

Leasing In a Mixed Use Project

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Mixed use projects have become increasingly popular in down town redevelopments. Leasing transactions in mixed use projects can be challenging if the lease form that is proposed was designed for a different type of use, for instance an office lease form offered for a retail use. Agents involved in such transactions should be aware of the issues that arise when the lease form is not appropriate for the intended tenancy.

Start by looking for inconsistencies in the “permitted use” clause of the lease. For instance, a check cashing business may be specifically prohibited in an office lease, but the proposed retail tenant on the ground floor may offer check cashing as an incidental service to its customers. Additionally, limitations on hours of operation may conflict and should be analyzed in the context of the use that is contemplated. Retailers often operate on weekends when office businesses are closed. Make sure that the use restrictions in the building or project do not conflict with the tenant’s intended business.

Operating expense pass-throughs warrant specific attention. Operating expenses that apply in office buildings are different than those that apply to retail properties. Common areas in office buildings often include lobbies, hallways, bathrooms, elevators and stairways. Retail tenants on the ground floor of an office building may not use any of these common areas, but if these areas are included as part of the CAM charges then the tenant may be subject to paying a share of these charges unless the lease is modified accordingly. Expenses for items such as janitorial services, elevator maintenance, and utility charges may also be inappropriate.

Additionally, limits on annual increases in operating expenses are handled differently in office and retail leases. Retail leases tend to distinguish between controllable and non controllable expenses and tend to place caps on the annual increase of controllable expenses (everything but property taxes, insurance and utilities). Office leases calculate provide a base rate per square foot for all expenses passed through to the tenant and the tenant pays annual increase over the base amount. Reconciling these two different calculations can be challenging if the landlord does not have the accounting systems in place to accommodate it. With creativity, however, a workable leasing solution can be negotiated.

Parking is another important clause to look at. Retail users rely on the ability of customers to visit their business and prefer to have parking within short distances from their store. The access to and from office parking garages should be considered within this context.

The rules and regulations in office buildings also vary significantly from those in a retail center. For instance, office tenants generally do not have the right to advertise their business on the exterior façade of the building. A retailer, however, relies on such signage to inform customers of their presence to generate foot traffic so the applicable lease provision may need to be modified.

This is not an exhaustive list of differences between retail and office leases. Depending on the lease form many other issues may need to be reconciled to ensure a successful leasing transaction.