is that if a tenant opens a competing store within a certain distance of the store premises, customers may end up shopping at the other store instead of at the store premises thereby reducing the amount of gross sales generated at the store premises and landlord's percentage rent payments. Radius restriction clauses may constitute a restraint of trade, unless properly drafted. The language must be carefully crafted and the restriction should be reasonable in terms of the distance of the radius restriction and scope. A well-draft clause should also properly address use clause issues, trade name issues, percentage rent issues, sales of the store or the chain to a competitor, and continuous operation clause issues. A 20 mile radius restriction in a suburban area in North Dakota may not be viewed in the same way by courts as a 20 mile radius restriction in the densely populated New York City metropolitan area.

b. **Inclusion in Gross Sales** - If the tenant violates the radius restriction clause, then the gross sales generated at tenant's violating store is included in the definition of gross sales in the percentage rent provision of the lease. By way of example, if the percentage rent rate under tenant's lease is 10% and the tenant has gross sales of \$1,500,000 at its store and its violating store located within the radius restriction area generates \$1,000,000 of gross sales, tenant would be liable to its landlord for the payment of \$150,000 in percentage rent at its store and \$100,000 in percentage rent at its violating store located within the radius restriction area. In addition, some landlords have made a violation of the radius restriction clause a lease default which could lead to the termination of the lease. Therefore, tenants must use the utmost care in making sure that the radius restriction language contained in their lease includes the requisite carve-outs and exclusions to avoid unintended financial consequences and possible lease termination.

c. **Carve outs and exclusions** - To effectively impose and enforce these restrictions, landlords must understand that tenants which operate more than a single concept, or under different trade names and/or offer different merchandise in their other concepts, will typically insist that their other stores are excluded from the radius restriction. Tenants faced with a radius restriction should try to achieve the following: minimize the restriction's physical scope, exclude from the restriction Tenant's existing stores within the radius, limit the restriction to a certain brand name or set of products if Tenant has multiple brands or product lines, and ensure that these restrictions shall not apply to a leasehold mortgagee who comes into possession of the leased premises, to ensure the financeability of the lease. Tenant's should also exclude sales made by Tenant or its affiliates of the same brand name product at wholesale or to department stores selling such brand name product in the restricted area. This is very important since a poorly drafted radius restriction clause could inadvertently result in sales at wholesale or to department store located with the restricted area being included in the landlord's calculation of gross sales and percentage rent at tenant's store location within the center.

Sample Radius Restriction Provision

If during the Lease Term Tenant directly or indirectly operates, manages or has any ownership interest whatsoever in any other retail store with a similar or competing business as the business

conducted by Tenant at the Premises (hereinafter collectively referred to as a "Competing Store") within ten (10) miles of the boundary line of the Center (the "Restricted Area"), it will injure Landlord's ability and right to receive Percentage Rent (such ability and right being a major consideration for this Lease and the construction of the Center). Accordingly, if Tenant operates, manages or has an ownership interest in any such Competing Store within such Restricted Area (a "Radius Violation"), then one hundred percent (100%) of all sales made from any such other Competing Store shall be included in the computation of Gross Sales for the purpose of determining Percentage Rent under this Lease as though said Gross Sales had actually been made at, in or from the Premises. Landlord shall have all rights of inspection of books and records with respect to such stores or businesses as it has with respect to the Premises; and Tenant shall furnish to Landlord such reports with respect to Gross Sales from such other store or business as it is herein required to furnish with respect to the Premises. Notwithstanding anything contained herein to the contrary, this Section shall not apply to and there shall be no Radius Violation with respect to sales of X branded products made by Tenant or its Affiliates (as such term is defined herein), at wholesale or to department stores selling X branded products in the Restricted Area. For the purposes of this Section, an "Affiliate" shall mean a person or entity which directly or indirectly controls or is controlled by Tenant or is under common control with Tenant.

ICSC Model Retail Lease Provisions for Radius Restrictions

SECTION 2.08. Trade Name, Use and Operation.

Tenant hereby acknowledges that Tenant's business reputation, intended use of the Premises, potential for payment of Percentage Rent and ability to generate customer traffic to the Premises and the Shopping Center were all relied upon by Landlord and served as significant and material inducements contributing to Landlord's decision to execute this Lease with Tenant. Accordingly, Tenant hereby covenants and agrees: (i) to operate in the Premises only under the Trade Name set forth in Section 1.01 and under no other name or Trade Name whatsoever without Landlord's prior written consent, and (ii) to continuously use, occupy and operate the whole of the Premises for the retail sale of its goods or services in accordance with its Permitted Use (Tenant hereby agreeing to minimize the space utilized for non-sales activities), and for no other purpose whatsoever, during minimum business hours of to, days per week (excluding the holidays of), or such other hours not to exceed as are from time to time designated by Landlord and applicable to all similarly situated tenants in the Shopping Center, without Landlord's prior written consent. Without limitation of the foregoing, Tenant further agrees not to operate in the Premises for any use in violation of (x) any exclusive use now or hereafter benefitting another tenant in the Shopping Center and binding on Landlord (but, with respect to any such exclusive use first existing after the date hereof, only to the extent that it does not conflict with the Permitted Use hereunder) or (y) any of the prohibited uses identified in Exhibit D. Furthermore, Tenant agrees that neither Tenant nor any party controlling, controlled by or in common control with Tenant will own or operate, either directly or indirectly, a physical retail store, for a use similar to the Permitted Use and which employs the Trade Name or a variation thereof, within a radius of miles of the perimeter of the Shopping Center or as a subtenant, licensee or concessionaire of another tenant at the Shopping Center, except for any stores in operation as of the date hereof. Without limiting Landlord's other available remedies, in the event Tenant violates the terms of the preceding sentence, Landlord may, at its option, treat all revenues generated by any such violative business as included in Gross Sales for purposes of calculating the Percentage Rent due under this Lease.

IV Maintenance and Repair Obligations in Retail Leases

a. **Landlord vs. Tenant Obligations** - Every retail store lease contains provisions which allocate responsibility between the landlord and the tenant for the maintenance and repair of the store and the Shopping Center. At first glance, it sounds like this should be an easy exercise since the tenant should be responsible for everything inside of the store and the landlord should be responsible for everything outside of the store; but is that really accurate? What happens when building systems run through the middle of a store, such as chilled water pipes or electrical conduits, the tenant connects to those systems and there is a subsequent damage or loss to those systems, which is not the fault of the tenant. Whose responsibility is it to repair or replace those elements? Does the fact that the systems run through the store premises and that the tenant tied into those systems automatically mean that the tenant must maintain, repair or replace those systems at the tenant's cost?

How are maintenance obligations typically allocated between the landlord and the tenant? New York courts have interpreted this very narrowly and in the case of *Leeber Realty LLC v. Trustco Bank*, 316 F. Supp. 3d 594, (S.D.N.Y. 2018), the court held that the landlord's obligation to repair must be expressly set forth in the lease and will not be implied. Accordingly, if the lease is not explicit as to the landlord's repair obligations, the courts may not imply an obligation on the part of the Landlord to repair. This case highlights the importance of drafting lease provisions that are very explicit and allocate the agreed upon repair obligations to be performed by the landlord and the tenant under the lease.

b. **Repair vs. Replacement Obligations** - Leases contain various obligations that are to be performed by each party. Such responsibilities include, to varying degrees, maintenance, repair and replacement. Often, however, these terms are not defined within the four corners of the lease. Unfortunately, a lack of clarity as to what these terms really mean, and whether they even differ, can lead to disputes between the landlord and the tenant. In order to avoid the potential consequences of vague drafting, it may be worthwhile to consider how some courts have interpreted these commonly used, yet seldom defined, words. In the case of *Best Buy*, the court in *Abbe Road Realty, LLC v. Kuehne & Nagel, Inc.*, No. 1:14 CV 2463, 2017 WL 10858881, at *8 (N.D. Ohio July 10, 2017), an Ohio court resorted to consulting the dictionary to provide clarity on what an undefined lease term may have meant. The court, citing the dictionary and other case law, stated that while repair is to "renew or restore an existing thing" or to "fix" it, the term replace means to "provide a substitute or successor for" the item as a whole [*please take note that while repair can include replacement, it only does so to the extent it is the "replacement of subsidiary parts"*]. The court further reasoned that if changes are extensive, or "breathe new life" into the item, increasing longevity and transforming it, then such changes are considered far greater than repair and such changes are in the nature of replacements. From the landlord's standpoint, it would be prudent to specifically define and use the word "replace" as part of tenant's lease obligations if the landlord's intent is to have the tenant replace items such as HVAC equipment when repair is no longer a viable option during the term of the lease.

c. **Good Condition vs. First Class Condition** - Reference is frequently made in retail leases to leaving the premises in "good condition". Courts may consider a variety of factors and sources when attempting to define good condition. In *Zundel v. Zundel*, 901 N.W.2d 731, (N.D. 2017), the court relied on the landlord's testimony that they equated good condition and repair with "functional and operable." In light of such interpretation, the court found that given the evidence that tenant made repairs on an as-needed bases, thereby keeping the site in functional condition, tenant had met its obligation to keep the site in good condition and repair. Another way to define good condition, without extreme particularity, is to require a tenant to keep its premises in as good condition as when tenant first occupied the space, which will at least provide tenant (and the courts) with a basis from which to start.

There is great divergence of opinion as to the meaning of first class condition. Is first class condition the same as good condition? Generally, first class condition is an extremely high standard. In the case of *Apple Glen Investors, L.P. v. Express Scripts, Inc.*, No. 8:14-cv-1527-T-33EAJ, 2016 WL 909322 at *12 (M.D. Fla March 10, 2016), the lease required the tenant to maintain the premises in a first class condition, however, first class condition was never actually defined. Given that the lease was silent on the definition of first class, the court looked to the meaning "first class" had to experts and people in the field (HVAC technicians, mechanical engineers, general contractors, appraisers, architects, etc.). In support of its assertion that the premises was in first class condition prior to leasing, the landlord hired an architect to inspect and prepare a conditions reports of various systems and aspects of the premises, using a scale ranging from first class condition to unacceptable condition requiring extensive repair and replacement. In addition, the landlord hired experts to testify as to the condition of various aspects of the premises before and after the tenant's occupancy thereof. Experts specifically stated that certain aspects of the premises were in a "Class A condition" which, in their opinions, was synonymous with first class. Also relevant was how much the landlord had invested into the premises prior to leasing it and what features the premises boasted, as experts used this in their review of the before and after. For example, experts considered what the age and estimated value of various improvements at the commencement of the term were and how much would it cost to repair or replace such improvements at the term's expiration. In defining first class, it is also helpful to consider what it is not. One of the landlord's experts in the *Apple Glen Investors, L.P.* case relied on industry-standard published authorities to define a physical deficiency which encompasses items approaching or exceeding their typical life and specifically excludes items that may be remedied with routine maintenance. The court found that a premises cannot be in first class condition if there is a physical deficiency.

d. **Restoration Obligations at End of Lease** - Depending on the specificity of a repair and maintenance provision, a court may look to it rather than a surrender clause when evaluating restoration obligations at the expiration of a lease. For example, in *Abbe Road Realty LLC*, the operating expenses provision required the tenant to maintain certain parts of the premises and went on to state that any failure to do so would survive lease termination. Towards the end of the term, the parties performed a walk through inspection and the landlord noted various items (that were the tenant's responsibility under the lease) requiring repair, however, the tenant vacated the premises without undertaking any of those repairs. The tenant attempted to argue that it was not responsible for the post-lease repairs in light of the surrender clause, as those items constituted normal wear and tear. The court, however, ruled that the tenant was liable for the repairs under the maintenance and repair provision of the lease which did not exempt normal wear and tear.

Even in cases where maintenance and repair or restoration provisions allow for 'ordinary wear and tear,' such exemption will not allow a tenant to neglect to make capital repairs or replacements. In fact, if systems or components are "approaching, have reached, or have exceeded their typical expected useful life," such conditions have exceeded the standard of ordinary wear and tear. In its determination of what constitutes ordinary wear and tear, a court may evaluate whether an improvement is still under warranty and what industry standard would consider ordinary wear and tear.

Sample Lease Repair Provisions

SECTION 10.1 Repairs.

Subject to the provisions of Articles ____ and ____ hereof, Landlord shall not be required to make any repairs or improvements of any kind upon or to the Demised Premises or to the Center, except for necessary repairs to the foundation and structural load bearing walls of the Demised Premises. Landlord agrees to make necessary repairs to the roof and the structural load bearing walls of the building of which the Demised Premises is a part, and the water and sewer lines servicing, on a non-exclusive basis, the Demised Premises that are located outside of the Demised Premises but within the Center and are not within the premises demised to any other tenant in the Center. Notwithstanding the foregoing, if the necessity for the making of any of such repairs shall have been occasioned by any act, omission or negligence of Tenant, or any subtenant, concessionaire or licensee of Tenant, or their respective employees, agents, invitees, contractors or subcontractors, Tenant shall be solely responsible for the cost of all such repairs, and at Landlord's election, shall promptly make such repairs.

Except for Landlord's obligations as expressly provided above in this Section 10.1, Tenant, at Tenant's sole cost and expense, **shall keep and maintain in first class appearance**, in a condition at least equal to that which is required when Tenant initially opens the Demised Premises for business, and in good order, condition and repair as determined by Landlord (including replacement of parts and equipment, if necessary) the Demised Premises and every part thereof and any and all appurtenances thereto wherever located. Without limiting the generality of the foregoing, Tenant, at its expense, shall maintain and promptly make any and all **necessary repairs to or replacements** of: (i) that portion of any pipes, lines, ducts, wires or conduits (whether contained within or outside the Demised Premises) which are installed by Tenant or that exclusively serve the Demised Premises; (ii) the glass windows, plate glass doors, and all fixtures or appurtenances composed of glass that are located in or about the Demised Premises; (iii) Tenant's signs; (iv) the floors and floor coverings, doors and door frames, windows and window frames, walls, storefront including security gates, grilles or enclosures, locks and closing devices, partitions and ceilings in the Demised Premises; (v) heating, ventilating, air conditioning, electrical and plumbing system(s) equipment and fixtures (whether contained within or outside the Demised Premises) which are installed by Tenant or which exclusively serve the Demised Premises; and (vi) the Demised Premises or any part of the Center when repairs thereto are necessitated by any act or omission (negligent or otherwise) of Tenant or any of Tenant's agents, employees, contractors or invitees, or by the failure of Tenant to perform any of its obligations under this Lease. Notwithstanding any contrary provision of this Section 5.1, Tenant, at its expense, shall make any and all repairs to the Demised Premises as may be necessitated by any break-in, forcible entry or other trespass into or upon the Demised Premises, regardless of whether or not such entry and damage is caused by the negligence or fault of Landlord or Tenant or occurs during or after business hours. Tenant, at Tenant's sole cost and

expense, shall promptly make all other repairs, replacements, renewals and restorations, interior and exterior, ordinary and extraordinary, foreseen and unforeseen, relating to the Demised Premises.

If Tenant fails to promptly make any repairs required hereunder, Landlord may make such repairs without obligation to do so and without liability to Tenant for any loss or damage that may accrue to Tenant's stock or business by reason thereof, and if Landlord makes such repairs, Tenant will pay to Landlord, on demand, the entire cost thereof, together with an administrative fee equal to twenty-five (25%) percent thereof. Landlord shall use reasonable efforts to do any required repair work with minimum inconvenience, annoyance, disturbance, interruption or loss of business to Tenant, as may be practicable under the circumstances consistent with accepted construction practice, but in no event shall Landlord be responsible or liable for any of the same or required to incur any additional expenses for work to be done during hours or days other than regular business hours and days. **Tenant shall keep the Demised Premises in a first class, like new and attractive condition throughout the Lease Term, consistent with the high standards of the Center.** All flooring must be replaced by Tenant and all parts of the interior of the Demised Premises (including display racks and other sales apparatus) and of the storefront and exterior doors and entrances shall be painted or otherwise refurbished by Tenant periodically as determined by Landlord, in accordance with plans and specifications first submitted to and approved by Landlord, in accordance with applicable provisions of this Lease. In addition to the requirements set forth in this Article X (and not in lieu thereof), all damage to Tenant's fixtures, leasehold improvements and other personal property in the Demised Premises must be repaired and/or refurbished by Tenant periodically as determined by Landlord, in accordance with plans and specifications first submitted to and approved by Landlord in accordance with applicable provisions of this Lease. Tenant agrees to provide regular maintenance and service (for example, without limitation, regular filter changes and fan replacement) to the heating and air conditioning and ventilating equipment in the Demised Premises and to keep in full force and effect a standard maintenance agreement on all heating and air conditioning equipment serving the Demised Premises. Tenant agrees to furnish a copy of such maintenance agreement to Landlord, upon request from time to time.

ICSC Model Retail Lease Provisions for Maintenance and Repair

SECTION 7.04. Maintenance by Tenant.

Tenant shall, at Tenant's expense, at all times keep and maintain the Premises and the appurtenances thereto in good order, condition and repair, including the replacement of equipment, fixtures and all broken glass (with glass of the same size and quality), and shall refurbish, redecorate or paint the Premises from time to time as shall be reasonably necessary in order to maintain the same at all times in a clean and slightly manner; excepting only such areas of responsibility as are expressly made Landlord's obligation as set forth in Section 7.05. In the event Tenant fails to perform any of its obligations as required under this Section, Landlord may, but shall not be required to, perform and satisfy same on Tenant's behalf and Tenant shall reimburse Landlord, as Additional Rent, for the cost thereof promptly upon demand. Tenant shall make any and all additions, improvements, alterations and repairs to or on the Premises that may at any time during the Lease Term be required by any lawful authorities or applicable insurance underwriters or ratings bureaus, except for such items as Landlord is obligated to repair and maintain as expressly set forth in this Lease.

SECTION 7.05. Maintenance by Landlord.

Landlord shall keep and maintain the structural elements, exterior walls, foundations, roof, gutters and downspouts of the Premises, and those elements of the mechanical, electrical, plumbing, life safety, HVAC or other systems located outside of or not otherwise serving the Premises exclusively, in good order, repair and condition, provided that the damage thereto shall not have been caused by negligence of Tenant or its concessionaires, officers, agents, employees, licensees or invitees (in which event Tenant shall be responsible therefor). Tenant shall promptly give Landlord written notice of the necessity for any repairs required to be made by Landlord. Except as expressly set forth herein, Landlord shall have no obligation to repair, maintain, alter or perform any other acts with reference to the Premises or its appurtenances.

V Force Majeure Clauses

a. **Effect of the COVID -19 pandemic** - As a result of the COVID-19 pandemic, commercial landlords and tenants found themselves in an unprecedented situation fraught with uncertainty. Government mandated business closures and wide-spread shelter in place orders caused substantial disruptions to both the economy and the way we live. Landlords and tenants scrambled to reevaluate their respective obligations under their leases to assess risks and mitigate potential adverse consequences as a result of the coronavirus crisis

b. **Excuse of performance and necessary elements** - Force majeure provisions in commercial leases generally provide for the suspension or excuse of a party's performance of an obligation as a result of an unforeseeable event that is beyond that party's control, such as the outbreak of war, strikes, natural disasters and acts of God, *provided that the unforeseeable event is expressly articulated in the lease provision at the time of contracting as an enumerated event that could occur in the future*. Force majeure derives from contract law, not common law - which means that the concept only applies if, and to the extent stated in the lease. Therefore, if the lease is silent as to force majeure events or if a specific force majeure event is not covered by the lease provisions, it is likely that no relief will be afforded a party seeking to suspend or excuse their performance as a result of those unforeseen events.

In cases where the lease agreement does not specifically list pandemics, outbreaks and widespread infectious diseases as force majeure events, the parties may be forced to rely on catch-all provisions, such as "events or circumstances beyond a party's control", to invoke force majeure. Courts, however, are reluctant to go beyond the four corners of a lease in an attempt to interpret what is and is not a covered force majeure event. Consequently, a well-drafted force majeure clause should be as broad as possible and enumerate as many force majeure events as possible.

c. **Continuous operation obligations** - Landlords and tenants struggled during the height of the COVID-19 pandemic to determine if their respective obligations were suspended or excused as a result of government-ordered or landlord-mandated store closures as a consequence of the COVID-19 outbreak (a "Mandatory Store Closure"). For example, if a party is prevented from being able to open its store on a certain date or finish store construction as a result of a Mandatory Store Closure, which is a covered event under the force majeure clause, the tenant's performance would normally be suspended for the duration of the force majeure event and the tenant would not be obligated to complete its performance under the lease or to continue its operations until after the cessation of the covered event.

d. **Rent relief provisions** - With regard to the obligation to pay rent, landlord's typically have contended that tenant's obligation to pay rent is not be excused by a Mandatory Store Closure since the banks are still open and tenants can make wire transfers and pay their rent. Tenants on the other hand argued no rent should be due during the Mandatory Store Closure since the tenant is not receiving the benefit of the bargain and cannot operate its retail store. The answer, however, depends upon the express wording of the force majeure provision in the lease. Most modern force majeure clauses in commercial leases expressly exclude the suspension or abatement of rent as a tenant remedy during a covered force majeure event. As a result of the pandemic, however, new leases have been recast to address the possibility of future lockdowns and retail store closures and landlords and tenants may have found middle ground as to the rent abatement issue through the concept of apportionment of rent. For example, if 100% of the premises is not useable by the tenant, then 100% of the rent would be abated during the duration of the Mandatory Store Closure. However, if 50% of the premises is not useable by the tenant as a result of a Mandatory Store Closure, then 50% of the rent would be abated during the duration of the Mandatory Store Closure. Below is a sample lease provision illustrating this concept of apportionment of rent during a Mandatory Store Closure.

Sample Lease Force Majeure Clause

(a) Notwithstanding the terms and provisions of this Lease to the contrary, if either party hereto shall be delayed or hindered in or prevented from the performance of any act required hereunder or if this Lease provides a time limitation for a party to perform an obligation, such time limitation shall be extended for so long as, and to the extent that, the party is prevented or delayed in performing the obligation due to a Force Majeure Event, as herein defined. For the purposes of this Lease, a "Force Majeure Event" or Force Majeure Events" shall mean strikes, lockouts, labor troubles, inability to procure material, failure of power, restrictive governmental laws or regulations, riots, insurrection, war, act of God, public health emergencies including COVID-19, pandemic or epidemic and related declarations, orders, laws and guidelines issued by public health organizations and/or governmental authorities (collectively, "Public Health Emergency Restrictions"), environmental remediation work whether ordered by any governmental body or voluntarily initiated or other reason of a like nature not the fault of the party delayed in performing work or doing acts required under this

Lease, the period for the performance of any such act shall be extended for a period equivalent to the period of any such delay.

(b) Notwithstanding the terms and provisions of this Lease to the contrary, in the event of any Public Health Emergency Restrictions, as such terms are defined in Section 84 (a) herein, Tenant's obligation (i) to open and/or remain open for business to the public at the Premises shall be suspended during the pendency of any such Public Health Emergency Restrictions and/or such other Force Majeure Events and until such time as any Public Health Emergency Restrictions have been lifted and/or such other Force Majeure Events shall cease so that Tenant can fully occupy, use and operate its business at the demised premises for the Permitted Use, and (ii) Tenant's obligation to pay Fixed Rent shall be abated by the percentage that the demised premises cannot be occupied and used by Tenant on account of any Public Health Emergency Restrictions multiplied by the Fixed Rent due under this Lease for each day or month that such Public Health Emergency Restrictions are in effect and are applicable to Tenant's business at the demised premises (the "Rental Reduction"). By way of example and for illustration purposes only, assume that the monthly Fixed Rent under the Lease is \$29,000 per month and that under the provisions of the applicable Public Health Emergency Restrictions only 50% of the demised premises may be occupied and used by Tenant. Based upon the foregoing, the monthly Fixed Rent of \$29,000 would be multiplied by 50% (or the percentage of the demised premises that Tenant is restricted from occupying and using during the pendency of the Public Health Emergency Restrictions) so that the monthly Fixed Rent would be reduced by amount of \$14,500 per month.

ICSC Model Retail Lease Provisions for Force Majeure

SECTION 17.06. Force Majeure.

If either party shall be delayed or hindered in or prevented from the performance of any act required hereunder by reason of strikes, lockouts, labor troubles, inability to procure material, failure of power, restrictive governmental laws or regulations, riots, insurrection, terrorism, epidemic or pandemic, war or other reason of a like nature beyond the reasonable control of a party (but not for the inability to meet its monetary obligations hereunder), the period for the performance of any such act shall be extended for a period equivalent to the period of such delay.