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Reconfiguring Shopping Centers

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When a developer seeks to reconfigure a shopping center and such reconfiguration affects the anchor, it is not uncommon for disputes to arise. In this article, the author explains how the language of the reciprocal easement or lease agreement can create or help to resolve the problems.

As developers and shopping center owners seek to maximize revenue from shopping center properties, they may seek to expand or reconfigure a shopping center. Developers may decide to build more anchor stores, replace an existing anchor store with a different type of store, or alter the overall location and product mix of a shopping mall. The ability to expand or reconfigure a center may, however, be subject to contractual restrictions. A reciprocal easement agreement ("REA") or lease may restrict a developer from building proposed stores or reconfiguring a shopping center without the consent or approval of a particular anchor store. Anchor stores, whose concerns include traffic, access, visibility and parking, may enter into agreements with developers that contain significant restrictions on the developer and special approval rights for the anchor. When a developer is seeking to reconfigure a shopping center and such reconfiguration affects the anchor, it is not uncommon for disputes to arise. The first step of analysis is the language of the agreement.

Expansion Outside Plot Plan Footprint

In some cases, the language of an REA or lease agreement may be unambiguous. In *Belk, Inc. v. Warner Robins Zamias Ltd. P'ship*,[1] a mall owner and one of its anchor tenants entered into a lease, which required the owner to obtain the consent of the anchor tenant before constructing any building not shown on the plot plan. The plot plan, however, was amended to allow for a future store of approximately 70,000 square feet. The amended plot plan also stated the following: "Actual Configuration & Size May Vary[,] A Minimum of 5.5 Parking Ratio Will Be Maintained."

The court addressed the question: whether the anchor tenant could veto the construction of a proposed 101,298-square-foot department store because 70,000 square-feet represented the maximum limit for a proposed store. The court held that the construction of a larger store was permitted based on the language contained in the plot plan, which expressly provided that the actual size and configuration of the future store may vary, as long as the parking ratio was maintained. Consequently, the court concluded that the 70,000-square-foot figure shown on the plot plan was only an approximation. There were other provisions in the lease that forbid the construction of buildings beyond a certain square footage, which was not the case with the plot plan. Additionally, the emphasis on the maintenance of a minimum parking ratio allowed the court to conclude that the parties contemplated expansion beyond 70,000 square feet. Query whether this result was contemplated by the anchor tenant.

In another case, the court relied on practical business reasons for enforcing restrictions against reconfiguration. In *Walgreen Co. v. American Nat'l Bank & Trust Co. of Chicago*,[2] the court upheld an injunction against the lessor and a new tenant for the construction of a Fotomat kiosk in the parking area of a shopping center. Specifically, the lease required the landlord to provide at least 150,000 square feet of parking for at least 400 automobiles. Additionally, the retail store was obligated to pay a proportionate share of the cost for operating and maintaining the parking facilities based upon leasable area. The proposed kiosk was to be placed in a part of the shopping center which, in the plot plan attached to the lease, was designated as a parking area for the retail store. The retail store opposed the kiosk because it would have the effect of eliminating three parking spaces from the parking lot.

The landlord contended that the terms and conditions of the lease were not breached as long as the shopping center provided a parking lot with an area of at least 150,000 square feet and with space to park at least 400 automobiles. The landlord argued that the dimensions and boundaries of the parking area, drawn on the plot plan, showed an area in excess of 150,000 square feet. The landlord's position was that this area, however, was only descriptive and illustrative. Further, the landlord argued that the plot plan depicted spaces marked off which totaled 463 spaces while the plan's legend indicated parking for 400 cars. Therefore, the landlord asserted that the plot plan was ambiguous.

The court looked to the lease as to whether the situation clearly allowed for the rearrangement and expansion of retail stores in two specified areas: First, there was no provision made for diminishing the designated number of parking spaces. As such, the court held that the area intended to be used for a kiosk was not reserved for retail expansion.

Moreover, the area had been used as a parking area for over ten years.

In addition, the court considered business reasons for granting injunctive relief to the retail store. The shopping center was constructed around a central pedestrian mall, and each establishment operated to attract customers to the central core. The kiosk would have been separate from the mall and would not draw customers to the mall and to the other stores and could easily disrupt the established pattern of customer travel and use of the parking facilities. The deprivation of a property right, the elimination of parking spaces, and the potential disruption of travel constituted irreparable injuries.

Landlord's Right To Reconfigure

In *Hess's Dept. Stores, Inc. v. Ernest W. Hahn, Inc.*,[3] the court held that a lease agreement authorized the lessor to build a proposed addition to the shopping center. In this case, the anchor claimed that the owner of the shopping center breached the lease by agreeing to construct an addition to the shopping center consisting of another department store adjacent to the anchor, occupying space currently used for parking. In attempting to block the construction, the anchor argued that the following lease provisions were ambiguous:

> Section 5.1 *Common Areas.* Landlord reserves the right to change from time to time the size, location, nature and use of any common area, to sell or lease any portion thereof, and to make additional installations therein and to move and remove the same; provided that Landlord shall at all times maintain the [5.5 per 1,000] parking ratio.
>
> Section 5.2. Tenant ... shall have the non-exclusive right ... to use the common areas as designated from time to time by Landlord subject to such reasonable rules and regulations as Landlord may from time to time impose... Landlord may at any time close temporarily any common area to make repairs or changes, to prevent the acquisition of public rights in such area or to discourage noncustomer parking.

The anchor tenant attempted to argue that although section 5.1 purported to reserve to the landlord the ability to retain absolute control over the common areas and parking facilities, section 5.2 provided that the landlord could only close common areas temporarily. An additional anchor tenant occupying space that was formerly a parking lot would be tantamount to permanent closure of that common area. Therefore, the anchor argued that the lease created a reciprocal restrictive covenant that would prohibit the developer from interfering with the anchor's right to use of the parking areas and other common areas. The court determined that the two lease provisions were consistent, construing the two provisions to avoid a conflict; the anchor tenant had the right to use the common areas that exist and the developer had the right to alter the common areas.

Additionally, the anchor tenant argued that the proposed construction would adversely affect its parking, access and visibility. The lease, however, was silent with respect to access and visibility. With respect to parking, the lease required only a ratio of 5.5 cars per 1,000 square feet of leasable area. The proposed construction did not reduce the ratio below the required minimum. The court therefore rejected all of the anchor tenant's contentions and held for the developer, allowing for construction of an additional anchor tenant. From *Belk* and *Hess*, one might conclude that if an anchor tenant wants to restrict future development at the shopping center, specific language and/or a specific plot plan indicating strictly defined future permissible building areas might be the best means to accomplish that objective.

Expansion As Impacting Use Restrictions

From their facts, neither *Belk* nor *Hess* seems like difficult cases. Some leases, however, contain much more ambiguous language. Courts, therefore, are required to interpret the lease based on the mutual intention of the parties as it existed at the time of contracting. For example, in *Edmond's of Fresno v. MacDonald Group, Ltd.*,[4] a mall owner challenged a lower court's ruling, which permanently enjoined it from leasing premises in a subsequently built portion of a mall to a retail jewelry business. In a lease between the landlord and a retail jewelry business tenant, the landlord agreed to lease space to no more than two retail jewelry stores in the shopping mall. Years later, the mall owner formulated plans for construction of a new enclosed mall, which was to be linked to the original shopping mall. Approximately 80 percent of the new mall was to be situated on land within the original boundaries of the shopping mall. The dispute arose when the landlord indicated that it would lease space in the addition to other retail jewelers. The tenant argued this violated the lease, which prohibited the landlord from leasing space to more than one other jeweler.

At trial, the court found that the provision of the lease that limited the mall to two retail jewelry tenants was applicable to the expansion, as well as the original mall. In California, lease interpretation is a legal conclusion and not a factual one, which requires an independent interpretation by the appellate court. The court determined that the provisions of the lease failed to explicitly apply itself to the new addition, and simply stated: "Landlord agrees that there shall be not more than two jewelry stores in Fresno Fashion Square," which is the designation for the shopping center.

On the other hand, other provisions of the lease did include contingencies for expansion, which suggested to the court that the lease was intended to relate to subsequent development of the center. Article 2 of the lease provided that the landlord may "change the shape, size, location, number and extent of the improvements shown [on the site plan] and eliminate or add any improvements to any portion of [the mall], provided that Landlord...not change the size or location of the demised premises without Tenant's consent." Article 19 stated: "Should Landlord...acquire additional land not shown as part of [the mall] on Exhibit A [of the site plan] and make the same available for employee parking or other common area purposes, then said expenses...shall also include all of the aforementioned expenses incurred and paid in connection with said additional land." Finally, in Article 31 of the lease, "automobile parking and common areas" was defined to include "malls, and all common areas within [the mall]."

The court determined that articles 2, 19 and 31 were indicative of the lease anticipating expansion. More importantly, that tenant was obligated to pay its pro rata share of the common expenses for any additions to the center. These provisions read in conjunction implied that the lease incorporated any future development within the designation of the mall (Fresno Fashion Square). The court held that since the provision restricting space to two jewelry stores applied to the whole mall, then it must also be interpreted to apply to the new development.

The court also held that the restrictive covenant was applicable to the new development by California's implied covenant of good faith and fair dealing, which is applicable to every contract. Generally, the implied covenant requires that neither party do anything which will deprive the other of the benefits of the agreement. Actions that would cause one party to suffer reduced profits from the demised premises are sufficient to violate the covenant. In *Edmond's*, the court found it reasonable to assume that permitting a competitor to operate a competing business in the new mall would create additional competition for tenant and would ultimately cause a reduction in the benefits that the tenant would otherwise derive from the demised premises. More competition within the mall would obviously cause a reduction on benefits for the tenant.

Parole Evidence To Interpret Document Ambiguity

In *Busch Dev., Inc. v. City of Cheyenne, et al.*,[5] the Supreme Court of Wyoming addressed a dispute between two developers concerning a parking site in a shopping center. One of the developers ("Busch") had purchased land to develop into a shopping center, and sold a tract of the land to another developer ("Pacific"). As part of that development, Busch entered into an REA with Pacific. Pacific con-

structed a retail store. The tract which Busch purchased and developed was divided into four major portions: (1) Portion 1, anchored by Albertson's, was referred to as the "BDI Site" in the REA (this parcel was later conveyed to another owner); (2) Portion 2 of the tract was sold to Pacific, which comprised approximately 1.38 acres (a retail store was constructed on this parcel and was referred to as the "PCC site" in the REA); (3) Portion 3 consisted of the parking site adjacent to the retail store, and was referred to as the "Parking Site" in the REA; and (4) Portion 4 was a berm area, or outward perimeter surrounding the retail store's facility and the parking area.

The following provision of the REA was in dispute between Busch and Pacific:

> The respective owners of the PCC Site, the Parking Area Site and the BDI Site reserves [sic] and shall have the right, from time to time, without obtaining the consent or approval of the other owner of the Site, if any, to make any changes, modifications or alterations in its portion of its own site...however, it being expressly understood that the accessibility of the respective sites to pedestrian and vehicular traffic is not unreasonably restricted thereby. The respective record owners...shall each have a right of approval of any material changes in the Parking Area Site, which approval shall not be unreasonably withheld.

The dispute specifically concerned Busch's plan to construct pads, including parking for the pads on the parking site which Busch argued was a reserved right in the REA. Pacific, however, argued that the REA did not permit Busch to develop the parking lot area on Pacific's site without Pacific's approval. The court determined that the REA was ambiguous and therefore allowed parole evidence to be admitted. The court looked to recitals of the REA. Paragraph C of the recitals to the REA stated that Busch could construct additional buildings and other improvements on the BDI Site. Paragraph B, however, stated that Pacific intended to construct parking and related improvements on the parking site. According to the recitals, Busch reserved no right on the PCC site or on the parking site to construct buildings.

The court also looked to past dealings between Pacific and the retail store on the PCC site. In the past, Pacific supplied the retail store with at least 360 parking spaces for a 36,000 square-foot building. Yet, the pad and parking area for the pads proposed by Busch required as much square feet as the retail store. Moreover, the development of the pads would leave only 295 parking spaces for Pacific's tenant. Further, Busch did not indicate what type of businesses would occupy the buildings. The court decided that the development of pads could affect the amount and movement of traffic on the parking site, as well as the visibility of the retail store from the highway. The court concluded that the development pads would constitute a material change, which may not be accomplished without the consent of the record owners and that the owner of the PCC parcel did not unreasonably withhold its consent.

Reasonableness Standards

In many instances, an anchor tenant may have approval rights, but must be reasonable in exercising them. Courts have addressed the reasonableness of a tenant's decision to withhold its consent for a proposed development of a shopping mall. In *Leggett of Virginia, Inc. v. Crown American Corp., et al.*,[6] a lease entered into by a developer and tenant provided that in any instance requiring the tenant's consent or approval, it must be given in writing and "shall not be unreasonably withheld or delayed." The developer proposed to build a 140,000-square-foot store on the east side of the mall, requiring the developer to deviate from the original site plan. The original site plan allotted two spaces for future construction; one site for an 80,000 square-foot store, and the other for a 65,000-square foot store. The developer proposed to combine the two sites for a single store. The tenant rejected the proposal. The court was unable to find authority interpreting whether the tenant acted reasonably. It used the analogy of reasonable consent in connection with assignment and subletting. Citing the Restatement (Second) of Property § 15.2, which provided the following definition, "a reason for refusing consent, in order for it to be reasonable, must be objectively sensible and of some significance and not be based on mere caprice or whim or personal prejudice."

The court stated several factors are "objectively sensible and of some significance" for a tenant to consider. These factors include accessibility, visibility and parking. In this case, the court determined that the construction of a new store on the back of the mall would not harm the tenant's visibility. In fact, the tenant occupied the prime location in the mall.

Similarly, the new store would not adversely affect the accessibility of the mall because the same routes would still be used. On the issue of parking, however, the court found that the tenant had a reasonable basis with which to refuse consent. The court agreed that expansion would have an impact on parking. The absolute number of parking spots was less of an issue than the configuration and distribution of those parking spots. The original site plan had several parking fields, whereas the proposal showed a large parking field readily accessible only to the customers of the proposed store, not to the tenant's store.

Finally, the tenant argued that its main objection to the size of the proposed store was the tenant's ability to sell a wide range of merchandise. The court agreed in concluding that the tenant could not hope to offer the same selection and range of merchandise in its 68,000-square feet of selling space as the competitor could with its selling space. Although the developer offered to expand tenant's space by as much as 10,000 square feet, the court stated that such an expansion would be impractical for reasons of cost and profitability. The tenant did not usually expand stores within its first 10 years of operation, and tenant had only been open for four-and-a-half years. The tenant's decor and fixtures had not become obsolete. Furthermore, the developer would not bear the cost of construction or redecoration. These significant costs would have been the tenant's responsibility, including construction, engineering and redecoration. Based on these considerations, the court determined that the tenant was not unreasonable in seeking assistance for construction costs it would have to incur to accommodate to developer's plans to enlarge the mall.

Favoring Unrestricted Use Of Land

Although an anchor tenant may validly reject construction of proposed stores, in one case, the anchor tenant could not prohibit the replacement of an old anchor store with a newer anchor store in the same mall. In *Simon Prop. Group L.P. v. May Dept. Stores Co.*,[7] a dispute arose between two department stores in a mall and the mall's developer. Each department store had a separate REA with the developer, but there was conflict as to interpretations and application of both REAs. The REA with the first anchor provided that no vertical or later additions to the building would be allowed if the shopping center site was expanded by "the acquisition of contiguous territory and area" unless parties agreed to negotiate in good faith for the respective rights of expansion of their respective facilities. The REA with a second anchor provided:

> "No Party shall expand any Building, or construct any additional building...without prior written approval of each other party."

The developer and each of the two anchors entered into a Supplement to Reciprocal Easement and Operation Agreement, which provided:

> "Notwithstanding the respective dates of execution or recording of the [first anchor] REA and the [second anchor] REA, said [first anchor] REA and [second anchor] REA shall be deemed to be *concurrent and coordinate*."

The dispute over these REA provisions involved the first anchor's plan to replace its store at the mall with a new, much larger store. Note that the old store was not a direct competitor of the second anchor and the proposed new store would be such a direct competitor. Plans were established to raze the existing store and construct a new store in its place, using both the existing site and the site of an

acquired former trailer park. The second anchor, however, opposed the expansion on the grounds that the second anchor's REA with the developer prohibited expansion without its consent. The second anchor argued that the covenant rights set forth in its REA applied to the first anchor through the Supplement. The second anchor therefore sought injunctive relief against the first anchor's expansion.

The first anchor argued that the acquired trailer park constituted "contiguous territory and area," and that the first anchor only had a duty to negotiate with the developer in good faith pursuant to its REA. Since the two REAs were inconsistent, the issue centered on the Supplement that made the two REAs concurrent and coordinate. The court concluded that an interpretation of these terms would not resolve the issue and therefore looked to Texas law for guidance. Covenants restricting free use of land are in disfavor, but will be respected when confined to a lawful purpose and clearly worded. Ambiguities are resolved in favor of free and unrestricted use of land. Accordingly, this equitable principle was resolved in favor of the proposed new store.

Conclusion

In interpreting REAs and leases with respect to the expansion of shopping centers, courts will generally turn to the language of the agreement(s) at issue to determine if the provisions and terms contained therein are clear and unambiguous. If they are, courts will enforce the terms of the agreement as they appear. Careful drafting of lease or REA provisions with respect to configuration or future expansion may avoid ambiguities. If, however, the language is unclear or ambiguous, courts will look to the intent of the parties and allow the introduction of parole evidence, if necessary, to make a determination. In jurisdictions that recognize implied covenants of good faith and fair dealing the court may hold that such a covenant will apply to the case. If there is potential irreparable harm to one party, injunctive relief may be an available remedy. In such cases, courts may turn to business viability and other factors in determining whether an injunction against the construction against expansion or reconfiguration is appropriate. If a consent right is involved, a court's validation of refusal to consent may depend on many factors: those may include accessibility, visibility, effect on parking, and additional costs.

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[1] 251 Ga. App. 633 (2001).
[2] 4 Ill. App. 3d 549, 556 (1972).
[3] 901 F.2d 552, 555 (6th Cir. 1990).
[4] 171 Cal. App. 3d 598, 603 (1985).
[5] 645 P.2d 65, 67 (1982).
[6] 1995 U.S. Dist. LEXIS 6536 (W.D. Va. March 8, 1995).
[7] 943 S.W.2d 64 (1997).