

FOOD FOR THOUGHT

Considerations in Negotiating and Drafting Food and Restaurant Leases

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Restaurant leases are just like other commercial leases, right? There should be no problem using the same form you used for the clothing store next door, right?

In fact, restaurant leases in many respects will be similar to your other commercial leases. However, there are a surprising number of provisions of the Lease which must necessarily be adapted in a good restaurant lease, whether you represent the Landlord or the Tenant. In addition to the business terms, the legal boilerplate language that makes your eyes glaze over can be particularly prejudicial to a party in a restaurant deal.

This presentation and these materials will focus on the various provisions of a commercial lease that should be considered in the negotiation of a restaurant lease.

EXCLUSIVITY CLAUSES

Exclusivity clauses are alive and, depending on whose interests you represent, well, in restaurant leasing. Any restaurant user that has recently tried to lease space in a Development that has a certain unnamed coffee shop has likely been exposed to this issue. Both Landlord and Tenant need to pay close attention to this clause.

- **Justification/Policy.** Restaurant uses are territorial, making an exclusivity clause important to Tenant for a number of reasons: (a) a trade market may be able to adequately support one but not two similar restaurant concepts in close proximity, (b) Tenant may be very successful in a trade market that could support another similar restaurant use and Tenant may not want to see its sales and profits cannibalized by a similar concept entering the area, (c) Tenant does not want to expend a considerable sum to identify a potential trade market only to have a competitor piggyback on Tenant's investment and hard work by jumping into the Development, and (d) Tenant may actually want to cannibalize one of its own stores without interference from the Landlord. This last reason may arise when an existing restaurant has strong sales and the trade market is strong enough that a second restaurant in close proximity will result in two restaurants with strong sales albeit at a level lower than the sales of the first restaurant operating alone.

On the other hand, each time Landlord affords a restaurant an exclusive, Landlord chips away at the potential pool of tenants to whom it may lease space. If Landlord accommodates Tenant's request for an exclusive, it will make all subsequent tenants subject to Tenant's exclusive, which in turn will undoubtedly give rise to such other subsequent tenants also requesting exclusives. Each time the pool of potential tenants is diminished, the Development becomes harder to lease which benefits neither Landlord nor Tenant. As a matter of principle, Landlord may refuse to grant an exclusive arguing that Landlord should not be responsible for Tenant's fear of competition.

- Scope. For all of Tenant's reasons set forth above, Tenant should seek an exclusive clause that is as broad as possible. Ideally, Tenant would like an exclusive clause prohibiting any other restaurant use in the Development. This will usually be unattainable and unnecessary. Tenant should identify the key unique components of its business and seek an exclusivity clause that protects those key unique components. To the contrary, Landlord will try to limit the scope of the exclusive to Tenant's core business. From Landlord's perspective, an exclusive should never be absolute but should only restrict a "primary" use of another tenant. For example, if Landlord grants an exclusive for "Chinese Food", any family style restaurant or grocery store that sells egg rolls or a stir fry dish could be deemed in violation. With many retailers, defining "primary" use is an easier concept to address as the parties can agree on a percentage of sales areas or monthly gross receipts. However, sales area is irrelevant in the context of a restaurant as all patrons order off of the same menu, and many restaurants will not report gross receipts to a Landlord. A practical solution when addressing the primary use for the scope of the exclusive may be restricting a percentage of entrée menu items or focus of advertising.
- Representations. Tenant should also seek assurances from Landlord (in the form of covenants, warranties, and representations, as appropriate) that (a) Tenant's current use will not violate any exclusivity clause of another Tenant, (b) no current use at the Development would violate Tenant's exclusivity clause, and (c) Landlord is under no obligation to a third party potential tenant to grant a use that could violate Tenant's exclusivity clause. Landlord should object to each of these representations, and instead, will agree to provide all of the existing exclusives of the Development for Tenant to review. Landlord should argue that Tenant is in the best position to assess whether an existing exclusive would prejudice Tenant's use. With respect to pre-existing tenants' uses, Landlord should except these from the scope of Tenant's exclusive, arguing that Landlord cannot modify the terms thereof. However, as a compromise, Landlord could agree not to consent to a change of use afforded to a pre-existing tenant if such change of use would otherwise violate Tenant's exclusive. Landlord must be careful though not to put itself in default of such other tenant's lease or otherwise be required to recapture such other tenant's premises.
- Additional Conditions of Exclusive. Tenant must also insure that the exclusivity clause: (a) prohibits Landlord from violating the exclusive use or permitting the

same whether by leasing, selling, conveying, or licensing; (b) will be contained in a recorded memorandum of lease; and (c) obligates Landlord to include the exclusive in all future instruments and conveyances. Subject to the issues relating to existing tenants as set forth above, Landlord may be agreeable to affording Tenant these protections, except that the recordation of a memorandum of lease can trigger taxes and fees in many jurisdictions, and Landlord will want Tenant to bear such costs. Landlord must also attempt to condition the exclusive on Tenant's continuous operation for such exclusive (core) use and on not being in default beyond cure periods.

- Remedies. Given the catastrophic effect a competing use may have on Tenant's business, Tenant will want extensive remedies for a violation of the exclusivity clause including: (a) requirements that Landlord take all actions to terminate a violation or threatened violation; (b) the ability to seek injunctive relief; (c) the ability to act to enforce the restriction on behalf of the Landlord if the Landlord fails to do so; (d) the right to collect costs, expenses, and damages incurred as a result of the breach of the exclusive, (e) the right to reduce or terminate rent, and (f) the right to terminate the Lease and seek damages. Landlord must be careful not to overexpose itself in the event of a violation of an exclusivity clause given to Tenant. The most common example of such overexposure occurs with a "renegade" or "rogue" tenant. For example, while another tenant's use may be subject to Tenant's exclusivity clause, the restricted tenant may disregard this prohibition and engage in the protected exclusive use. In such an instance, Landlord has committed no wrongdoing, but may be faced with the need to institute enforcement proceedings to stop the violating use coupled with the liability to Tenant as a result of a violation of the exclusivity clause. Landlord will want to eliminate or reduce Tenant's remedies due to a violation by the renegade tenant, agreeing only to enforce (or assign to Tenant the ability to enforce) the violating tenant's lease. Of course, whenever Landlord assigns the enforcement right, it should be subject to an indemnity from Tenant. Landlord's arguments for limiting Tenant's remedies are weakened if the violation of Tenant's exclusive is not due to a renegade tenant but rather due to a failure of Landlord to subject another tenant's lease to Tenant's exclusive. Landlord, however, will still want to limit the effect of a violation. Landlords vary significantly with respect to preferred remedies, some preferring to allow tenants to bring any action allowed at law or in equity (believing that damages will be too difficult to prove), some preferring to allow tenants to reduce rent (or pay percentage rent only) for a period of time subject to a "sunset" provision whereby within a specified period of time, Tenant must choose to return to full rent or terminate the Lease, and some prefer to limit tenants to a termination right with or without payment of unamortized costs.
- Radius. In some circumstances, Landlord may actually seek an exclusive from Tenant. This occurs most often when percentage rent is part of a Lease. Landlord will want to try to prohibit the Tenant from cannibalizing its current restaurant under the Lease by operating another restaurant in close proximity to the Development. Landlord will seek a clause that prohibits Tenant from operating

another restaurant of the same primary use within a certain radius of the Development site. Tenant may also want the radius clause, precluding Landlord or any affiliate of Landlord from permitting a violation within a certain radius of the Development. Landlord will resist the radius as it could affect the marketability of, or ability to finance, the Development. At the very least the radius imposed upon Landlord must carve out (a) any then existing tenants of property within the radius (whether such property is acquired by Landlord or another developer that is acquiring the Development), and (b) any mortgagee or successor thereto.

Sample Language.

A sample Tenant exclusive clause is as follows:

As material inducement for Tenant to enter into this Lease, Landlord and its respective successors and/or assigns, shall not convey, assign, license, sell or lease any property adjoining the Premises [or within a ____ mile radius of the Premises or within the _____ Development], whether now owned or hereafter acquired by Landlord, without first prohibiting the use of such property to be conveyed, assigned, licensed, sold or leased for the operation of a _____ (the "Restriction"). The Restriction shall apply only as long as all of the following conditions exist: (i) Tenant is occupying the Premises and operating as a _____, and (ii) Tenant is not in default of a material term of this Lease beyond all applicable periods of notice and cure. Such restriction shall be set forth and contained in the Memorandum of Lease and in any instrument of transfer as a covenant running with the land for the benefit of Tenant.

A sample Landlord exclusive clause is as follows:

A. Landlord shall not hereafter lease any store space within the Development during the Term to a tenant whose primary business is the sale of hamburgers ("Exclusive Use"). As used herein, "primary business" means that fifty percent (50%) of Tenant's entrée menu items consist of hamburgers (different toppings do not constitute separate entrée menu items). Tenant expressly understands that the immediately preceding paragraph does not apply to (i) presently existing leases, or to successors or assigns of tenants under such existing leases or to any lease renewals, expansions, extensions, relocations or replacements of such tenants, or (ii) new leases with tenants occupying more than 10,000 square feet of space. In the event of a breach of Landlord's agreement set forth above, Tenant, at its election and as its sole and exclusive remedy for such breach, may terminate this Lease upon prior written notice to Landlord, which notice shall be given by Tenant not less than ninety (90) days prior to the effective date thereof; provided that such termination shall be rendered ineffective if during such ninety (90) day period Landlord causes the cessation of the activities causing the breach. Tenant's right to terminate as provided for in this paragraph shall be conditioned upon Tenant giving Landlord notice within six (6) months of the date of Landlord's breach. Failure of Tenant to give such

notice within the above time period shall be a waiver of Tenant's right to terminate. Tenant shall have no remedy for a violation of this Exclusive Use provision if another tenant or occupant in the Development violates a provision of its lease or license agreement regarding its premises, which either does not permit or specifically prohibits such occupant from using their premises in violation of Tenant's Exclusive Use as set forth above. Landlord, after receipt of notice from Tenant advising of such violation, shall commence an action (or arbitration, if required by such lease or license agreement) against such other tenant or occupant, and thereafter shall use good faith efforts to enforce its rights under such lease or license agreement and to obtain Judicial Relief. For purposes hereof, "Judicial Relief" shall mean a temporary restraining order, preliminary injunction, order of eviction, other court order, or order resulting from an arbitration proceeding enjoining the lease violation; provided, however, Landlord shall not be required to appeal any adverse decision denying Judicial Relief

B. In the event Landlord receives a claim from a third party, whether a governmental officer or private party, claiming that the terms and provisions of this Exclusive Use provision constitute a violation of a law or statute, or are not enforceable in claims, damages or compensation, then Tenant shall be immediately informed by Landlord, and Tenant shall defend, hold harmless and indemnify Landlord from and against any expense, liability or damages (including but not limited to attorneys' fees) resulting from such claim, demand or liability. This Exclusive Use covenant shall cease and terminate and be of no further force or effect if (i) subsequent to the Rent Commencement Date, Tenant is in default beyond the expiration of any applicable notice and cure period, or (ii) the Premises shall cease to be used for the Exclusive Use for a period of thirty (30) days, excluding temporary interruptions of said operation due to events of Force Majeure, or (iii) Tenant assigns its rights under this Lease or sublets all or any portion of the Premises. If the Exclusive Use granted to Tenant hereunder is found to violate any federal, state or local anti-trust law or other law, governmental rule or regulation, this Exclusive Use provision shall immediately become void and be of no further effect.

USE CLAUSES

There are a number of issues particular to a use clause in a restaurant lease that Tenant's counsel must consider. By its nature, a restaurant requires periodic re-imaging, spruce ups, updates, change of concepts, and other use flexibility in order to stay profitable and in line with market trends in trade areas. In addition, any restaurant use that is operating as a franchise will be subject to various image and use requirements imposed by the franchisor and the franchise agreement. All of these factors must be taken into account during Lease negotiations.

- Breadth and Change of Use. Tenant's counsel should make every effort to negotiate a use clause that permits a general restaurant use, and should also seek language to permit a change to any other retail, service, or restaurant use (a) not in conflict with other restrictions that may be applicable to the Premises and/or the Development and (b) that is consistent with the theme of the Premises and/or

Development. Similar considerations for Tenant's flexibility in use should also be addressed in the alterations and signage sections of the Lease to permit the Tenant to re-image or re-brand as may be necessary due to market needs or as may be imposed by a franchise agreement. Landlord's counsel, on the other hand, will want to make sure that it maintains its desired tenant mix and therefore will seek to limit the extent to which Tenant can change restaurant concepts. Landlord may not want to duplicate certain cuisines or themes in the Development and will be sensitive to certain restaurant uses that may be more parking intensive than others. In addition to attempting to reserve certain absolute restrictions for changes of use in this regard, Landlord's counsel should also seek approval and recapture rights for a proposed change of use or format. If Landlord balks at including a "general restaurant" use provision, Tenant should try to negotiate language that allows for a use consistent with a majority of Tenant's other restaurant locations, so long as not in conflict with any exclusives that may be applicable to the Development. While this will permit Tenant flexibility to adjust its menu and image from time to time, Landlord still needs to be concerned that such a "morphing" of a menu or image does not mask a change of use giving rise to the same concerns above.

- Conflict with Franchise Agreement. Leases for franchise locations involve critical use clause issues that will have a grave impact on Tenant if overlooked. The issue arises where Tenant's counsel negotiates a use clause limited to one use and Tenant's franchise agreement requires a re-image not permitted by the Lease. In this situation, Tenant will be in the unenviable position of having to choose between being in default under its Lease or under its franchise agreement. While it reduces some of the impact, Landlord consent is not a cure for this problem, as Landlord consent will cause delays and the same conflict between the Lease and franchise agreement will remain if Landlord refuses to consent. In order to square the two documents, the parties may need to negotiate a "forced recapture" in order to preserve the parties' respective interests, however, Landlord will want to ensure that the conflict and resulting "put option" is a uniform franchise requirement and not simply a fabricated or discretionary requirement thereby affording Tenant a termination right.

Sample Language:

A sample Tenant use clause is as follows:

Tenant shall have the right to use and occupy the Premises (the "Use") for the purpose of operating a restaurant or similar retail operation. The initial Use of the Premises shall be for a _____ restaurant with drive-thru service and sale of alcohol for on site consumption to be open up to 24 hours per day and up to 7 days per week all in Tenant's sole discretion. Thereafter Tenant may change the Use to any other lawful use that does not violate any use restrictions or exclusive clauses for the Development filed of record at the recorder's office or county clerk's office in the county where the Premises is located. Tenant shall not permit any operation that is in violation of "Laws" (as defined in Section _____ of this Lease).

A sample Landlord use clause is as follows:

Tenant shall use the Premises for the operation of a full service (which for all purposes in this Lease shall mean a restaurant where food and drink orders are primarily taken from, and served to, seated customers at tables by waitstaff, upscale, white tablecloth, sit-down, _____ restaurant, subject to the restrictions set forth on Exhibit B, and for no other purpose. Attached hereto as Exhibit F is Tenant's menu. Tenant's menu shall list the items that Tenant intends to sell at the Leased Premises. Tenant is permitted to change the menu prices and delete items from the menu but Tenant is not permitted to add items to the menu without the prior written consent of the Landlord. Notwithstanding the foregoing, if Tenant (or any party occupying the Premises under Tenant) desires to change the use of the Premises, Tenant must first receive Landlord's written consent, which consent shall not be unreasonably withheld or conditioned. Without limiting the factors to be considered by Landlord in granting or withholding Landlord's consent, in no event may the new use (i) violate the exclusive or restrictive rights, or conflict with the primary use, of any other then existing tenant in the Development; (ii) increase the legal parking requirements for the Premises or Development or otherwise cause Landlord to obtain a parking variance; and (iii) be a use which is not customarily found in first class Developments in the _____ Metropolitan Area. Notwithstanding the foregoing and in addition thereto, if Tenant desires to change the use of the Premises, Tenant shall notify Landlord in writing of the intended change (the "Change Notice"). Landlord shall have the option, to be exercised within ninety (90) days of Tenant's Change Notice, to notify Tenant that it wishes to terminate this Lease. If Landlord elects to terminate this Lease, such termination shall be effective ninety (90) days after the date of Landlord's termination notice.

CONTINUOUS OPERATION

Negotiating a restaurant lease is often a time of great expectations. Tenant seeking to open a new restaurant has great hope of success. However, counsel for a restaurant Tenant must play the role of a naysayer or pessimist in order to adequately protect the client's interests. This role is particularly important in the often overlooked area of continuous operation clauses. Tenant's counsel must check the hours and days of operation required by any continuous operation clause. These requirements may be located in the main body of the Lease or as an exhibit or rider to the Lease. These requirements may also be located within an Operating Easement Agreement ("OEA"), Restrictive Easement Agreement ("REA"), or Declaration of Covenants, Conditions, and Restrictions. Counsel will have to obtain a copy of these instruments and all amendments.

- Justification/Policy. Continuous operation clauses require Tenant to be open for business continuously during the Lease term on days and at hours pre-established by the Landlord. Variations of these clauses may require Tenant to be continuously open and adequately stocked and staffed so as to maximize sales or profits. Days and hours will vary from location to location and among types of

locations such as malls, shopping centers, strip centers, power centers, or life-style developments. Landlord seeks a continuous operation clause for a variety of reasons. Among these are a desire to maximize Tenant sales when percentage rent is part of a Lease, a desire to maximize traffic flow within the Development in order to draw customers, a desire to promote the overall health and value of the Development, a desire to maintain a clean, profitable and inviting image for the Development, and the need to meet any co-tenancy requirements contained in other tenants' leases. While seemingly benign on its face, a continuous operation clause has hidden problems for the unwary or unsophisticated restaurant Tenant.

- Hours and Days of Operation. The issues of days and hours of operation must be resolved early during the Lease negotiations. Very few items will be less palatable to Tenant than finding out at the end of a Lease negotiation that the site will not be acceptable due to hours or days of operation after having spent a sizeable sum of money on development costs and attorney's fees. Upon review of the applicable provisions by Tenant's counsel, three main issues may be presented, the first two of which relate to Landlord imposed days and hours of operation. The first issue arises when the days and hours required are longer than those contemplated by Tenant's business model. A restaurant's costs to do business are heavy on labor, costs of goods sold, utilities and rent, and profit margins are thin. For these reasons, being open longer than projected in Tenant's business model may cause Tenant to go from being profitable to being unprofitable. It may also stretch Tenant's ability to provide stock and staff for a site. The second issue arises when the days and hours required are shorter than those contemplated by the Tenant's business model. Being forced to be closed during Tenant's optimal hours could also severely affect profitability. Alternatively, Landlord may allow Tenant to remain open longer than such required hours but may charge Tenant for additional costs (such as security, lighting, utilities, and maintenance).
- Going Dark/Recapture. The third issue arising from a continuous operation clause is perhaps the most difficult for Tenant's counsel to present to his/her client, as it involves the preservation of an exit strategy if Tenant's business is not successful. Tenant will want to stop the bleeding by either terminating the Lease or ceasing operation thereby reducing its costs and expenses at the site. In the face of a continuous operation clause, the latter would place Tenant in default under the Lease and subject Tenant to greater exposure and damages. Tenant's counsel must be sure to get some flexibility in this area for the client. However, Landlord will argue that Tenant's failure should not be Landlord's problem and will often insist that Tenant remain open and operating even if it means operating a losing business. Compromises can often be reached in the form of "going dark" and "recapture" clauses.

A "going dark" clause permits Tenant to stop operating at a site without being in default under a Lease provided Tenant complies with all of its other Lease obligations including the payment of rent. A "going dark" option may be available immediately or after a period of time (1, 2, or 3 years or more of operation). The going dark clause addresses Tenant's need to reduce expenses in

the face of a failing business without otherwise being in default under the Lease. However, Landlord is then faced with a closed space that is not maximizing sales or traffic flow, and otherwise creates an eyesore or the impression of a failing development. The diminished image is even a greater concern for a ground leased restaurant site where the dark restaurant is likely near the entrance of the Development. A “recapture clause” may address Landlord’s concern. A “recapture clause” permits Landlord to regain control of the Premises after Tenant closes under a going dark clause for a stated period of time (usually 90 to 180 days). When Landlord elects to recapture the Premises, the Lease is terminated without further future liability between the parties. This affords Landlord the opportunity to re-lease the Premises thereby increasing sales, traffic, and the health and value of the Development.

Tenant’s counsel should be sure to negotiate two provisions in the recapture clause. First, the clause should carve out periods of time that Tenant may close due to casualty, repair, maintenance, alterations, re-imaging, or force majeure events. Landlord’s counsel will want to limit the time periods for such permitted closures and require Tenant to diligently pursue re-opening. Second, the recapture clause should require Landlord to pay to Tenant the Tenant’s unamortized leasehold improvement costs at the time of the recapture. Landlord will object to having to pay Tenant to assist Tenant in exercising an exit strategy, particularly if the improvements are specific to Tenant and cannot be re-used by the Landlord. This is often a larger point of contention in a ground lease where Tenant may have expended significant sums in constructing leasable improvements on otherwise raw or paved land. Of course, should Landlord agree to pay such unamortized improvements, the parties will need to address the method and timing of amortization, the costs to be amortized (i.e. hard and/or soft costs, initial costs and/or subsequent improvements) and Landlord’s inspection rights of records relating thereto.

A sample Tenant continuous operation, going dark and recapture clause is as follows:

Tenant agrees to open for business to the public in the Premises fully staffed and stocked for business for a period of one (1) day. Nothing contained in this Lease shall be construed to require or impose upon Tenant an obligation to operate continuously in the Premises. If Tenant ceases to operate its business on the Premises for more than ninety (90) consecutive days (excluding any period the Premises are not being operated due to casualty, condemnation, renovation or repairs and periods falling under Force Majeure as defined in Section ____ of this Lease), Landlord shall have the right as its sole remedy to terminate this Lease by giving written notice to Tenant ("Landlord's Termination Notice"). If Tenant fails to re-open within 30 days following receipt of Landlord's Termination Notice, this Lease shall terminate upon Landlord paying Tenant for the value of the unamortized amount of Tenant’s leasehold improvements, the costs and expenses incurred for the Development of the Premises and for the Improvements made to the Premises by Tenant (collectively “Tenant’s Unamortized Cost of Leasehold Improvements”). If Landlord and Tenant are unable to agree

upon the Tenant's Unamortized Cost of Leasehold Improvements within thirty (30) days after the receipt of Landlord's Termination Notice, then Tenant's Unamortized Cost of Leasehold Improvements shall be determined by the following binding procedure. Landlord and Tenant shall, within ten (10) days following the expiration of such thirty (30) day period, each designate an independent broker or appraiser (respectively, "Landlord's Appraiser" and "Tenant's Appraiser", individually an "Appraiser", and collectively the "Appraisers") with at least ten (10) years experience in the leasing of comparable commercial property in _____ County, _____ . The Appraisers shall determine Tenant's Unamortized Cost of Leasehold Improvements and the Landlord and Tenant shall have the right to submit memorandum and other evidence in support of their positions to the Appraisers. The joint decision of Landlord's Appraiser and Tenant's Appraiser shall be final and binding on Landlord and Tenant. In the event either Landlord or Tenant fails to appoint its Appraiser within such ten (10) day period, the decision as to Tenant's Unamortized Cost of Leasehold Improvements made by the Landlord's Appraiser or the Tenant's Appraiser so appointed, as the case may be, shall be final and binding on Landlord and Tenant. In the event that Landlord's Appraiser and Tenant's Appraiser fail to agree as to Tenant's Unamortized Cost of Leasehold Improvements within thirty (30) days after their appointment, then Landlord's Appraiser and Tenant's Appraiser shall jointly designate a third individual having the qualifications set forth above (the "Third Appraiser") for determination of Tenant's Unamortized Cost of Leasehold Improvements. In the event Landlord's Appraiser and Tenant's Appraiser fail to agree as to the appointment of the Third Appraiser within ten (10) days of the expiration of such thirty (30) day period, then the Third Appraiser shall be an individual with the required qualifications selected by the American Arbitration Association located in or serving the City of _____, _____ pursuant to its then current procedures. The Third Appraiser shall, within fifteen (15) days after his or her appointment and after due consideration of the respective positions of Landlord and Tenant, either accept the decision of Landlord's Appraiser or the decision of Tenant's Appraiser or adopt its own position. In any case, the joint decision of Landlord's Appraiser and Tenant's Appraiser or the decision of the Third Appraiser, as the case may be, shall be final and binding on Landlord and Tenant. The costs of engagement of the Third Appraiser shall be borne equally by Landlord and Tenant, and the costs of engagement of Landlord's Appraiser, Tenant's Appraiser and each party's counsel shall be borne by the respective parties. Upon payment to Tenant of the Tenant's Unamortized Cost of Leasehold Improvements, this Lease shall terminate, Tenant shall surrender possession of the Premises to Landlord, and the Landlord and Tenant shall be relieved from all obligations, each to the other, except for obligations and liabilities occurring prior to the date of such termination. Upon such termination, this Lease shall be null and void and of no force and effect, and all parties shall be released from any and all liability accruing subsequent to the effective date of termination.

A sample Landlord continuous operation, going dark and recapture clause is as follows:

Tenant shall open for business on or before the Rent Commencement Date and shall continuously operate for the Permitted Use during the Development Hours for a period of three (3) years thereafter (“Mandatory Operating Period”). At any time after the Mandatory Operating Period, Tenant, in its sole and absolute discretion, may elect to cease to operate in the Premises by giving Landlord not less than one hundred eighty (180) days’ prior written notice (“Go Dark Notice”). At any time thereafter, Landlord shall have the option to terminate this Lease and recapture the Premises, upon giving the Tenant thirty (30) days’ prior written notice of its intent to do so. It shall be an Event of Default if Tenant ceases operations without giving such notice or if Tenant closes for business prior to the expiration of the one hundred eighty (180) day period. After Tenant ceases operations at the Premises, Landlord shall have the right to install on the exterior of the Premises (but not so as to unreasonably obstruct the view or access thereto) the customary "For Rent" sign and to show the Premises to prospective tenants during normal business hours. Tenant's obligation to pay Rent or perform any other obligations under this Lease shall continue until the effective date of said termination by the Landlord (“Termination Date”). All Rent shall be prorated through the Termination Date and Tenant shall promptly pay any of said sums to Landlord. If Landlord elects to terminate under this Paragraph, Tenant agrees it shall surrender the Premises to Landlord in the same condition that Tenant would have been required to if this Lease had terminated on the original Expiration Date. On the Termination Date, the parties hereto shall be released from any further liability and obligations under this Lease, excepting any liability or obligations accruing prior to the Termination Date. While operating for business, Tenant shall operate in a first class manner consistent with other operating _____ restaurants.

ASSIGNMENT & SUBLETTING

Assignment and subletting provisions are often the source of significant negotiation in commercial leases in general, and justifiably so. Although the parties’ interests are important, thankfully, there is usually enough middle ground in such provisions to allow the parties to accommodate each other’s concerns.

- **Justification/Policy.** A restaurant Tenant often enters into a long term Lease and wants the maximum flexibility to assign the Lease or sublet the space (without remaining responsible for the tenant obligations after the assignment) in order to fully realize the benefit of the business it built from a potential purchaser or, like the going dark provision, in order to maintain a satisfactory exit strategy. Landlord, on the other hand, may have negotiated the economic terms of the Lease based upon the name, operation and net worth of Tenant, and will therefore want to preserve these elements of Tenant’s business in an effort to maintain the benefit of Landlord’s bargain. Unconditionally allowing an “unknown” assignee/sublessee Tenant would strip Landlord of such benefit

- Standards. In restaurant leases, certain typical Landlord limitations on subleasing can, if not negotiated in advance by Tenant’s counsel, severely limit the pool of assignee candidates eligible to take on the Lease. Generally, there are three standards which can be found in assignment and subletting clauses: (a) Tenant’s unfettered discretion to assign or sublet without Landlord’s consent, (b) Landlord’s unfettered discretion to disallow any such transfer, and (c) Landlord’s obligation to be reasonable when assessing the assignee or sublessee. While many parties opt for the last option as a reasonable compromise, counsel should recognize that it may not address the parties’ concerns, and can often lead to litigation if the parties do not agree. In many circumstances a potential assignee/sublessee will not wait around for litigation to be resolved and will look elsewhere for sites. In this regard, Landlord and Tenant may benefit by setting forth conditions for consent during Lease negotiations.
- Conditions/Net Worth: Landlord should require the assignee (and perhaps even subtenant) to maintain a certain net worth. Even if Tenant remains liable after the assignment, the tenant in possession must have the financial wherewithal to operate its business. In addition, unless Tenant is a large restaurant group with a significant number of stores, Tenant’s liability may be significantly diminished (almost worthless) after the sale of its restaurant. Landlord may require that an assignee have the “same net worth” or similar revenue stream as Tenant. While generally, this would not be a concern for a mom and pop restaurant owner, if the original Tenant is a larger restaurant owner with multiple locations, or even a multi-site restaurant owner with fewer locations, this condition may be nearly impossible to satisfy. A compromise position is to establish in the Lease what net worth minimum would be acceptable to Landlord. Landlord will also want such net worth to increase over time during a long term lease and will want such net worth to measure as a “tangible” net worth, exclusive of good will.
- Conditions/Use. As discussed in greater depth in the use clause section above, Landlord may also condition an assignment or sublease on the assignee/sublessee operating the “same business” or selling the same product as the original Tenant. If Tenant is a franchisee, or if Tenant predominantly serves American-style cuisine and Tenant wants to assign to someone who would operate a Chinese food restaurant, there would be an issue meeting Landlord’s condition. Further, an assigning Tenant is typically not assigning over its business to the proposed new tenant, and an assignment of just the Lease and not the business operations can generally pose a problem when the Lease contains a “same business” condition.

Use restrictions and exclusivity provisions in the Lease, as well as those in place between Landlord and other tenants in a development, including provisions in REAs and OEAs, will also be factors in the negotiation of permitted assignees. Landlord’s obligations to other tenants not to allow competing uses, and Landlord’s desire to provide a mix of tenants in the center are likely to override Tenant’s desire to walk away from a site quickly or easily. The issues can be addressed in a similar manner as they are addressed in the use clause discussion above.

- Conditions/Experience. Another potential condition Landlord may factor into its decision to approve a potential assignee or sublessee may involve the transferee's experience in the restaurant business. As many new restaurants tend to fail if they do not establish themselves quickly in a market or location, Landlord may require that the proposed new tenant has been in the restaurant business for a number of years, operated in another location in the area for a number of years, and/or operated a number of other restaurants.
- Related Parties. There are instances in which a Tenant should demand that Landlord's consent not be required, as having to go through Landlord could prejudice or delay a multi-store or internal business transaction. Tenant's counsel should carve out certain relationship parties to whom Tenant could assign or sublet the Lease without permission. Typical permitted assignees or sublessees include:
 - Franchisor of the Tenant
 - Other franchisees of Tenant's franchisor
 - Affiliates of Tenant
 - Majority owners of Tenant (or their estates or trusts created by or for them)
 - Transferees of stock/ownership interests

Landlord should attempt to inject as many of the conditions set forth above, even for such transfers, to avoid Tenant circumventing Landlord's consent. In addition, if Tenant is attempting a multi-restaurant transfer, Landlord should seek a requirement that substantially all of such restaurants are being transferred to such transferee (including a minimum number of sites) to preclude Tenant from unloading underperforming restaurants to a lesser operator.

- Liability. Tenant will request a release after an assignment, however, a release is often deemed draconian by Landlord. Landlord bargained for Tenant's particular business, and while Landlord may have a practical outlook in allowing Tenant to transfer its business, Tenant should be required to stand behind its transferee.
- Other Issues. There are quite a few other issues that may/should be addressed in assignment or subletting clauses such as recapture rights, sharing of profits arising from the transfer, ability to subdivide space, execution of an assumption agreement, leasehold mortgages, costs of reviewing requests, and nondisturbance agreements afforded to subtenants, among many others. Indeed addressing all of these issues could be the subject of an entire seminar and will not be separately addressed here. Counsel, however, should be aware that additional issues exist.

DUE DILIGENCE AND SITE SELECTION

Site selection is often performed by Tenant's business personnel and engineers long before counsel's involvement with Lease negotiations. Tenant's counsel should be sure to discuss specific site issues with the client prior to commencing negotiations to identify any special needs regarding Lease provisions.

Due diligence does not typically commence until after the Lease is signed. Tenant's counsel should be certain to consult with the client to confirm that enough time is negotiated into the Lease for the different aspects of due diligence to be appropriately completed, and to become aware of any due diligence items that will have an impact on whether or not Tenant decides to proceed with a site at all. Some due diligence may even be needed prior to protracted Lease negotiations.

Key due diligence considerations in a restaurant lease include:

- Parking is critical to a restaurant, particularly stand-alone, outparcel restaurants. If a customer sees no close parking spot, they may drive away to the next restaurant. Important parking considerations include: how much is needed; how much is available; is it exclusive or non-exclusive; will valet parking be allowed (and if so, is there a designated valet area); is the parking lot designated a "no-build" area; what provisions are in place to limit where employees park; is the parking area safe and well-lit; and how does traffic flow.
- Cross-Access Rights can be particularly important to outparcel sites, especially those who rely heavily on drive-through business. Tenant's counsel should consider: what cross-access rights exist; who/what other types of businesses share the cross-access areas; what limitations and protections are there from change to cross-access rights; issues relating to flow of traffic; how the cross-access affects drive-through stacking and parking lot traffic flow; obtaining rights for future cross-access lanes (e.g., if Landlord obtains adjacent land not owned at the time of Lease commencement).
- Title issues are most often dealt with after the Lease is executed, but having some knowledge of your neighbor can be important to negotiating the restaurant deal on the front-end. Knowledge of the rights of your neighbors in terms of recorded documents like OEAs and REAs (where large anchor tenants are in place) can have a big impact on the ability to obtain desired exclusivity, the ability to obtain as broadly worded a use clause as possible, and the ability to obtain a liquor license, among other things. A quick preliminary title search can spot problem issues at the beginning of negotiations, but if this is not feasible or practicable, enough time for thorough title review should be permitted by the Lease, along with a Tenant termination right in the event the proposed business would be hampered by a title issue. If the cost of a preliminary title review is not feasible, Tenant's counsel should ask Landlord to provide copies of any OEAs, REAs or other documents of record that could have an impact on Tenant's operations, and these items should be attached to the Lease as exhibits. Tenant should also

request a provision in the Lease preventing Landlord from adding additional future title restrictions that could impact changes Tenant may make to its business model over the term of the Lease. Landlord will want to limit any prohibition on its ability to make changes to the restrictions and exclusions applicable to the Development location particularly, so Tenant will be limited in what concessions it is able to obtain in this regard. Tenant should always require Landlord to allow Tenant to record a Memorandum of Lease, so that Tenant's interest is of record and has a priority over future recorded changes.

- Permits and Zoning are critical to Tenant as Tenant must determine whether its intended use will be permitted on the Premises and if not, whether a use variance is obtainable or advisable. Permits and approvals may be required from governmental, quasi-governmental, and private agencies and organizations. Tenant must analyze local laws, zoning regulations, and private development agreements to determine the permits and approvals that will be required, along with the time needed to complete the building approval process. Building and construction permits and signage permits and approvals, must be obtained prior to commencement of construction. Food permits, health department permits, and alcohol licenses must be obtained soon thereafter. The failure to obtain any required permits will result in Tenant incurring a hefty lease liability without the right to operate its business on the Premises. Appropriate time frames for obtaining these items should be built into the Lease. Landlord will view this, however, as Tenant's responsibility.
- Construction needs of Tenant should be compared against private construction requirements for the Premises. Counsel must become familiar with the Tenant's construction needs and, if Tenant is a franchised restaurant, with the franchisor's construction requirements. Tenant's counsel should review private construction requirements found in Development Agreements, OEAs, REAs, or any declarations to be sure that the specific Tenant construction needs will be achievable. Landlord will often want approval rights for Tenant construction. Tenant should seek to limit Landlord approval rights to exterior and structural items only. If Tenant is a franchisee, it must also seek language providing that any construction requirements imposed by the franchisor and consistent with the franchisor's then current image requirements will not require Landlord consent. Tenant should seek language providing that a failure of Landlord to disapprove construction plans within a certain time period (generally no more than 30 days) is deemed to be approval of the construction plans. The Lease should clearly state which party is installing utility services. Hook-up fees, tap fees, connection fees, meter installation fees, impact fees and usage fees must be considered and negotiated. Finally, it is critical that Tenant insure that the utilities installed by Landlord are adequate to serve the Tenant's intended restaurant use.

SIGNAGE

There are very few elements of a national or regional Tenant's success that are more important than name recognition and signage. While there are many different types

of signage, most can be broken into one of two categories, building signage and free standing signage.

- Building Signage. With respect to building signage, the restaurant Tenant, as is the case with most retailers, will want sole discretion as to its design, colors and size to achieve the most prominent visibility and trade recognition. However, Landlord will often be quite protective over affording Tenant broad signage rights as it may lead to an architecturally inharmonious appearance at the Development and may encourage other tenants to request variation from a uniform signage criteria. This is usually less of a concern for Landlord in a restaurant ground/pad lease as uniformity for signage is generally not as important as it would be for inline space. Landlord may therefore agree that so long as such signage on a pad/ground lease is consistent with Tenant's prototypical signage in the region and is professionally prepared, Landlord's consent will not be required.
- Freestanding Signage. If the premises is a pad restaurant/ground lease, Tenant may want the right to erect its own pylon/monuments on its pad to enhance visibility and trade recognition. Landlord, however, will be concerned that any pylon or monument erected by Tenant may diminish the allowable free-standing signage at the Development. Landlord will also be protective of visibility issues, as a free standing sign adjacent to a main thoroughfare may block or detract from the visibility of a main Development pylon. In addition, many anchors will try to reserve the right to be on any free-standing signage at the Development. While Landlord will try to carve out the pylon for any free standing buildings from such a "most favored nations" clause, Landlord's counsel should be aware of any such restrictions prior to giving such free-standing signage rights to a pad restaurant.

LIQUOR LICENSE

The ability to obtain a liquor license can make or break a restaurant. It is critical that Tenant's counsel be aware of what the local liquor license requirements and rules are prior to negotiation of the Lease.

In some jurisdictions, parties may be unable to obtain a liquor license if the site is too close to a school, church, daycare or similar establishment. Knowing these rules can save a client significant time and expense in negotiating a lease for a site that is ineligible for a license. Zoning regulations play an important role in this regard as well, and these regulations should also be consulted prior to proceeding with lease negotiations. Some states require that the terms of the Lease specifically state that Tenant may sell and serve alcohol in and on the Premises. Tenant's counsel should confirm with local authorities what language may be required.

Timing of obtaining a liquor license can also affect the timing of various lease provisions:

- Tenant will want the Lease to contain a condition or contingency that the Tenant be able to obtain state and local liquor licenses for the site, and Tenant's counsel should negotiate a cancellation right in the event a liquor license cannot be obtained. This is especially critical in states where only a limited number of liquor permits are available.
- Tenant should negotiate that a required opening date (and if at all possible, rent commencement) be linked to Tenant's obtaining its liquor permits – no tenant will want to open (or be required to open) without these permits. Knowledge of average timing in the locale is critical to effect negotiations.
- Landlord on the other hand will be very concerned about open-ended contingencies and rights to cancellation. If Tenant requests a long lead time to obtain liquor permits, Tenant should expect that Landlord will limit the period during which it will not collect rent. Landlord may also add requirements that applications be submitted no later than a certain date to avoid delays.
- Often REAs and OEAs (see Due Diligence discussion) will contain limitations on the volume of alcohol allowed in a shopping or lifestyle center. Tenant's counsel should pay particular attention to title due diligence on the site, as waiver letters may be necessary to achieve the level of operations Tenant desires.

PERCENTAGE RENT/GROSS SALES

Including percentage rent as part of a restaurant deal is usually determined in a letter of intent long before the Lease is referred to an attorney for preparation or negotiation. For chain or franchise restaurants, whether Tenant pays percentage rent is often a matter of corporate policy, some agreeing to pay in certain instances (inline or mall space but not pads) while others will simply refuse to ever pay percentage rent or even report sales. Percentage rent for local or mom and pop restaurants are not uncommon however. In any deal where percentage rent is included, the parties must negotiate inclusions and exclusions. As with any retail lease, Landlord will of course want as broad of a definition of gross sales as possible, including any receipt, payment, credit or value received (not just realized) at the Premises, whether by Tenant or any of its licensees, subtenants or concessionaires. Restaurants, however, have particular concerns with respect to otherwise includable items and will want to exclude the following from gross sales:

- Employees' Meals. Because wait staff rely heavily on tips instead of salary, restaurants frequently offer significant incentives by way of reduced priced meals to keep top employees. Restaurants also want

employees to be familiar with the menu to be able to field customer questions. Landlord will try to limit such a deduction of gross sales to a percentage of total gross sales.

- Tips. These are not realized by Tenant and therefore Landlord will typically agree to exclude them from gross sales.
- Vending Machine Sales. Many restaurants have vending machines or games as an accommodation to waiting customers, as a marketing tool or to enhance a theme of a restaurant. Often, these do not generate profit and are sought by Tenant to be excluded. Again, Landlord will attempt to limit the amount of receipts from these machines as exclusions from gross sales.
- Complimentary or Promotional Food Dispensed or Spills. Many restaurant tenants will account for these in their books for accounting/record keeping purposes notwithstanding that no receipts are realized therefrom.
- Off-site Sales. Because catering or delivery sales are received and perhaps filled by different stores or departments, the parties must be clear as to how these are included in gross sales.
- Refunds. To the extent originally included in gross sales, Tenant will seek to deduct amounts of refunds, allowances made on merchandise claimed to be unsatisfactory or discounts to customers.
- Sales Not in the Ordinary Course of Business. Tenant will seek to exclude sales of trade fixtures or store operating equipment from gross sales.
- Promotional Items and Coupons. Tenant will seek to exclude sales of premium items (toys and trinkets) that are sold separately as promotions where the premium items sold are essentially a loss leader to Tenant. Here, Tenant may sell premium items near or below cost as a means of driving additional sales of food items. Tenant will want to exclude from gross sales amounts represented by coupons or similar credits from gross sales.

NUISANCE, WASTE & ODORS

Non-restaurant leases will generally cover this topic in a sentence, maybe two. The very nature of a restaurant requires the lawyers to think a little more about the issue.

- Nuisance clauses in many Landlord form leases can be pretty broadly worded: “shall not cause any nuisance ...” These clauses may be linked to noise prohibitions as well. Landlord will often have a provision limiting the use of

outdoor speakers or other noise outside the four walls of the restaurant building. Tenant's counsel will need to be sure to add a drive-through speaker exception or hostess paging exception in the event either such system is critical to Tenant's operations. Particular care should be taken in the negotiation of nuisance clauses in a Lease for a Mixed Use Development or an office building where stacking of different uses on top of each other can further complicate nuisance and noise issues.

- Landlord no obnoxious odor clauses are also generally broad prohibitions. From a restaurant's perspective however, some foods that smell wonderful to one person may disgust the next. Tenant's counsel should be sure to add an exception for "normal odors associated with the preparation of food and the operation of a restaurant." Landlord may add clauses mandating certain types of venting and air circulation systems, particularly in a mall food court location.
- Garbage is a big issue in a restaurant deal. Not only do restaurants tend to generate more garbage on a pound for pound basis than other retail locations, restaurant garbage can smell bad pretty quickly. Landlord will mandate that the restaurant Tenant remove garbage from inside the restaurant promptly and that dumpsters are emptied on a daily basis or more often if situations require. A mall Tenant will also be prohibited by Landlord from leaving garbage in service hallways, even for a temporary period before taking it to the dumpsters or compactors. Attention should also be paid to compactor usage in a mall restaurant lease – what are the requirements and limitations, are there extra service charges for different levels of use? In an outparcel or inline space, Tenant will want to be sure that dumpsters are located in places that are convenient to the restaurant (think safety to employees taking out the trash in the dark) and that do not impede parking for the restaurant. Tenant's counsel should be sure the client has carefully reviewed the site plan to confirm appropriateness of the dumpster site.
- Pest control – need we say more? Tenant and Landlord should spell out who is doing what and where. Is it part of Common Area Expense for exterior pest control?
- If your restaurant fries anything (and even if it doesn't) there will be a grease trap. In mall food courts, there may be a community grease trap for which all food court tenants share expenses. As with pest control, Landlord and Tenant should spell out the responsibilities and liabilities of the parties or there could be a big mess (both literally and figuratively). Landlord will often require that Tenant provide written proof of regular servicing/emptying of the grease trap.

In all these areas, saying a few words more than what is covered in a "regular" noise, odor and nuisance section of the Lease can save a lot of headaches over the term.

CASUALTY

How is a casualty event at a restaurant different than a casualty affecting other types of retail establishments? In many ways they are the same but since the refurbishment of a restaurant is far more expensive than that of a clothing store, for example, Tenant and Landlord will negotiate more regarding responsibility for repair, rebuilding and the payment of rent during the rebuilding process.

The party responsible for restoration and rebuilding will want to limit its responsibility to rebuild in the last years of the term of the Lease. In a ground lease situation, Tenant will request a right to terminate if substantial repairs or replacements would be required in the last several years of the Lease term. Landlord will generally allow this termination right in the last two to three years of the Lease term (and perhaps at any time during a Lease extension period), but only if the damage exceeds a significant percentage of the Premises. If Landlord and Tenant do agree on Tenant termination rights, this provision should also address to whom insurance proceeds should be paid (remember Tenant may still not have fully amortized its buildout, and Landlord may still want the benefit of improvements and/or a building at the end of the term) and whether Tenant must demolish the building in order to exercise its rights of termination.

Many restaurants, even tenants with multiple locations, are self-supporting. If operations are negatively impacted by a casualty event, Tenant can get into a cash flow bind quickly unless a rent abatement is available. Business interruption insurance may cover the issue – Landlord will certainly ask for Tenant to maintain this as a first line of defense – but if for some reason the coverage is not triggered by the casualty event, many tenants would fold if no rent concessions are made. Addressing these issues during Lease negotiation is thus very important to Tenant. Landlord should be very careful about granting abatement rights in a casualty situation as it may affect the ability to finance the property. Particularly, in a ground lease where Tenant insures its own building and improvements, Tenant is in the best position (and perhaps only position) to insure over the rent stream through its causes of loss policy, and rent should not therefore abate.

As gas and electric service are critical to the function of a restaurant, Tenant's counsel should consider whether the prolonged unavailability of these services or other critical utilities during and after a weather event like a hurricane or ice storm or other significant force majeure event should result in a reduction of rent for the period of unavailability (normally, rent is not abated during a force majeure event). This consideration is necessary since most force majeure clauses specifically do not excuse the payment of rent. After Hurricane Katrina, for example, government authorities kept businesses from returning even to check damages for weeks after the actual storm was over, or if the business did return, power and gas service was interrupted for weeks and even more. If the actual premises were not damaged, business interruption coverage may not have covered the loss due to inability to operate. In areas affected by these types of phenomena, Tenant should consider at least requesting rent abatement during the outage period. Landlord will understandably be reluctant to bear this loss, so a counter-offer of a

rent deferral (made up in increments over time) could save Tenant in a period of zero cash flow. Landlord may also limit this deferral to situations in which service is unavailable for an abnormally long period of time, for example for over a week as opposed to just a couple of days, thus requiring Tenant to bear the loss for an initial period. Sample language to address this issue follows:

Suspension of Operations. Without in any way limiting the rights of Tenant in the event of casualty damage to the Property and Improvements as set forth hereinabove, in the event a named tropical storm or other significant weather event, act of war or other natural or manmade disaster impacts the Property, and Tenant's operations at the Property are suspended due to (i) mandatory governmental evacuation orders in excess of seven (7) days; (ii) power outages caused by such event in excess of seven (7) days; (iii) "boil orders", lack of potable water or lack of sanitary sewer services with respect to the Property in excess of seven (7) days; or (iv) any other cause outside of Tenant's control relating to such event (other than physical damage to the Property and Improvements (which shall be governed by the provisions above [casualty provisions of Lease])) which results in suspension of operations in excess of seven (7) days, regardless of the extent of physical damage to the Property or Improvements, then Rent shall be abated commencing with the eighth (8th) day of such suspension until such time as Tenant is able to reestablish operations on the Property, provided that Tenant makes commercially reasonable efforts to resume operations as soon as possible. The aggregate Rent so abated shall be paid to Landlord by Tenant in twenty-four (24) equal monthly installments together with the then current installment of Rent due commencing on the first Rent payment date following Tenant's reestablishment of operations on the Property.

SURRENDER

Every Lease should provide for the disposition and ownership of equipment, fixtures and property at the end of the Term thereof. However, because such equipment, fixtures and property in restaurants are more specialized and often more valuable than the racking or display cases of normal retailers, the surrender provision is often more heavily negotiated. A restaurant Tenant, particularly chains or franchises, may want to retain its equipment, fixtures and property to use at other sites, while Landlord may want to keep the premises as a restaurant for a future user and be able to afford a new tenant the benefit of the equipment, fixtures and property, particularly in a ground lease, where Landlord may contend that having a building for use as a restaurant at the end of the term was part of its bargain and determination of rent. A provision in a Lease which allows one party to designate certain items for removal at the end of the term is usually not deemed equitable by the other party, and therefore the issue should be addressed during Lease negotiation.

The concerns of both parties also extend to the removal of Tenant branding and identification. Unlike the equipment, fixtures and property set forth above, both parties are more likely to have similar interests with respect to Tenant branding and

identification, as Tenant will likely not want its trade names and dresses used by another party, and Landlord will likely not be able to use the same for the subsequent tenant. Additional issues, however, often arise in ground leases where the trade dresses of restaurant buildings involve more than signage and colors (i.e. prototypical and unique roofs or entry features). In that regard, the parties should address these items in the same manner as equipment, fixtures and property as set forth above.

CONDEMNATION AND EMINENT DOMAIN

Condemnation, eminent domain, or any other governmental or semi-private takings raise a number of critical issues in a restaurant ground lease. Two of the more important issues are determining what amounts to a total taking and the valuation of what is taken.

Perhaps more than any other use, a restaurant use is often adversely affected by seemingly minor changes in the premises or surrounding common areas. Even a small taking can have an enormous impact on sales and Tenant's ability to operate profitably on the Premises. To successfully negotiate a condemnation clause, Tenant's counsel must be sure to first understand the client's operational needs. For example, what is the minimum number of parking spaces that the client will need in order to operate profitably? What access points and drives will be critical to the client's operation? Where are the drive-thru and escape lanes located and why? Where are parking spaces located and why? Where is signage located and why? What are the critical site visibility corridors?

Once operational issues are understood, condemnation lease clause language should ideally provide that (a) any taking of parking spaces that has a material adverse impact on the operation of the business on the Premises or that cause the Premises to fall below the client's minimum critical parking needs should be deemed a total taking; (b) any taking which results in parking spaces below government requirements should be deemed a total taking; (c) any taking of a portion of the drive thru or escape lanes should be deemed a total taking; (d) any taking of a portion of the building should be considered a total taking; (e) any taking of critical drives or access points should be considered a total taking; and (f) any taking of critical signage or that adversely affects the visibility of the site should be considered a total taking.

Landlord's counsel will undoubtedly seek to take the discretion away from Tenant in determining what takings affect Tenant's business. A taking of any portion of the Premises on a ground lease which includes parking areas and drive aisles, would likely reasonably give rise to a Tenant termination right, as the essential nature of such areas was probably used in determining the scope of the land within the Premises.

However, with respect to areas outside of a ground leased premises or common areas for an inline lease, Landlord will want to designate certain common areas as "No Take Areas", the taking of which would give rise to a Tenant termination right.

Landlord will also want to reserve a termination right in the event of a taking so substantial that it wishes to raze the Development and construct a development of an entirely different nature (e.g. residential). While indeed, such provision may be offensive to a ground lease restaurant tenant, it may be more palatable if Tenant is one of many inline stores who are also being terminated.

In addition, Tenant's counsel must also consider the question of valuation in a condemnation taking. There is an inherent struggle between Landlord and Tenant in valuation issues over whether reimbursement for leasehold value will reduce the fee estate. A restaurant ground lease is generally long term (up to and in excess of 20 years). This often results in the fee value being determined by the leasehold value. However, Tenant's counsel must be alert to the fact that Tenant will have significant leasehold improvement costs invested in the site including utilities, site development, and building construction. Tenant's counsel must be prepared to seek lease provisions that permit Tenant to recover for any unamortized value of leasehold improvements, lost profits and business income, costs to rebuild and restore, and costs to relocate.

Landlord on the other hand must make sure that it can obtain the rents to which it otherwise would have been entitled but for such taking, as this constitutes Landlord's leasehold interest. While indeed the value of Landlord's fee in a long term ground lease may be diminished, Landlord is still entitled to such value as it may be determined, whether by appraisers or condemning authority. Also in a ground lease, Landlord may seek to have such value determined using improved land, arguing that the improvements were part of Landlord's bargain at the end of the term of the Lease. Tenant will object, arguing that it took the land raw and that it is only required to return it raw (see Surrender discussion). The negotiation as to the award also usually involves priority. In a long term ground lease, if the Lease is not terminated the award should first be used to repair or restore the Premises and the balance should be allocated *pari passau* based upon each party's interest.

INSURANCE

As in any lease negotiation, it is critical for Tenant to confirm with its insurance carrier that the insurance required by Landlord is available and affordable. As restaurants are susceptible to substantial damage from fire, property/casualty insurance will need to be at full replacement cost. Deductible amounts and limits are often negotiated by the parties, and the amounts Landlord will allow will, as in other types of leases, be commensurate with Tenant's financial status.

Many restaurants are franchises or chains where Tenant insures its operations and sites on a company-wide basis. Often, the company-wide program will include a set liability threshold for each restaurant location and a large umbrella policy that covers all locations and operations. Landlord will often require that Tenant increase its coverage for the location after a set period of time elapses in a long-term lease scenario or otherwise upon notice from Landlord. Tenant will always try to remove these provisions, as a Tenant with multiple restaurant sites will want to avoid if at all possible different

limits for different sites. Landlord is not likely to be concerned about Tenant's other lease locations, and therefore, may not be swayed. In the event Landlord requires more liability coverage than the company-wide program provides on a per site basis, or wants the right to increase policy limits during the term of the lease, Tenant should include a provision that the limits required can be satisfied through umbrella coverage. Additionally, Tenant may request a provision that limits any increase to no higher than what it pays for a majority of its locations.

Lastly, the Tenant should confirm whether any OEA or REA imposes additional or different insurance requirements. If this is not checked during Lease negotiation, Tenant could be surprised by additional expenses that must be incurred.

LAGNIAPPE (A LITTLE SOMETHING EXTRA TO THINK ABOUT)

As you can see, a Restaurant Lease is not just another retail lease. The following are just a few additional items to think about:

- Know your client's business. Nothing is more important for Landlord or Tenant counsel.
- Pay attention to the restaurant's proposed environment. Certain of the issues discussed above could be very different if the restaurant will be in an office building or if Tenant intends to operate a food kiosk on the street in a major urban area, for example.
- The law of mechanic's liens is complicated and varies greatly from state to state. Counsel should never negotiate a Lease clause regarding mechanic's liens without possessing a thorough understanding of the applicable mechanic's lien law.
- Mixed Use Developments are becoming very popular. Often, these Developments involve multiple condominium regimes. The restaurant tenant's counsel needs to carefully examine which condominium his client will be in and how taxes and operating expenses are allocated amongst the units and with respect to other condominiums in the Development. In such a property, Landlord may require additional controls over contracts entered into by Tenant to control pests, noises and odors and will want extensive discretion over the installation and operation of the grease trap.
- Smoking ordinances (the banning of smoking in public buildings) are also spreading throughout the country. In some jurisdictions, smoking is prohibited indoors but may be allowed in outdoor seating areas. In other jurisdictions, smoking may be allowed indoors, or it may not be allowed at all. If Tenant wishes to include a smoking section, the parties should specifically provide whether or not a smoking section is permitted if allowed by law.

- The ability of the Tenant to include an outdoor seating area should be specifically addressed in the Lease. Attention to local ordinances and applicable REAs and OEAs is necessary during Lease negotiation.
- Mall food court leases require additional analysis of issues relating to the shared elements like the seating area, trash receptacles and grease trap. Attention should be paid to the method by which Landlord is splitting the costs of these items among the various food court tenants. Landlord may also impose signage conformity requirements that could impede Tenant's ability to effectively use its standard logo.