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Exclusive Use Clauses in Shopping Center Leases

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Exclusive use clauses are not uncommon in shopping center leases. Tenants often request these clauses to prevent the landlord from renting space to other tenants who are competitors. Ideally, a shopping center includes a diverse mix of tenants that are compatible with, but do not compete with, one another. As such, landlords are not averse to granting exclusive uses to particular tenants, but both landlords and tenants have a number of factors to consider when negotiating such clauses.

A requirement for an exclusive use clause should be included in any letter of intent specifying the business terms of the proposed lease. This ensures that the parties do not waste time, effort and money negotiating a letter of intent or preparing a lease without such a requirement only to find that it is a deal killer later when the issue is raised. It is not necessary to negotiate the entire exclusive use clause in the letter of intent, but it should be mentioned as a requirement to be included in the lease, with at least a basic reference to the type of business the tenant wants to protect from competitors.

If a landlord or its affiliates own other retail centers nearby, a tenant can sometimes get the landlord to agree that the exclusive use clause will also apply to those other centers, usually within a limited radius around the tenant's location. This would also apply to future phases of a retail center under construction.

A tenant which is a national or regional company like a grocery store or pharmacy chain will routinely require that it be granted an exclusive use. As a prospective anchor for the center, the company will be paying significant rent and potentially attracting a lot of customers. An anchor tenant therefore has the leverage needed to induce the landlord to give it an exclusive use clause. The anchor tenant will often have its own exclusive use clause to include in the lease, and it will be reticent about negotiating it.

Tenants normally want the exclusive use clause to be broad and include as many uses as possible that will compete in any way with their business. On the other hand, landlords prefer the clause to be as narrow as possible to avoid limiting the types of other tenants in a center. There will usually be

a fair amount of give and take as an appropriate clause is negotiated.

If the tenant's use is very narrow, it is fairly easy to identify the nature of the competition being precluded. The more products or services the tenant offers, the more comprehensive and detailed an exclusive use clause becomes. In any event, the exclusive use clause should cover what are considered the "primary" products or services offered.

It is important to both parties that the exclusive use clause be clear and concise. It should also not inadvertently preclude businesses that do not actually compete with the tenant desiring the exclusive use. For example, a liquor store selling beer, wine and alcoholic beverages for off-premises consumption may wish to preclude other businesses in a center from selling those products. If the other business is a restaurant or bar offering those products to customers for on-premises consumption, there is no actual competition.

At times, it is helpful to identify specific competitors as being included in the list of businesses that the landlord will not permit to operate elsewhere in the center. Many tenants have a pretty good idea who their primary competitors are, and while such a list may not be exhaustive, it can be illustrative of the types of business being prohibited.

Before agreeing to an exclusive use clause in any lease, a landlord needs to know that its other existing tenants have leases that contain relatively narrow permitted uses that do not compete with the new tenant's business. If an existing lease says that the tenant may operate its premises for "any lawful use," then that tenant may start out with one use but convert it later to another. Alternatively, the tenant may be entitled to assign its lease to a new tenant with a different type of business. Landlords will not want these events to trigger a default under an exclusive use clause granted to a subsequent tenant since the landlord cannot control what the prior tenant may do with its premises unless the prior tenant's lease grants the landlord approval rights over a future use. Landlords should be careful to maintain accurate records of permitted uses and exclusive uses under all leases that can be referred to and updated each time a new lease is negotiated.

Likewise, the tenant with whom an exclusive use clause is being negotiated should not have the flexibility in its lease to change its use in the future to "any lawful use." Future prospective tenants could be deterred from leasing at the center if their business would compete with an existing tenant's new or changed use.

It is helpful to record notices among the public records specifying exclusive uses granted to tenants. This is usually done using a Memorandum of Lease. All leases should require the tenant to comply with recorded covenants and restrictions on the title to the center. This would include any recorded document granting an exclusive use to a single tenant. If this is done and all exclusives are recorded, then it would not be necessary to specify in every lease what all the exclusives are in the entire center.

Exclusive uses should be for the duration of the applicable lease. Sometimes notices of exclusive uses (even in a Memorandum of Lease) that are recorded in the public records merely state that no other tenant will use its premises for a particular type of business, but they do not say how long that restriction lasts. If the lease with the tenant to whom that exclusive was granted has terminated or expired, the exclusive use should automatically terminate.

A tenant with an exclusive use clause will expect the landlord to use reasonable efforts to enforce the clause if another tenant operates a competing business that is covered. Landlords who don't comply may be found in breach of the affected tenant's lease. Since a contractual agreement with the competitor doesn't exist, the tenant usually can't bring a legal action against its competitor. The tenant's only remedy is to make a claim against the landlord under the lease.

The affected tenant should be able to require the landlord to enjoin a competing use by getting a court order requiring that it cease. This can take time, so the affected tenant will also want other remedies, such as the right to terminate its lease and recover damages or to keep its lease in effect and reduce its rent by an agreed upon amount (even if based on a formula). Damages may include the tenant's investment in the leased space and relocation costs if it terminates the lease. It may also be possible to recover more if a new and equivalent space elsewhere costs more to lease.

For the tenant, the remedies should include damages in an amount which is significant enough to deter the landlord from deliberately breaching the exclusive use clause. If not, the landlord may breach it simply because enough additional rent from the competitor can be obtained to cover damages to the affected tenant. Additionally, a tenant's damages should be great enough to deter the landlord from deliberately breaching the exclusive use in order to relet the space, even if rental rates go up significantly. Otherwise, the higher rental rates will provide the landlord with extra funds sufficient to cover the low damages.

The bottom line is that exclusive use clauses present multiple issues that require careful consideration in negotiating and drafting, yet they usually get less attention than they deserve. This article is intended to provide only an overview of the subject matter and does not address all the issues that can come up when addressing exclusive use clauses. It is therefore important to consult with an experienced real estate attorney when negotiating such a lease.