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PERSPECTIVE

Pop-up retailers: A landlord's perspective

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As department stores continue to struggle and exit malls across the country while pop ups are taking the world by storm, mall operators are taking notice. Pop-up shops are temporary retail spaces, ranging in duration from one day to a year, that test new products and boost brand awareness. Once a solution to filling vacancies, pop-ups are now a part of some malls' strategy to attract new and returning shoppers. In Los Angeles malls like Westfield Century City and the Grove have devoted permanent space to pop-ups.

Given the unique nature of pop-up shops, there are a number of legal considerations including: the type of relationship, i.e., lease or license, use, rent, improvements, and insurance and indemnity that should be considered by landlords before entering into the relationship.

Lease vs License

Pop-up retailers come in varying shapes and sizes, so landlords should vary the type of agreement they reach with a prospective pop-up tenant based on the size and needs of the tenant. For a longer term retailer, a more traditional lease agreement provides the landlord with stability by treating a popup tenant like a long-term occupant with respect to financial responsibility for contributions to common area expenses and insurance and indemnity obligations. In contrast, a landlord should consider utilizing a license agreement when renting smaller space to short-term retailers. A license generally allows an owner to terminate the relationship, upon short notice to the licensee, if the pop-up shop is unsuccessful or if a long term tenant becomes interested in the space.

Simply naming an agreement a lease or a license does not make it so. As such clarity and precision in drafting are essential in order to avoid unintended consequences.

Use Clause

From the landlord's perspective the "use clause" should restrict the tenant to using its premises for a specific purpose, clearly defining how the space can and cannot be used. Before entering into an agreement with a pop-up tenant, landlords should review other existing long-term leases at the property to ensure that the pop-up's proposed use does not violate any existing tenants' exclusive uses or otherwise interfere with the operations of the long-term tenants. Landlords may want to consider revising leases with long-term tenants to include language in their exclusive use provisions that provides an exception for uses by pop-up retailers.

The governing documents should make the tenant responsible for any due diligence necessary to confirm that the proposed use of the premises is permitted by applicable zoning and municipal regulations.

Rent

Start-up pop-ups are generally more concerned with visibility than profit when introducing a product, so landlords with more bargaining power should require rent in a fixed amount to minimize losses. Landlords should also carefully access the specific site needs of a proposed pop-up, including possibility of excessive utilities costs or additional security needs and structure the deal accordingly.

For pop-ups involving high-profile brands with a track record of financial success a percentage rent structure, based on the tenant's gross sales, may be a better option. Because the items included within the definition of "gross sales" impacts the amount of percentage rent to be paid by the tenant, landlords will want to broaden the definition as much as possible, including online sales within the definition. Leases containing percentage rent clauses should also contain an anti-partnership clause disclaiming any partnership between landlord and tenant.

Build-Out and Alterations

Landlords should not compromise the long-term marketability of a space due to use specific alterations requested by a pop-up tenant. As such, the license or lease should require a tenant to seek the landlord's approval before making any alterations to the premises as well as require the tenant to restore the space to its original condition upon termination of the lease or license term. Landlords should also avoid extending concessions or allowances for build-outs or improvements to tenants occupying the space on a short-term basis.

Insurance and Indemnity

Even if the pop-up retailer is only operating for few hours a day it is essential that the tenant has appropriate insurance, including at a minimum, commercial general liability and worker's compensation insurance. Landlords with more bargaining power can require the tenants to carry employer's liability insurance and business interruption insurance, representing loss of at least approximately six months of tenant's income for longer term tenants. Some landlords carry the additional insurance and pass the cost down to the pop-up shop as part of the rent.

The governing documents should further require the tenant to indemnify and hold the landlord harmless from all losses and liability (including costs and attorney fees) incurred by reason of (a) damage to property or injury to persons occurring on the premises or caused by fault or neglect of the tenant and (b) tenant's failure to comply with governmental laws, ordinances, and regulations applicable to the condition or use of the premises during the occupancy.

The pop-up concept appears to be here to stay. Considerations regarding lease or license agreements, use and applicable laws, and insurance will go a long way toward ensuring a successful landlord-tenant relationship.

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