



# Real Estate Resource Guide



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## Purpose

For both existing and startup co-ops, this guide will help:

- Identify key points in decision making to help co-ops make better real estate decisions
- Identify key external resources needed to develop and execute real estate decisions
- Develop a process to decide a store concept and site criteria
- Develop an appropriate strategy and plan to secure an appropriate site

This guide covers the timeframe from initial concept planning until the site is secured, and covers only issues related to real estate.

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*Developed by Food Co-op Initiative, CDS Consulting Co-op, National Co+op Grocers and NCG Development Co+op.*

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# Introduction and Goals



Congratulations! Your co-op is beginning its journey into the increasingly competitive world of grocery retail real estate. From a real estate development perspective, you have an exciting product for the market — a community-owned business that helps support local agriculture, natural and organic foods. You could be a stable keystone asset for the right retail development. And it's likely that your co-op will face competition for prime locations from other grocers, many of which have access to in-house market research and development teams as well as capital that can be allocated quickly. It's your job to build your own resources to secure a site quickly and effectively with as little risk to your organization as you can.

Rest assured there are professionals who can and should help guide you through this process; your new location, and how it is secured, may be the single largest investment the co-op will ever make. You can go back and fix lighting, shelf placement, merchandising and pricing, but your real estate choices — the location you select and how you finance and secure it — will last many years, so it's important to get it right. This resource guide is intended to help introduce core concepts for successfully securing a site.

## Goals

This guide seeks to clarify the tools and resources available for food co-ops to efficiently secure and develop the physical space needed for their store. In an increasingly competitive grocery market, the need to design and build an attractive facility in a location that easily serves a growing shopper base and can attract new customers is more important than ever. As with any retail business, a co-ops' location is either a strategic advantage or disadvantage in its success.

Due to the complexity and competitiveness of the current marketplace, it is best to work with experienced real estate professionals to ensure the best result. In this light, for both existing and startup co-ops, this guide will:

- Identify key points to help co-ops make better decisions,
- Identify key external resources needed to develop and execute these decisions,
- Create a process to decide on a store concept and develop site criteria, and
- Develop an appropriate strategy and plan to secure an appropriate site.

This guide covers the timeframe from concept development until the site is secured and covers only issues related to real estate, and assumes:

- A strong board and solid governance is in place,
- For existing co-ops, a general manager (GM) that is operationally established and stable in that role,
- The co-op has the time and financial ability to both invest properly in due diligence and planning, and to invest in the physical infrastructure of a store, and
- The co-op has the operational capacity to run a larger store.

This guide treats the process in three major steps:

1. Organizational alignment around clear goals and expansion concept,
2. Site search and selection, and
3. Securing a site.

# Getting Ready: Development of Vision, Goals and Alignment



## Concept Development and Real Estate

When your organization is ready to start planning for a new store, there are plenty of questions to answer before you begin the search for the right location. While a mission statement might answer the question *why*, the process of concept development requires you to identify specifically *who you want to serve and how you want to serve them*. These answers will influence the location, size and format you choose. A food co-op that wants to fill a need in the market for quick, healthy prepared foods may require a different size and location than a full-line grocery store that is convenient for the entire community, or a neighborhood store targeted to a specific community. Clearly answering these questions at the outset is important, as it will affect many decisions down the road. The answers to *who* and *how* will drive your location search, the retail and non-retail concepts you wish to include in your store, and the tradeoffs the team is willing to make as you move through the process.

The *who* could include:

- long-time owners of the co-op,
- specific groups of people within a larger community, or
- the entire community, especially in small towns or urban areas with limited access to healthy foods.

The *how* includes both retail and non-retail concepts and could include a focus on:

- healthy food at a reasonable price for the community,
- a full-line grocery store that resembles a one-stop traditional grocery experience,
- being a welcoming and inclusive place for people/communities that may be unfamiliar with either the cooperative model or the products being offered,
- convenient, ready-to-eat prepared food options for families on-the-go, or
- including teaching kitchens or community meeting spaces to help support the mission of the co-op.

Consider not only how to appeal to the most dedicated, core shoppers, but also how to expand the co-op's appeal to occasional or casual grocery shoppers. Choosing a location that makes it easy for new shoppers to find you, and a concept and merchandising strategy that makes these new shoppers feel welcome and comfortable, will help grow the co-op community and sales.

As you consider your options for retail concepts, establish a clear set of priorities for what is most important and also less vital to the success of the co-op. Because you will have to make tradeoffs as you move forward with your project, clear priorities early on will provide a good roadmap for your project team.

### **Building Team Alignment and Project Parameters**

One of the most important tasks early in the process is making sure that the board and general manager (GM) (or person responsible for the search) have strong alignment around the co-op's priorities and needs. This will help guide the search process, providing guardrails or parameters for the project and clarity for all participants. At this point, two key parameters will help guide decisions on the type of real estate interest you are looking for and how you will conduct the search: timing and financial.

In terms of timing, co-op management and board must clearly understand whether there are any time constraints that may drive decisions, either quickly or at a slower pace. Understanding constraints like an expiring existing store Lease, pending option renewals or limited funds available for a search may necessitate making compromises on the site choice in the interests of time. For example, a co-op with an expiring Lease may be willing to make some compromises to get into a new space, or decide to move toward a Lease in an existing building rather than choosing to work with a new ground-up development. Without such constraints, a longer search time frame may result in a more optimal site and better long-term results.

For the financial criteria, co-op management and board should decide on how they plan to assess financial viability of the project, or to choose between scenarios. Some metrics could include:

- Co-op funds at risk
- Amount of capital needed from members, or funds from existing operations
- Debt Service Coverage Ratio (ability to pay back debt)
- Days Cash on Hand (minimal cash flow)
- Return on Investment (especially if comparing different investment options)

Moreover, an existing co-op looking to add a new location would want to discuss what, if any, of its existing assets it would be willing to collateralize to finance the new store. Financial models should guide the co-op toward a scope that will ultimately be feasible to finance and build.

### Lease or Purchase: Type of Development for the Co-op

One of the most important considerations that should be addressed within and guided by your pro forma is what type of development the co-op will move forward with — a lease or a purchase. This historically has been (and continues to be) a highly debated subject for many co-ops.

In general, a real estate purchase is more expensive and often comes with more risk than a lease. However, to the extent that the co-op can afford the purchase and development of a store, other considerations should be weighed: How stable are the co-op's operations, board and ownership? How stable is the real estate market in that area? How well can the site accommodate future growth? Is the development team strong enough to be able to mitigate

development risk often absorbed by others? Purchasing land and building should be viewed as an additional long-term investment, over and above normal interior buildout, fixtures and equipment needed for a grocery store. With that additional investment comes risk as well as the potential for financial reward.

Many would argue that most of a co-op’s assets should go toward running great grocery stores, not great real estate assets. A good landlord can be a great partner to help defray capital cost and development risk to the co-op and to leverage established local design and construction resources. Because leases require less capital outlay and are less risky and more flexible, this is the route chosen by most national grocery retailers.

That said, each co-op should consider both its own needs and abilities, as well as any specific sites for this discussion. There are times when a purchase makes sense and others when leasing is the preferable option. Timing plays a role, too, as there are opportune times for buying and leasing within the market. The table below helps lay out a few considerations for such a discussion:

<b>Lease or Purchase: What type of development is right for your co-op?</b>		
<b>Option</b>	<b>Pros</b>	<b>Cons</b>
Lease	<ul style="list-style-type: none"> <li>• Less to finance</li> <li>• More assets going to running a grocery store</li> <li>• Use of Landlord as a financing partner for some improvements</li> <li>• Less development risk</li> <li>• More flexible in long-term</li> </ul>	<ul style="list-style-type: none"> <li>• Harder and more expensive to finance leasehold improvements</li> <li>• Lack of real estate asset value growth potential</li> <li>• Less collateral</li> </ul>
Buy	<ul style="list-style-type: none"> <li>• More control of site and building</li> <li>• More favorable bank financing due to real estate collateral</li> <li>• Perception of permanence within community</li> </ul>	<ul style="list-style-type: none"> <li>• More expensive</li> <li>• More development risk</li> <li>• Ties up capital in illiquid real estate and building assets</li> <li>• More difficult to relocate if market shifts or co-op needs more space</li> </ul>

Here are a few types of development options, listed in order of increasing investment (and risk):

- **Lease — Existing Building:** The least risky and least costly type of project for both co-op and Developer/Landlord. While it does not come with all of the benefits (and burdens) of ownership, the right Lease can still confer many of them.
- **Lease — Build to Suit:** A Lease scenario in which the Landlord builds a more customized building for a Tenant. Riskier from a Landlord's perspective, especially with an untested Tenant, because it requires more investment but also leaves them with a potentially less flexible space to lease in case of a business failure. Just the same, for an established operator, this can reduce capital outlay for both land and building for a Tenant while still getting a custom building.
- **Land Purchase — Fee Developer or Design/Build:** A co-op can purchase the land (or ground lease) and hire a Developer to coordinate the design, approval and construction of a space for a fee. This can be a good way to marshal and coordinate resources quickly and efficiently.
- **Land/Building Purchase — Self Develop:** Co-op purchases land and contracts and internally coordinates design, approval and construction. This works best with some prior experience, but internalizes all capital and development risk through the process.

### Other Scope Parameters

A few other types of parameters for your project that would be guided by the pro forma should be set early on with the board, GM and executive team. Issue areas that will be useful in guiding the search could include:

- **General building and retail size:** While the type of development (buy vs. lease) will affect the capital available to build your store, your market study and financial model steer the size of space you search for by providing sales and operational inputs to ensure financial feasibility.
- **Location and site criteria:** In an increasingly competitive natural and organic grocery market, these criteria are becoming more important for co-ops to consider. It's no longer enough merely to provide the space, it's important that it be visible and convenient. Cheaper but out-of-the-way or invisible locations have started to present real financial problems for some co-ops. Accordingly, you should decide what compromises you may be willing to make, and which you cannot make. Define goals for traffic, visibility, parking and other criteria that your team has for site selection, and understand how you will weigh them.

- **Social criteria:** Some co-ops, either as a core or secondary selection criterion, may include social criteria, such as serving an underserved population, cleaning up a dirty site, or revitalizing an area. Going in, know that these efforts can be risky and accordingly take much more planning to be successful. They may cost more, and may result in a lower sales threshold. Areas undergoing revitalization may have vacant spaces or ongoing construction projects, either of which can be planned for, but can still make it more difficult to attract new customers. These kinds of opportunities may also bring local, state or federal financial incentives to help offset some of the risk. All the same, if social criteria are part of your parameters, it should be clear to the team whether these are primary or secondary considerations.

### **Role Definition and Communication**

With clear guardrails set by the board and management for the search, clarifying the roles of the search team and guidelines for communication are next. These are critical aspects of any pre-search work, and any organizational relationship or decision-making issues should be addressed before beginning the actual search.

Clearly determine who is doing what on the search, as well as how and when updates will be provided to the board. An established co-op will likely use the GM and/or someone else from the executive team to take the lead role in the due diligence, search and development process and reporting to the board.

At a startup, the board may fill the lead role with a designated board member, a paid project manager, or a committee that combines board members and a paid staff member. While any of these can be effective for a startup, successful startups would generally not involve the full board in the search, and the search members would have clearly defined roles.

To establish clear roles, responsibilities and communications processes, discuss how the team will:

- apprise members of the search team on progress,
- apprise the board on how the search is progressing,
- secure the services of the professionals you'll use in the search, and
- obtain signatures on Letters of Intent, Leases, Options to Purchase and/or Purchase Agreements.

## Real Estate Decisions in Startup Co-ops

Startup food co-ops have some special considerations in delegating responsibility and authority for real estate decisions. They may have a project manager or other employees on board, but rarely an expert in real estate. Here are some of the possible scenarios:

### **Project Manager**

Project managers hired to build ownership levels or conduct capital campaigns may have a good understanding of the owners' needs, but are not likely to have experience in site selection and negotiation. They are rarely the best choice to lead real estate analysis.

### **General Manager**

If a general manager has already been hired, it is tempting to turn over the real estate process to her or him. The skill set that a startup food co-op needs in a general manager is broad and usually the ability to organize a new staff, prepare for and conduct operations are the most critical. Real estate and construction are generally better handled by a project manager with those areas of experience.

### **Board Member**

Board members are often excited about finally choosing a site and having something concrete to show co-op owners. There is a real temptation to be a part of the site selection and negotiations. However, this excitement can sometimes cloud judgment and lessen critical analysis. If the board has one or more members with professional commercial real estate experience, then they may be potential candidates. Working with outside experts is still a good safeguard. Be especially cautious if any board members have a personal interest in any of the properties being considered. The relationship among the board members leads to trust and potential to be less critical in analyzing the options. The member with the conflict of interest should recuse her/himself from all real estate discussions and decisions, and the support of an outside professional will be essential.

### **Committee Members or Volunteers**

Site selection committees are commonly formed by a startup board to research options and propose sites for further consideration. Such committees should be well-versed in the characteristics of a good location and site that could fit the co-op's plans. Ideally, the committee's role should be restricted to identifying properties with potential and turning over that information to the site selection lead. They should not become involved in direct negotiations which are generally handled by the co-op's broker, attorney, or both.

### **Implementation Project Manager with Professional Support**

The ideal situation is for the co-op to hire or contract with a project manager specifically responsible for Stage 3 Implementation. This role typically would include site selection leadership and coordination of buildout activities. The implementation project manager works closely with the board and the general manager, once present. The board should define clear limits of authority and expectations for reporting and approvals. Ensure that the process is transparent, well-understood and fluid. Decisions cannot be delayed by excessive review and approval processes. Depending on the experience and qualifications of the implementation project manager, the co-op will probably still need to hire professional support for lease or purchase negotiations and legal review.

### Confidentiality

It is also important to address the issue of confidentiality in communications. It will be no secret that a startup co-op is looking for a location. However, it may not make sense for an existing co-op to publicize that it is looking for a site. Whether this is a startup or existing co-op, discussions or considerations on any specific site should be dealt with confidentially, in Executive Session, with information on any specific site released to co-op owners and then to the public, *only after the site has been secured* with a Lease, a Purchase Option or agreement. At that point, your project will most likely be more fully fleshed out and you may even have renderings to show. To publicize earlier could compromise negotiations and disappoint your owners if the site falls through. Even after a site has been secured, certain real estate and site-related information should remain confidential.

### Getting a Market Study: Testing for Market Feasibility

Once you have agreed upon a store concept and know whom you would like to serve, a market study from a reputable analyst can help determine:

- the ideal location(s), area, or intersection to site your store, and
- how much you might expect in top line sales from a store at that location. This will generally reflect the market opportunity in that area, but actual performance will be strongly influenced by some of the locational and site attributes described later, as well as your execution of the store concept.

The sales forecast predicted by the market study is impactful for a number of reasons. First, it establishes whether there is actually a market for your specific store concept. Second, after appropriately discounting sales within your pro forma, this sales estimate is one of the first big indicators that helps determine overall project financial feasibility. Based on the sales forecast, the project team may need to revisit decisions around type of development, size or other criteria, and make appropriate adjustments. This is not uncommon; depending on the sales forecast, the team may decide that the project is not feasible, or may need to adjust some of the project parameters to make the project workable.

Remember that the top line sales number is an estimate, and your financial projections should be discounted accordingly. A market study will make certain assumptions around visibility, parking and operations that are important to pay attention to — if these assumptions are not achievable, adjust top line sales numbers accordingly.

As the team moves forward with the site search based on your market study, you may update the study to reflect the sites under consideration. Sites nearby the recommended “ideal location” likely will not change sales significantly, so long as primary site characteristics (e.g., visibility, access, parking, size) do not change appreciably. If a site you are considering doesn’t have each of the characteristics that are assumed, consult your market researcher on changes to the estimate, or to update sales to conform to realities on the ground.

## Developing a Plan and Timeline

Assuming that you have a viable concept (either as conceived, or adjusted based on your market study), it is time to start developing a plan and a team with well-defined roles. When you begin to investigate sites, you will need to act quickly and credibly. That means having a team in place to begin due diligence for a site, with a plan for how this will be accomplished. As you put together the team outlined in the next section, talk to each potential member about the goals for the project, and how quickly you would like to move in due diligence and securing a site; seek the team’s feedback on the feasibility of your anticipated timeline; and ask whether they have the capacity to move at that pace. Further, ensure that you clearly understand the amount and timing of their fee structures to make sure it fits within your budget.

## Building Team for Site Search and Selection

Your competitors are hiring the best in the industry to search for sites, secure real estate and build stores as quickly as they choose. The co-op will achieve better and faster results with a strong, communicative team. As you plan for the site search, being well prepared in terms of business and financial planning fosters credibility with potential financiers and land partners. Assembling a strong team to search and develop strong options is doubly important in helping to showcase the co-op’s vision to the development community. This section will give you a quick overview of the types of skills and partners the co-op will need for this phase.

### Broker

Brokers can serve as the bridge to the development community, connecting you with the appropriate landowners, developers or landlords that may be interested in your concept. Your broker should have substantial experience in commercial real estate development, and better yet, grocery experience. Markets vary, but lease brokers’ commissions are typically paid by the Landlord, not the co-op, especially if you’re going into an existing space.

A broker is also invaluable in providing:

- information on space/properties that may not yet be on the market, which is useful both in hot and cold markets,
- market-specific pricing information for both land or lease space,
- information on some of the deal points that you'll review in the LOI/Lease or Option to Purchase/Purchase Agreement; these are often as important, if not more, than the actual price paid for a lease. Your Landlord or seller will in all likelihood have a broker with all of this information, and you're negotiating with a large information asymmetry without one, and
- professional representation with your potential landlords/sellers. Transactions are often helped along by utilizing two brokers who are less emotionally attached to your business or individual deal points.

### Attorney

A good real estate attorney is invaluable during a Lease negotiation, and can provide some guidance during site due diligence for any option/purchase, and during the run up to a Letter of Intent (LOI) for a Lease. Ensure that your attorney has extensive real estate development experience, as they will be involved in many finer deal points that the co-op's general business attorney or someone without real estate experience may miss.

### Financial Planning

The co-op needs financial expertise both for business modeling — understanding the nuts and bolts of running a grocery store — and for preparing for the planning of your facility. In-house finance managers or out-of-house consultants like CDS Consulting Co-op, Food Co-op Initiative and National Co+op Grocers' Development Co+operative, can each provide some or all of these services. For the facility, they should continue to update financial estimates throughout feasibility, examining different Sources (Financing) and Uses (Budget) options. For the site search, your pro forma should include future operations, as well as the most current real estate scenario that includes an updated project budget, reasonable financing assumptions and occupancy costs that reflect what your broker estimates the co-op may expect to pay.

### Project Costing: General Contractor or Cost Estimator

A co-op should work with a partner to provide reliable costing information for different scopes of work. Equipment estimates may be provided by entities with equipment/store planning

expertise (see below). Construction cost estimates can come either from a cost estimator or a general contractor:

- A cost estimator is generally a fee-for-service entity that can help provide rough unit costs to build a budget or help advise on the cost to build something from drawings. Working with a cost estimator would be acceptable for a site selection, but would require the future hire of a general contractor, who would provide their own budget.
- A general contractor (GC) may or may not charge for estimates within this phase of work, especially if they anticipate getting a bid out of the estimate. You may avoid having to pay for an estimate twice if you choose a GC now, but the relationship and any fees should be well understood by both parties to avoid unexpected fees. It may be early to officially hire a GC at this point, but they should be looked at as another costing resource.

### Site and Building Design Professionals

Depending on the type of development (i.e., existing building versus new building), the team will need to develop:

- an effective and competitive conceptual store floor plan,
- an effective and competitive conceptual site plan, which would show the store footprint as well as accommodations for both customers' needs (visibility, ingress/egress and parking) and store operations — trash, baler, delivery and truck movements, cart corrals and employee parking.

Several types of professionals can help in different ways on this. During this due diligence phase, you will need a store planner — a professional with experience laying out grocery store interiors — to ensure that an effective interior store plan is developed. Depending on whether it is the co-op's responsibility (or a Landlord's) this person may also be able to lay out your conceptual site plan. The right architect or civil engineer should be able to produce a good site plan, while also ensuring that trucks can maneuver appropriately for deliveries. All of this should be checked before closing on any land or lease.

As the team moves into the design and construction phases, architects and engineers (you'll see the term MEP for Mechanical, Electrical and Plumbing often) will be needed to design the space. They could be hired by the co-op or by your designer/builder or a Landlord/Developer. These services are not generally needed during this due diligence, however.

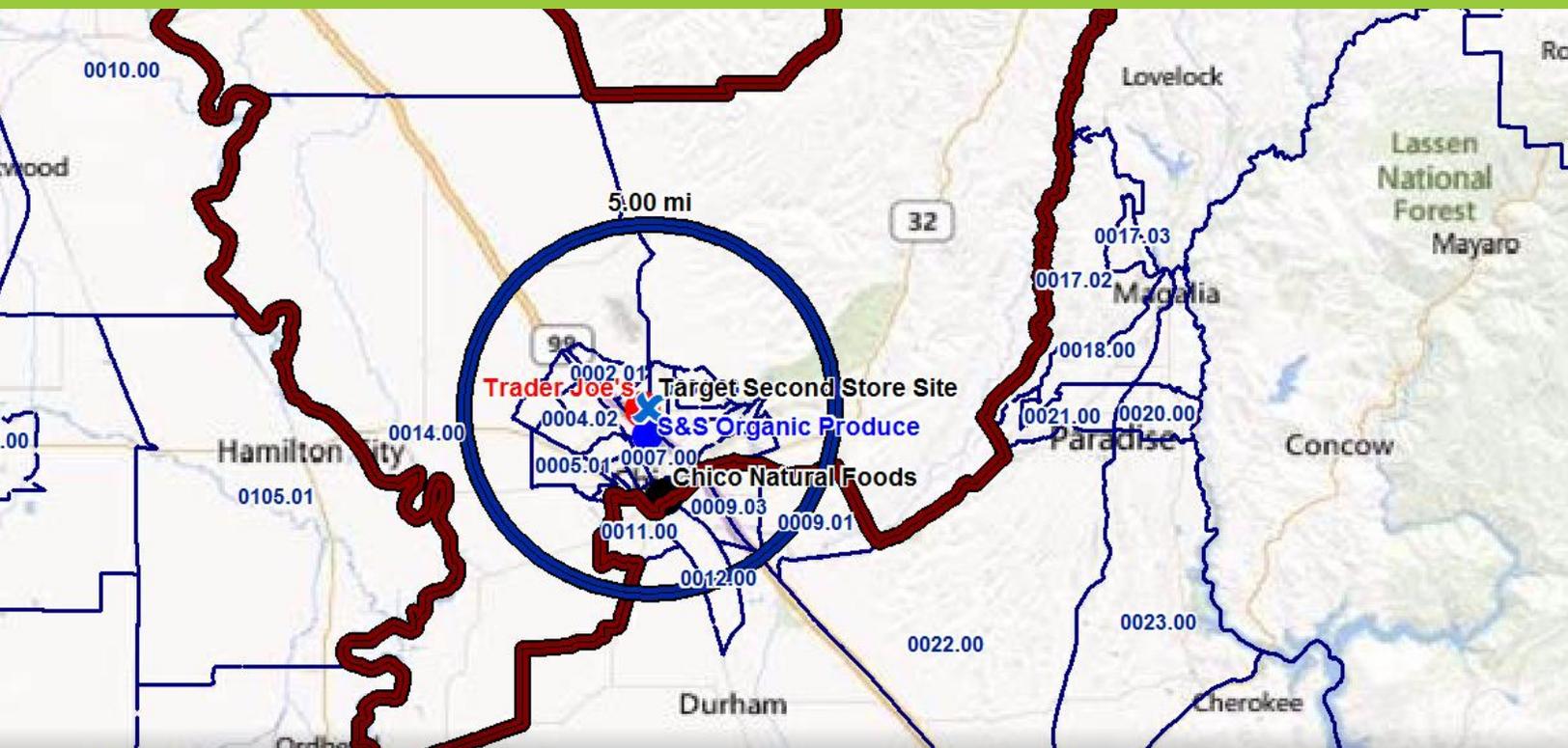
### Co-op Grocery Consultant

When assessing the strengths and weaknesses of your organization and its ability to develop vision and goals, to develop a plan, and to search and secure a site, there are elements specific to grocery co-ops that some of the above professionals may not have experience with — either specific to natural foods retail or to cooperatives. Each of these elements brings certain unique requirements to the planning, search and securing of real estate. This guide specifically aims to assist but not substitute for the guidance of organizations like NCG, FCI and CDS.

## Planning with the Team

When you begin your search, it is helpful to know how long due diligence for a site will take. Talk to each of the parties above and ask what they need for their due diligence, and how long it will take (e.g., a site survey and building survey for the site and store planner, requiring three weeks to get to a conceptual plan). Build an understanding of dependencies (e.g., cost estimator needs to see the current conditions and the designer's site plan before estimating site work costs), and then work together to build a work plan with goals and timelines, or an understanding of how they will work together.

# Site Search and Selection



Armed with a market study, a planned concept, a conceptual budget and the right team for due diligence, it is time to start talking to your broker about what's available on the market. Take the time to find out what market comparables (i.e., comps) for retail or grocery space are to verify your pro forma assumptions and to build an understanding of the types of tradeoffs that may have to be made either in price, location or otherwise.

When you start to look at sites, there are two types of attributes to consider: locational attributes and site attributes. Locational attributes refer to the position of the site within the entirety of the marketplace and understanding these will help you think about how to make it as easy as possible for as many people as possible to get to the site. Some locations may welcome new co-op members and shoppers who are exploring, and some will send cues that are less welcoming.

Site attributes refer to how easy the site is to see, to get into and to navigate once onsite, and to the buildability of the right store on the specific site. Is the building falling over, and can the site accommodate large trucks? Are there environmental, grade or parking issues? Some of these questions will be answered during due diligence, but some are easily identified at a glance.

## Locational Attributes

The location you choose should be both an expression of your concept and make it easy for people to choose the co-op in an increasingly competitive marketplace. For example, shoppers are generally increasingly frustrated by heavy traffic and driving, so removing any barriers to smooth ingress/egress to the co-op's parking lot is very important. Be sure to review the following with your broker (the market expert will also have taken these into account for sales estimates):

- **Traffic counts:** a good measure of the convenience of a site for people, most often measured in cars per day
- **Accessibility:** how many people live nearby, measured in population within a trade area, radius (e.g., 3-mile population), or a certain drive time (e.g., within 10-minute drive)
  - Look at demographics for different sites to understand who is best served by the site and who might shop incidentally. Are you making it easier for either core shoppers or new shoppers?
  - Look at changes in demographics and consider how these might change in 5-10 years, since presumably the co-op will remain in that location.
- **Retail synergy:** This is more subjective, but think about surrounding activity and fit of the location for a food co-op.
  - What else is bringing people to this area? Are there other retail or commercial spaces nearby that people will be coming to anyway, or will you be the primary trip driver? Is there a lot of commercial space or just a little?
  - Are there similar types of commercial spaces nearby, and how does the co-op fit with the neighborhood? Will the presence of your concept make sense to the people who may not be familiar with co-ops or natural/organic food? When are those nearby spaces most active (daytime, weekend, all the time)? There should be enough traffic both on the road and on site to help make trips easy, but not so much that it keeps people away at certain times. Will this be a “weekend shop” only type of location, or is it convenient all the time?

## Site Attributes

As above, when investigating available sites, some site attributes may be obvious, and others may come out in due diligence. Looking at a site through different lenses may yield different answers,

and it is the team's job to put all of the viewpoints together to drive the right decision. A few important perspectives to consider include:

- The customer: Visibility, access and parking. Can I see the store? Can I get there? Can I park? All three may be immediately answerable, but often parking may need a little more due diligence.
- The retail operator: Can we physically build and operate the concept that we want here?
  - Site configuration — Can a large truck get to the building, load and unload with the trucks we use? Where will we put trash, balers, recycling?
  - Retail configuration — Is the configuration of space conducive to the concept, or does it look like a distinctly different kind of business?

These may seem like small questions now, but they can be deal breakers down the road.

- The lawyer: What issues do we know about, or need to ask about around:
  - City approvals, zoning, or other entitlements — Can we build the grocery space here that we want, or will there be hurdles?
  - Building condition and environmental — Are there floodplain issues, environmental contaminants on site, asbestos in the building, structural issues, and whose responsibility is it to remediate?
  - Legal restrictions — Are there easements, use restrictions, or other encumbrances on the site that might prevent the co-op from building what it wants? For example, if there is an access easement where you want to put a building, the easement would have to be renegotiated or vacated before you could build, and you may not get it. In shopping centers, it is not uncommon for tenants to restrict the other tenants' product selection or activity, either through leases or on the actual deed. For a lease, it should be Landlord's job to provide clear title; look at the title policy to ensure it is consistent with your use under the lease.
  - Timing — When, and for how long, is the space available? Your perspective may be different if the Landlord wants to rent space tomorrow, rather than have you design/build it within 9-18 months. Is this a sublease that only runs for 8 years? These may not match your logistical or financial timelines.
- The banker: Is the offer on the table really cheap? If so, why? Are there public incentives (federal, state or other municipal) or Landlord incentives that we already know about with this site? Would they be worth it?

### Site Attributes Summary: Different Lenses Yield Different Answers

Choosing a site for your co-op is a long-term investment in the success of your business. When weighing site attributes, consider multiple perspectives before making your decision:

- Customers: Is it enticing? Is it visible, easy to drive to, park and enter the store?
- Retail Operator: Can I physically build and operate the facility as I need?
- Lawyer: Can I legally build the facility I need?
- Banker: Are there additional costs or incentives associated with different sites?



### Parking: City Code, Landlord Wants and Co-op Needs

One of the most common mistakes in site selection and design for co-ops is underplanning for parking. Parking codes have traditionally dictated how many parking spaces a grocery store must have on site, typically around four to six spaces per 1,000 square feet of building. Depending on the municipality, this may be supplemented based on any café parking requirements your space may trigger.

Because these same codes have led to an overbuilding of parking particularly in suburban shopping centers, municipal codes have begun to shift to smaller requirements, and some even instituting maximum parking requirements to encourage density. Others are accepting parking requirements based on anticipated long-term volume, on the correct argument that it's a business's volume that is a better indicator of parking needs than size.

This development can be good and bad. Underparking the site is something that can limit attractiveness to a shopper, and can limit sales and sales growth. Where you once may have been prevented from underparking by code, that is no longer the case. More flexible codes now demand that you assess your own parking needs. Anticipated volume is the most important consideration here, but equally important is the setting of the site. Unless you are in an extremely dense area like New York City, where little to no parking is expected and most everyone would expect to walk, you will need ample parking for anyone traveling over about one-quarter mile. Further, as you determine your needs, also consider how many employees you would need to provide parking for.

A Landlord may also prefer to use a flexible municipal code as an argument to reduce the parking, allocate to other users and build more space. Accordingly, it's important to state within the Lease (if leasing), the minimum number of spaces to be dedicated to both the shoppers and also co-op employees. Municipal code may change, and is no longer something that you can depend on as a defense against an overparked lot.

## Evaluating and Securing Sites

The team may have a number of sites to evaluate further at this point. And there may not be any that look particularly attractive. Having no good options means that your broker may need to do more work to see what may come on the market in a few months or a year or more, or start knocking on doors. It also means that the co-op may need to revisit the timing criteria that were established early on to decide whether it makes more sense to pursue the site search later or make some compromises now.

If you have a few good or acceptable options, review these to determine how closely they meet your established criteria. Every site likely has tradeoffs (or, if there are no site tradeoffs, the best sites often also cost the most). Can you afford the sites under review? What due diligence still needs to happen? It may be that the team can choose two sites on which to do more due diligence, and develop a rough scope and budget for each to help determine which option is the best to pursue. Understand a Landlord's or seller's timing, but know that making commitments on very little due diligence without proper contingencies can be a huge mistake. Work with your broker to understand if/how you need to control the site (which will be discussed below), and how you can minimize cost in doing so.

## Due Diligence

You do not necessarily need to jump to commit now — identify one or two good options and look to control the site while you do more due diligence. It is important to understand what due diligence you still need to do and how long this will take.

### Project Due Diligence

Consult your project team and build a plan to get to a conceptual scope, schedule and budget, including:

- conceptual site plan
- conceptual store plan
- initial construction and equipment budget
- updated pro forma

### Legal Due Diligence

For planning purposes, consult your broker and/or real estate attorney on other necessary due diligence on each site and how long this will take, for any issues such as:

- land or building environmental or structural survey (these may be used for scoping/ budgeting above as well, as necessary)
- real estate title, including use restrictions, easements
- other existing lease/sublease issues

For leases, some or all of these items may be the Landlord's responsibility to provide for your review, depending on the deal. More of this may be done after either an LOI or Option to Purchase is signed.

### Public Entitlement Due Diligence

Finally, an architect, engineer, real estate attorney, or even the Landlord should start to provide insight into what sort of public approvals or entitlements you will need, and how long it will take to get them. You will not know fully what approvals are required until the project scope is better developed, but public entitlements are usually well defined and should be easily discovered. To minimize financial risk, you will want to either have such approvals in hand or have such receipt as a contingency in any Lease or Purchase Agreement as you move ahead.

# Securing a Site



Whether the co-op wants to lease or purchase, the process and goals for securing a site are similar:

- Identify the site
- Perform due diligence
- Negotiate for exclusivity (either with an LOI or Option to Purchase)
- Secure with contingencies (Lease or Purchase Agreement)
- Additional design, financing and public approval work
- Release contingencies

The ideal goal is to secure a legal interest in a site, but to delay obligations of payment (or minimize payments) until after the store is designed and ready to build, your financing is secured and the board has approved the full project. This section will walk through some of the basics of the lease and purchase process, and what to look for to move toward that goal.

## Working Toward a Lease (with Contingencies)

This section will detail how to move from an identified site to a Lease using the intermediate step of a Letter of Intent (LOI), which is generally a non-binding way to enter into exclusive lease negotiations on a site. Your broker will be your main partner, but your entire site diligence team will have work to do throughout to make sure that your site plan, store plan, project and operational budgets all work within the parameters of the LOI.

### Beginning with the Letter of Intent

If the co-op is working toward a Lease, the first formal step in securing a site is an LOI, which should provide exclusivity to negotiate on a site. Both Landlord and Tenant benefit from joint exclusivity to ensure that their due diligence will not be undermined by another deal. During the exclusive period, both parties continue their own due diligence on design and cost work toward a Lease with contingencies.

Your LOI is the document that will set the framework for your Lease. It is often *non-binding*, and either party can generally walk away even after signing the LOI, but it does set the terms. It describes the major business points such as the leased premises, how much the co-op will pay for it and when, who maintains what parts of the building, and many other points listed in the *LOI Primer* [see Appendix I]. This document is written in plain English, so it should be relatively easy to understand, and will be generally advised more by your broker on the business points than by your attorney.

Because your LOI sets the framework for your Lease, terms set in the LOI may be hard to change later, so it is important to negotiate for what the co-op needs. Your negotiation leverage is highest at this stage so you should feel free to negotiate hard for what you want. Moreover, while some Landlords may want you to sign a very short LOI, identifying more details of your Lease early on will lead to fewer, potentially derailing surprises later. The *LOI Primer* [see Appendix I] contains a broad range of issues that should be addressed in your LOI.

There is not a standard form for LOIs and most often, the Landlord will write a document from which to negotiate, but your broker should have their own version as well. Your team's biggest contribution during the LOI process will be to make decisions as to what is best for the business. Understand what your broker knows about your co-op and its financial position, and

what they don't know. For example, if they have not worked for a grocer before, they may not know the importance of certain use restrictions or of HVAC systems. If they have not worked with co-ops, they may be more inclined not to bring up issues like Guarantees, which may be typical in some leases, but are not typically agreed to by co-ops.

## Contingencies

It is important to note the role of contingencies in your Lease, which you will want to ensure are brought up during the LOI negotiation. Because of the nature of co-ops' fundraising and governance structures, you will need to ensure that, after a Lease is signed, you have contingencies for both financing (including for any member capital raise) and board approval of project scope and budget, before your Lease is finalized. Other contingencies are addressed in the LOI Primer.

### Contingencies: an added measure of control

Contingencies give you an added measure of control over securing a property, regardless of whether you are buying or leasing. Even beyond budget and scope, there are a number of things you don't control that underpin a store's development: your member fundraise amount or timing, your bank's approval, your board's approval, your city's approvals. An issue on one of these areas could leave you with land you can't develop, additional carrying costs or lease obligations you can't (or wouldn't want to) fulfill.

Your goal is to secure a legal interest in a site, but to delay or minimize payment obligations until after the store is designed and ready to build, financing is secured, and the co-op's board has approved the full project.

## Moving Toward a Lease

For a Lease, your attorney and the Landlord's attorney will usually use a form lease (typically Landlord's) and use the business points from your LOI to start to fill in the blanks. These documents can be mind-numbingly long and detailed, and as mentioned above, a good real estate attorney is invaluable to identify potential risks and advocate solutions. It is important to stay connected, and to ensure that you (and your broker) confirm that your business points were appropriately translated into legal language and that new provisions that might not have come up during the LOI are not too disadvantageous. Additional negotiating points

that are more legal or operational in nature will come up and the Potential Lease Deal Points [see Appendix II] highlights a few of the important ones.

Consult the co-op's design professionals as you finalize your site plan and other operational items. Continue to check with your attorney to see who else you need to consult with on deal points as they are finalized, notably for maintenance budgets, taxes, utilities and insurance. Ensure that the timing on contingencies works for each project team member — that your design timelines allow for ample budgeting, that your financing is given ample time to be completed.

Finally, before you sign a Lease, make sure to finalize your project scope, schedule and budget, ensuring all parties are aligned before the team goes to the board to finalize and approve your Lease. After that, move ahead with the signature process, and then celebrate — the site for your new store has been secured!

## **Purchase Option or Purchase Agreement with Contingencies**

If the co-op is not leasing, the process moves a little differently, but the basic steps are the same. A purchase can be an expensive and risky investment for your co-op, so even more than for a Lease, your goal should be to minimize as much risk as you can before you purchase the land or building. Ideally, this means that the co-op would close on the land and start construction the next day, with all of the approvals, permits and designs already complete.

While this cannot always be achieved, it should be your goal. This is very common in real estate development for good reason: The longer you hold the asset before you build, the higher the risk that the land value goes down (asset risk), that you can't build what you want (development risk), or that you can't afford to build what you want (financial risk). Accordingly, there will be more due diligence on risk and more long-term planning to do early with a land purchase.

### **Contingencies and Timing**

The purchase process is often somewhat simpler than negotiating a Lease, as there are fewer legal details to figure out. While you need to ensure that the title is clear, the land is clean and you can legally do and sell what you would like on the property, there just are not the same myriad details around term, maintenance and insurance, since (in most cases) the co-op will be the sole occupant on the land. Accordingly, so long as the price is acceptable, there are fewer

terms to negotiate. Your broker can help advise your team on an appropriate price, and this should be allowed for within your pro forma. However, a prudent approach to a purchase will minimize risk to the co-op by allowing time for due diligence and design.

The co-op should still include the same contingencies as above (financing and board approval after additional design development) in the purchase as you would for a lease. With leases, you'll recall that it is the Landlord's responsibility to provide title clear of encumbrances so you can build and operate as you'd like, and it's often their responsibility to provide public entitlements/approvals. Since you won't control these after you close on a property with a purchase, it's imperative to include these as a contingency on any purchase. As mentioned above, the timing of the closing will ideally be as close to the beginning of construction as possible. Early in the due diligence phase, work with your design and engineering teams to establish a schedule to complete both design and public approvals or entitlements. This (plus some additional time in case things hit a snag) should be your target close date. Finally, environmental contingencies and surveys for any existing building conditions are also a standard contingency for a purchase.

### **Controlling a Property without Purchasing**

If your timing or contingencies seem like too much for your seller to swallow within a Purchase Agreement, but you still want to maintain control over the land, you could control the property with a Purchase Option until your due diligence is complete. An Option gives you the right to purchase the property at a later date at an established price. There is often, but not always, a price associated with the Option, but it keeps the property off the market. If the property has been on the market for a long time, or has a lot of site or building risk associated with it, you may get a "free look" — meaning a free Option that will maintain your control. This would be a type of inducement by a seller to get another party to spend money on due diligence while giving them some control of the land. Maintaining control in this way is very common in real estate amongst both developers and retailers; it helps to minimize risk and capital outlay, and to push it out until are ready to build.

If at the end of your Option, you have found issues in cost, timing, financing, engineering/design or elsewhere, or if the value of the land has dropped significantly, you have the option of renegotiating or walking away without purchasing the property. This is the most flexible and least risky way to control a property, and as mentioned, is often used by developers and other retailers in their development process. The co-op should consider and talk about

an Option with your broker. Your broker can help you choose the right strategy, and it will depend on the deal, the market and the seller.

## Communication and Confidentiality

Whether leasing or purchasing, confidentiality remains important for the co-op. There are two audiences for whom you will want to control the message and timing — the co-op's owners and the public.

For co-op owners, you want to determine what, when and how this important group hears about the location so that you can properly message why this site is the best site for your store, and use those ideas and excitement around a capital campaign. Regarding timing, *messaging about a site is best done after your Lease is signed — not after signing a non-binding document like an LOI*. Public or owner discussion about a site prior to securing it with a Lease can undermine lease negotiations, both in terms of credibility (e.g., there's infighting around this site, so do they support this lease?) and in terms of negotiating leverage (e.g., if your co-op membership is so excited and determined to have a particular site, or has communicated publicly about it, the co-op may end up with a less favorable Lease).

The co-op's owners should be the first group to be notified of a signed Lease or Purchase Option. As above, it helps to control messaging and conveys the importance of the relationship your co-op has with owners when it comes time for your capital campaign. After owners are notified, it would be appropriate to go public with the lease announcement to build excitement in the community, and attract additional interest and ownership for the co-op.

Talk to your broker or attorney about your goals around confidentiality and what documents or provisions should be included in your LOI/Lease or Option. The Landlord or Seller may have needs around confidentiality as well. However, you'll need to go public for public approvals and your member capital campaign, so it's just a matter of building understanding with your Seller or Landlord on timing and scope of any announcement.

## Credibility in the Marketplace

One of the issues that has come up in the past for co-ops is credibility in the real estate marketplace and this has manifested itself in not hearing about good locations or not being seen as a desirable Tenant. This could lead to losing out to national grocers for the best sites at desirable rents.

Some of this credibility is financial, especially for startups, but most any startup business would have this issue. But some of your credibility in the marketplace is the professionalism with which your co-op presents itself — how strong is your business plan, how well thought through are your financial projections? How does your broker portray your business to the real estate community — do you know what you want to build or are you reacting to what's available? The upfront work your co-op does in planning goes a long way in establishing credibility. You want to impress everyone you work with, even your own team, with your concept planning and parameters you've worked hard to develop. For context, visit the real estate websites of some of your potential competitors — this is a great view into what else is out there for brokers, banks, landlords and sellers to look at [see Appendix for examples].

Your co-op likely cannot offer the same credit that a national chain could, and that credit goes a long way for landlords, banks, and even sellers when you ask for a long due diligence period. Each of them, rightly, wants some security that your co-op will be able to fulfill its long- and short-term obligations. However, in addition to a strong financial and business plan, be prepared to tell the story about what your co-op does offer and show other similar successes (though be aware of and able to speak to any failures). How have other co-ops succeeded — with fundraising, with operations — and how do you know your co-op can do the same? What organizations are there to help your co-op succeed both in the development and post-opening stages? Providing clear, concise communication around the networks of co-ops and co-op partners can help build credibility.

Finally, remember that your co-op's financial strength is the community in which you work — it's your owners — and the strength, stability and the community support that comes with a well-managed co-op has traditionally outlasted the recessions or other hardships where national chains may have closed an underperforming location. Co-ops can be hard to build, but once established, they are incredibly resilient and adaptable.

# Conclusion and Resources

This Real Estate Resource Guide was designed to provide guidance on moving efficiently from concept planning to securing a site. You've seen that there is a lot of up front work to be able to move quickly and credibly on a site — defining a concept, setting search parameters, defining roles, confirming concept with a market study and building a team for site diligence — even before you start looking at sites. Once you start reviewing sites, this guide has provided advice on factors to consider in choosing your site and how to decide, and then reviewed ways to secure a site to reduce cost and risk to your co-op. Please review the Appendices for further resources that can help guide your decisions. Good luck!

Additional Resources:	For additional assistance contact:
<ul style="list-style-type: none"><li>• LOI Primer (attached as Appendix I)</li><li>• Lease Primer (attached as Appendix II)</li><li>• Cooperative Grocer Articles (by Debbie Suassuna); available at <a href="http://www.grocery.coop">www.grocery.coop</a>.<ul style="list-style-type: none"><li>- <i>Location, Location, Location - Part 1: Location characteristics are key to getting started.</i> May-June 2011</li><li>- <i>Finding the Right Site for Your Co-op - Part 2: Evaluating visibility, ingress/egress and parking.</i> July-August 2011</li><li>- <i>The Right Fit - Part 3: Facility considerations for your co-op.</i> September-October 2011</li><li>- <i>Understanding Marketing Research: Information leads to opportunities for improving sales.</i> July-August 2010</li></ul></li></ul>	<p>NCG Development Co+operative John Guerra <a href="mailto:realestate@ncg.coop">realestate@ncg.coop</a> <a href="http://www.ncg.coop">www.ncg.coop</a></p> <p>CDS Consulting Co-op Mark Goehring <a href="mailto:manager@cdsconsulting.coop">manager@cdsconsulting.coop</a> <a href="http://www.cdsconsulting.coop">www.cdsconsulting.coop</a></p> <p>Food Co-op Initiative Stuart Reid <a href="mailto:info@fci.coop">info@fci.coop</a> <a href="http://www.fci.coop">www.fci.coop</a></p>

# Letter of Intent (LOI) Primer

This primer is meant as a tool to help you understand what a Letter of Intent (LOI) is, and to identify some of the most important business issues that co-op grocers should understand and include in an LOI, as well as identify the co-op's most important partners in this process.

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*Developed by Food Co-op Initiative, CDS Consulting Co-op, National Co+op Grocers and NCG Development Co+op.*

## **Anatomy of an LOI**

A Letter of Intent (LOI) is an agreement that helps a Tenant and Landlord or Developer set basic terms for a Lease agreement. Sometimes also called a Memorandum of Understanding (MOU) or Term Sheet, a LOI sets a basic framework and allows each side to have confidence that, with due diligence and drafting, a Lease will come to fruition.

Some LOIs are as short as one page, but the more information you address up front, the less likely it is that there will be any misunderstandings, any unexpected issues that are small but non-negotiable, or even any deal killers later. In order to adequately address any pertinent information, it's likely that your co-op will be signing an LOI that is closer to ten pages long rather than one page. Once the co-op begins Lease negotiations, you will be dealing with a much longer document with many small issues to negotiate. The co-op is better off identifying and settling business issues big and small on the table during the LOI process; even if you don't have all the answers, the LOI can lay out the timing and mechanism by which these issues will eventually be resolved.

Once the co-op signs this document, most often your team will continue due diligence (design, financial, entitlement) and move toward a full Lease document with your attorney.

## **Key Partners**

The co-op's real estate broker should be the main driver of the LOI, though your real estate attorney should also be involved both in issue-spotting and some drafting. This is not meant to be an overly legal document, but more of a summary of the important business points stating exactly what the co-op, as Tenant, is paying for and how much, as well as what the Landlord is contributing to the project. While some business points and language will be fleshed out further in the Lease negotiation, ideally the co-op or your Landlord should be able to provide the LOI to your real estate attorney and have them draft an extensive Lease document without the need for a lot of substantive business issue negotiation. Your team will be focusing more on the finer legal points instead.

## Things to Do Before You Sign

While the co-op's broker and real estate attorney will be your key partners in putting together the LOI, the design team (store planner, architect, engineers), the construction or cost estimating partner, and the financing team should all have seen relevant information regarding the site as well, and start to sketch out their part of the store to ensure there are no major issues.

As this document sets the stage for entering the Lease, your team should have already addressed and agreed upon:

- the store and site plan,
- the budget and financing plan for the co-op's share of the project,
- board support for such a plan (i.e., does it fit within defined project criteria),
- the timing of the project (due diligence, construction and opening), and
- your Landlord's ability to perform.

## LOI Deal Points

There is no industry standard LOI, and every deal will require different considerations. Below is a list of 27 typical deal points that should be contemplated in your LOI with some recommendations or notes on each one. While there is no right order, they are shown in a somewhat typical order, starting with the most basic project information, and moving toward more specific.

Remember:

- It is fine, even preferable to use your broker's or Landlord's form LOI. The form itself is not important, but inclusion of all of the important deal points is critical.
- Not all provisions below will apply to your deal; your market, your specific location and your negotiating partners will dictate which of these are most important. For example, use restrictions would not apply to a single-use building.
- Because you are a co-op grocer, there are key deal points that are slightly more co-op or grocery specific which your broker, lawyer or Landlord may be less familiar with, including but not limited to the following. Each of these will be explored further within their sections.

As a co-op:

- Guarantee (#4)
- Assignment (#18)
- Confidentiality (#20)
- Contingencies (#21)

As a grocer:

- Facilities — parking, mechanical, signage, delivery area, receiving/trash (#5)
- Term and Rent (#6 & 7)
- Use Restrictions (#17)

## Typical Provisions within a Letter of Intent

1. **Project:** ID's location/address
2. **Landlord:** Landlord/Entity
3. **Tenant:** XXXX Co-op
4. **Guarantor:** None, subject to review of financial statements

*Note: Some Landlords might expect a guarantor from an entity owned by a corporation, partnership or individual, but a guarantee is not something that the co-op is likely in a position to provide. It would generally entail putting up collateral or ensuring payment by another entity (like co-signing a loan) in case the co-op as Tenant defaults on the Lease.*

5. **Premises:** Defines what it is that you're leasing

*Note: For a simple single-use building or ground Lease, it may be defined simply as an address with some description of size. For more complicated retail locations (strip malls, multi-use building) more detailed explanations should be used. A site plan exhibit should be provided as part of the LOI to help define the space, and can be very helpful in clarifying intent. Here you can also define the square footage of the store, patio, receiving/storage/trash areas and even parking and other common areas listed below on the site plan. These may also be defined in other portions of the LOI.*

Potential inclusions:

- a. Store
  - i. Building, square footage of floor area with any mezzanine or basement space called out
- b. Facilities
  - i. Parking (including employee parking areas lit for security)
  - ii. Signage (pylon, building, etc.)
  - iii. Dock, Baler, Trash
  - iv. Cart Corrals
- c. Common Areas
  - i. What you and your customers have access to that you want to keep the same or control: entrance/egress, parking lot, patio, jointly controlled receiving, hallways, restrooms
  - ii. Areas your trucks have access to drive through, that you should maintain control over any changes to
- d. Site Plan

## 6. Rent and Additional Rent

- a. Base Rent
  - i. Determining Rent and Market Rent

*Note: To some extent, market rate does not matter — you care what you can pay within reason within your pro forma to get a deal done. That said, understanding market rents helps you understand if you would be overpaying for a Lease or, alternatively, if as structured, your pro forma doesn't get close to a market rent.*

*A Tenant broker is essential for both understanding what an appropriate market rate might be for rent for a grocery store and for understanding what would be appropriate for rent increases or escalators for future years, percentage rent, etc. Remember that strong grocers have traditionally been very stable tenants because of high equipment costs, and can be seen as great drivers of foot traffic for a Landlord. To the extent that your store is an anchor tenant for multiple other smaller tenants, this relative stability and foot traffic should be leveraged for lower than market rent. Please consult your broker here.*

b. Additional Rent

i. Escalators

*Note: Escalators are a way for a Landlord to keep up with inflation in the market. A broker will be able to advise what is typically seen in your market — how quickly and how much escalators move your rent up. Consumer Price Index is one common way to make sure that inflation rates are appropriate, but because of volatility, should be capped. Another way is to build in a set percent — this may over/understate inflation, but is certain.*

*A set rate through the initial term (handled in Section 7) is common, with escalators with the exercise of each option. As initial term lengthens, so does Landlord's desire for an increase in rent. The other thing to consider here is how often to allow increased rent, understanding that it compounds each time. Fewer compounding events are better, with a 10% increase every 10 years being slightly better than 1% increase every year for 10 years, for example.*

ii. Percent Rent

*Note: In the past, some Landlords may have charged a percentage of sales as additional rent in lieu of escalators to keep up with inflation. Some still use it as a way that a Landlord can capture some of the upside in your sales. While it does take more of your upside, it may be a way for Landlord to offer a lower base rent, especially in early years, and capture rising values in lieu of rent escalators. There may be two advantages for a Tenant here: 1) depending on your formula, if your sales decline, so may your rent, and 2) Landlord is more financially incentivized to invest in the property to maximize your rent than if on a set schedule. Floors (e.g., 2% of sales over \$10M) or ceilings (e.g., 2% of sales up to \$30M) may be considered to have these provisions not overtax the Tenant at either low-volume levels or to take too much of the upside in sales. Do realize that with these provisions, you will need to provide evidence of your sales to your Landlord, which may be a sensitive issue.*

(I) Sales Disclosures

*Note: Some Landlords may ask you to disclose sales or financials on a regular basis, even without a percentage rent clause. Do realize that there is an information asymmetry here that can be exploited when it comes to a future negotiation. While for some tenants, this may be completely proprietary information, co-ops may have a different take, given that sales are likely more public. Should you agree to a disclosure, do make sure that there is not an overreach in terms of frequency or*

*type/cost to you in disclosing.*

iii. **Triple Net Charges: Common Area Maintenance/Tax/Insurance**

*Note: In a triple net lease (which is the most common), the Tenant will take on the direct costs for maintenance, taxes and insurance. If you are in a multi-tenant development, these are most often allocated according to your pro rata share (a.k.a., pro rata or PRS) which typically is calculated by your percentage of square footage for the entire development.*

(1) **Definition of Common Area**

*Note: In a typical retail development, all users more or less use all of the services.*

*Ensure, however, that costs for separate parts of the development are not allocated to your Lease (e.g., all of the tenants would want access to the large joint parking lot, but you may not want to pay for maintenance on interior elevator and lobby space for the entire development when you're on the ground floor).*

(2) **Cost Allocation (Pro Rata Share)**

*Note: Pro rata share is a quick and easy way to allocate costs for a development, and usually the best. However, some users may use different parts of a development significantly more or add incremental cost (i.e., an all-night diner for which the entire lot is being lit 24 hours a day, or a movie theater using disproportionate amounts of parking). Please examine the co-tenancy within your development to make special provisions for such instances.*

## **7. Term and Options**

*Note: Any Tenant will want as short an initial term and as long a tenant option period as available (e.g., 5 years initial and ten 5-year options). Landlord will want as long an initial term as possible.*

*Practically speaking, 10 years generally is the minimum you, as a grocer, would need to depreciate the investment in your equipment, so a 10-year initial term is a good place to start. Much longer than 15 years, and you are likely locking yourself into a space for longer than can reasonably be expected for either the location or physical space to fit the needs of the business. Moreover, you would be giving up the option of renegotiating for additional Tenant Allowance money or a different rental rate, if the space does still suit the business. Further, your Lease may specify that a default on your Lease may trigger the full amount for the full term of the Lease being due, so it is a good idea not to overcommit on initial Lease term. Again, every deal is different, but 10-15 years is a reasonable initial term. Expect though, that a Landlord may give you a lower rental rate for a longer initial term.*

*For the additional tenant option periods, a 30-year control period (e.g., 10 years initial + four 5-year*

*options, or 15 years and three 5-year options) should be your minimum goal. Some leases will provide options for much longer (60-100 years), but Landlords may have financial constraints that prevent them from going longer. You should try to get control for the site for as long as you can, and if you're an anchor grocery tenant, you should use your leverage to negotiate for additional optional term. Also ensure that your options are tenant options, not joint options or landlord options to renew your Lease. These options should be at your sole and absolute discretion.*

*Think ahead — if your deal involves a significant Tenant Allowance, 15-20 years would be a good time to ask for that again to help the Landlord invest in their space. Option periods can be a good time to do that.*

- a. Negotiate for a 10-year initial with four 5-year (tenant) options, with more options if possible

## **8. Possession and Rent Commencement**

*Note: Your broker should have some guidance on what you should expect in terms of rent commencement. Depending on your scope, consider with your construction partners how long your buildout will take from when you accept the space (with a little buffer). A few free months at the beginning of the Lease is really nice to help build cash at the outset.*

*It is also appropriate to plan ahead and provide for delays in Landlord's performance. If they are late in providing the space or finishing the space, what does that do to you, and how can they keep you whole in that event?*

- a. Possession and Inspection of Landlord Work — this would describe how and when you formally accept the space from the Landlord, and how you verify that the work has been done properly and to your requirements, if any.
- b. From possession, anticipate the length of Tenant construction — longer for a larger scope. Three to six months may be a reasonable starting place.

## **9. Security Deposit**

*Note: Your Landlord may require a security deposit with the Lease. This may or may not be negotiated to be credited toward rent upon opening. Be specific with amounts and timing to avoid confusion later.*

- a. [x] months' rent, due [when], credited toward Tenant [when]

## **10. Landlord Work**

*Note: There is no right answer in terms of what condition of completeness a Landlord would*

*provide to a Tenant. For a ground lease, the Tenant would just lease the land and then build and maintain their own building — this might be more appropriate for a well-financed chain with a pre-designed building, and a design and construction team that has worked together extensively. On the other end of the spectrum are tenants for whom landlords either fund or perform almost all of the building and interior buildout work. Tenants may have less control on design and execution, but may also have less invested (and less depreciation expense).*

*For existing buildings, though, the negotiations could revolve more around the condition of the interior space, who pays for the work (see Tenant Allowance below), and how payments are structured. Avoid vague terms like “vanilla shell” as this means different things to different people; instead work with your broker to use more descriptive scope terms like “warm, dark shell” which would indicate heated but unlit space. This will lead to both a stronger preliminary budget for you, and less confusion down the road.*

*Linked to Tenant Allowance, which you should discuss with your broker. While overages on any buildout are Landlord’s risk if they do the work, coordination is easier if you do it all yourself, with a portion of the work paid for by Landlord.*

## **II. Tenant Improvement Allowance**

*Note: Landlord may be willing to contribute to the cost of improvements for your buildout.*

*The LOI should state how much the contribution is (usually per square foot), but also:*

- *when the money will be disbursed (lump sum, installments, reimbursed, only upon completion),*
- *to whom it is paid (does Landlord pay contractors directly), and*
- *if there are any restrictions as to what the money can be used for.*

*Also be aware there are accounting implications when structuring who does what work. Clarify with your broker, attorney and financial partners who gets to “claim” depreciation as an expense. If Landlord does work on your behalf, they claim the improvements and depreciation. If they provide funding for you to make the improvements, you are more likely to be able to claim the depreciation expense for tax purposes.*

## **12. Tenant Work**

*Note: Landlord may ask for approval of your plans and to clarify what the scope of your work is, especially if there is a significant Tenant Improvement Allowance, which would be appropriate.*

### 13. Parking

*Note: Parking needs are commonly determined using municipal codes at a ratio of 5-7 spaces per 1,000 square feet of retail space. In urban or urbanizing areas with less available parking or areas with a mixed-use code, provisions for parking may be significantly less (1-3 spaces).*

*Understand who will be coming to shop your store and how they will be getting there — the city code may not reflect your needs, though both city and Landlord may push you to accept it. Urban planners typically quote one-quarter mile as the maximum people will routinely walk — how many shoppers do you expect to live/work within one-quarter mile? This works a few places, but not that many. In addition, shared parking is a concept that works well for many uses with hours that do not overlap, but grocery's hours often coincide with other users as it is typically open earlier and later than normal retail hours.*

*Make sure that:*

- *your market analyst is aware of the parking available for your store*
  - *you'll have a place for your employees to park, while still providing adequate customer parking*
  - *parking isn't over-allocated at your development, and if it is, make sure there are provisions for your Landlord to address it.*
- a. Ensure that development's parking is adequate, allocated properly and protected.
  - b. Make sure that your parking is called out on site plan.
  - c. Think about any allowances/operational items you may need for cart movement or storage as well.

**14. Utilities:** Should be separately metered.

### 15. Signage

*Note: Signage is an oft-forgotten issue early in a deal, but this is the best time to negotiate it, especially in a multi-tenant development. Signage is the first way a new customer will learn where you are and should be a strong statement of your brand. Without strong signage, a future shopper may never realize that your co-op exists.*

*Top or prominent position on any major pylon/monument signs should be expected by anchor tenants. Remember, in a multi-tenant development, if you don't require this early on, it may be*

*promised to someone else first and will be too late when you go back to request it.*

*Just what you ask for or require depends on the development, but get visibility to any major thoroughfare, entry points, and any wayfinding within the center or interior of the development (including directory). You want to make it easy for people to find you.*

- a. Top position, 50% or more of total space, Landlord support for variances

## **16. Landlord Maintenance and Repair**

*Note: This section helps to define who performs what maintenance when. For the LOI, it is especially helpful for a Tenant to get a first year per square foot (psf) estimate of costs here. Common area maintenance are costs for maintaining common items at a development (e.g., parking lot, landscaping, entry ways) and are typically allocated by the proportionate square footage, commonly called the pro rata share. Do ensure that there are mechanisms to control scope of work and costs here, and make sure that you are using these common items if you are paying for them, and that services are not duplicative with what you expect to provide.*

- a. Building
  - i. Mechanical
  - ii. Structural
  - iii. Windows (inside and out) and Walls
  - iv. Roof
- b. Common Area (Pro Rata Share)
  - i. Interior, a.k.a. Load Factor
    - (1) Shared Bathrooms, Corridors — sweeping, etc.
  - ii. Exterior
    - (1) Sidewalks
      - (a) sweep, snow
      - (b) cracks, replacement
    - (2) Parking Area
      - (a) utilities (lighting, sprinklers)
      - (b) sweep, snow
      - (c) patch, mill overlay

- (3) Other (Landscaping, etc.)
- iii. Signage — Power, Maintenance
- iv. Management Fees/Overhead/Security/Depreciation/Capital Costs
- v. Fee Structure (psf + escalator or actual + fee), Audit Rights and Influence

*Note: Maintenance will be defined more clearly in the Lease.*

## **17. Use**

*Note: Use restrictions may be a very important part of your Lease, and there are two types you should expect to come across — restrictions on your space that the Landlord puts on, and restrictions/exclusives you may ask for on the balance of the shopping center.*

*Restrictions on your premises should allow for your planned operations, but could also contemplate future changes to the business (liquor, restaurant, pharmacy). Landlord may ask to restrict your use to grocery, which may or may not be appropriate. If your Lease is “grocery friendly,” in terms of length of lease, rent and Tenant Improvements that is reflective of a long-term anchor Lease, this may be appropriate: Landlord needs the stability and foot traffic a grocer brings to attract other tenants. If you are getting a retail market rate lease that treats you more as a standard retail tenant, stronger tenant use restrictions are less appropriate. Remember that any use restrictions you agree to may limit who you could assign a Lease to later as well. Do ensure through the LOI/Lease that you understand what, if any, use restrictions may already encumber the premises as well.*

*Use restrictions on the balance of the development should restrict noxious uses that are non-complementary for a grocery store, but also protect your business from current or future competition or operational impediments, such as conflicting truck movements, or more importantly, uses that are parking-intensive like residential, restaurant, gyms, etc. For the operational items, think about both what’s allowed on paper, and also how it would be enforced (e.g., if parking is sparse for residential, guests will likely park in your lot — how is this policed and enforced by Landlord, and at whose cost).*

*Uses like restaurants and farmers markets should be contemplated carefully, as they have impacts on parking and may be competitive with your offering, but may also be a complementary use that helps drive traffic to your store. You may rather have the right one right next to you rather than somewhere else in town.*

- a. Premises (Tenant)

- i. Permitted Use (grocery, on/offsite food, liquor, GM, but allow flexibility to change)
- ii. Clarify existing exclusives already on property with Landlord, if any
- b. Balance of Property (Landlord), as applicable
  - i. Retail
    - (1) First Class Use/Non-noxious Uses (automotive repair, dry cleaner, smoke shop, strip club, etc.)
    - (2) Exclusive Uses (grocery, on-premises food, off-premises food, off-premises liquor, drugstore, GM and wellness)
    - (3) Restaurant
    - (4) Parking Preservation (fitness, coffee, restaurant, bar — keep away from your front door)
  - ii. Non Retail: Housing, Office, other Commercial
    - (1) Parking Placement and Enforcement
    - (2) Loading Noise

## 18. Assignment and Subletting

*Note: It is nice to have the flexibility to assign your Lease to someone else or sublease without a formal approval from your Landlord in the event you want to relocate/close this location in the future. However, especially if the Lease is an anchor-type lease, Landlord would likely be unwilling.*

*Given what we're seeing in the grocery business recently, your floor should include the first of the following two things, and you should push for the second:*

- *the right to assign your Lease in the case of a merger or acquisition, change of structure, transfer to an affiliate, and*
- *the right to sublease a percentage of your store to an outside vendor (bakery, deli, etc.)*

## 19. Improvements and Alterations

*Note: In addition to Tenant's work and maintenance above, it can be helpful to think about the future investments you may want to make to your premises — expansions, remodels, etc. You may be able to set aside space on the site plan for a future expansion right (with rent amounts contemplated now), or think about how you may want to remodel the space in the future. You*

won't want to have to get your Landlord's approval for any change to make to signage, interior décor, fixturing/programming or equipment, but structural changes (if they built the building) would likely need Landlord approval. Address all of that now, while you still have the leverage.

- a. Future — expansion, décor, equipment and signage
- b. Provisions for any exterior/roof attachments for telecommunications, security and HVAC

## 20. Confidentiality

*Note: Confidentiality clauses are not uncommon within LOIs. Many tenants want to keep their interest in a site a secret for as long as they can for competitive, reputational, financial, or other reasons. Co-op grocers may have a few reasons to keep quiet until the right time — as above, competitive reasons make sense here, but additionally you will want to control when and how your board, staff and membership will hear about the site you've secured. You will not want to tell your full ownership about a site until it is fully secured with a Lease, and you will want to make sure that you control the message then, too. It should not come from a Landlord publicizing his new Tenant. Timing and messaging with your membership is particularly sensitive if your membership will be relied on for a portion of your financing. Start thinking about how and when you will want to deliver the news, and reflect that in a clause in your LOI.*

- a. Board and Membership, Landlord and Municipal

## 21. Contingencies

*Note: Contingencies are a good way to protect yourself from issues that you cannot control or did not foresee happening. If you are unable to raise the capital you need, if you hit a permitting issue with the city, or your budget is far in excess of what you expected, a contingency can help you walk away from the Lease with little or no recourse.*

*Your contingencies are likely a little different from some other entities that your Landlord is accustomed to dealing with. Your ownership, member capital raise, and your board approval process are all unique for you and the Landlord to deal with together. Remember, though, you don't necessarily control how much a bank or members will lend, whether the city entitlements will resolve, or how the Board will vote. You need to ensure you're not financially liable for the Lease before all of the pieces are aligned. Accordingly, while some may have already been met prior to signing of the LOI, each of these contingencies is conceptually a "must have" in your Lease, and therefore should be addressed in your LOI.*

- a. Financial (Bank and Member Financing)

- b. Board Approval (Scope, Schedule and Budget)
- c. Developmental (often Landlord’s responsibility, but could apply to Tenant, especially if Tenant is developing)
  - i. Legal, e.g., Environmental/Title issues — it is Landlord’s responsibility to provide a site that has no environmental issues and clean title (e.g., they can prove they own the parcel, and it allows you to build and operate as contemplated in the LOI). There may be easements or other restrictions over the property that make the location of a dumpster problematic, or that make selling food, health or beauty items, coffee or alcohol illegal. Ensure that these issues are dealt with.
  - ii. Landlord Performance on Design or other Deliverables — if Landlord is supposed to design or build a building for you, and doesn’t hit milestones on time or if costs exceed what you expected, you may want contingencies to be able to cancel the Lease if it no longer meets your timing or financial needs. Lay out these expectations now.
  - iii. Public/Private Entitlements or Approvals — if the co-op is responsible for certain zoning changes, approvals, variances, homeowner association approvals, neighboring property/neighborhood approval, or other permissions that could prevent your store from being built, ensure that you can walk away from the Lease if you’re not able to get them. Expect Landlord to ask for the same if they are responsible for these items.

## **22. Brokerage Fees**

*Note: Merely clarifies if/who the brokers are and who will be paying them (and how) upon Lease signature. Depending on the market, broker fees are typically paid by Landlord.*

## **23. Form of Lease**

*Note: This item merely clarifies who will be first drafting the Lease document. Your broker or attorney may have a form lease; otherwise, Landlord will likely provide.*

## **24. Expiration**

*Note: Simply describes how long the LOI offer is on the table.*

## **25. Title Insurance**

*Note: States that at their cost, Landlord to prove to you their ownership, as well as any restriction*

*to title or encumbrances to your use (condo association, use restriction).*

## **26. Non-disturbance**

*Note: States that Landlord shall provide, at their cost, a mutually acceptable non-disturbance agreement to you from any current lessors, mortgage, or lien holders within 30 days of Lease execution, or placement of any additional leases, mortgage or liens. This ensures that you keep your Lease in the event of a non-tenant created foreclosure.*

## **27. Non-binding**

*Note: LOIs can be binding, non-binding, or partially binding agreements. A non-binding LOI is extremely common, and is the assumed position for this Primer. The intent of this document is to set the basic terms for future binding documents. While it is not binding, it does allow both parties to continue to spend on due diligence. Accordingly, a period of exclusivity is highly recommended, so both parties can negotiate in good faith without the specter of another entity taking the deal.*

# Lease Primer

While most are familiar with the concept of what a lease is and does, this primer is meant to be a tool to navigate the process of lease negotiations, to understand who should be involved and how, and to identify major red flags within a lease.

## **This document will address:**

### The Co-op's Team

#### What to Understand Before You Start

- Mechanics
- Tone
- Assumptions
- Negotiating Position

### First Draft and Response

#### Negotiating

- Framework for Terms
- Communications
- Other Considerations
- Don't Wait Until the Last Minute

### Before Signing

- Final Checks
- Announcing the Lease

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*Developed by Food Co-op Initiative, CDS Consulting Co-op, National Co+op Grocers and NCG Development Co+op.*

## We’ve signed an LOI (Letter of Intent). Now what?

While the LOI won’t include every provision of the Lease, it should provide the basic framework for the deal. For most co-ops, one of the most common omissions is a financing contingency that allows time for the co-op to secure both owner and lender capital toward the deal. Please refer to the LOI Primer for a sample list of items that should at least be considered for an LOI. If an item was unintentionally omitted from your LOI, talk to your attorney about how to address during Lease negotiations.

Negotiating the terms of the Lease is the next concrete step, but before you have your attorney draft, step back and assess:

- the roles of your co-op’s team and what you will need from each party,
- what you should understand about the mechanics of the negotiation, and
- how to approach the negotiations.

## Your Team

### Co-op Board

- Approves the signing of the Lease, Option and/or Purchase Agreement
- Approves taking on additional debt for project expenses including but not limited to land

purchase, land and building improvements, store equipment, inventory and other project costs.

**Project Lead (often general manager) — head negotiator — connects the dots**

- Ensures LOI business points translate into the Lease, as your attorney may not have been part of all of those conversations. Your broker may help with this as well.
- Ensures that the pro forma assumptions (both budgetary, cash flow timing and operational) match the Lease, or can accommodate changes from lease negotiations
- Ensures budget includes scope of work contemplated in Lease
- Ensures site plan is reflected properly
- Ensures attorneys come to effective solutions that protect the co-op

**Attorney** — Should have experience with commercial real estate, and grocery experience preferred. You'll work with this person to mitigate risk and protect interests. The attorney will be heavily involved in the Lease negotiation. Assume your Landlord is hiring the best attorney in the state — a good real estate attorney is invaluable for getting a positive result.

**Broker** — Depending on broker and attorney, may help advise on some business and financial points or find creative solutions.

**Site and Building Design Professionals** — Ensures adequacy of any changes to building footprint and site plan as negotiations progress.

**General Contractor or Cost Estimator**— Should review the Lease's language around Landlord and Tenant scope of work and milestones to ensure all scope items are included and properly budgeted and that timelines for construction and store opening are appropriate.

**Financial Planner** — Updates pro forma prior to signature due to changes to project budget (Sources and Uses), timing of funds, timing of open, etc., as Lease negotiations evolve.

**Co-op Consultant** — Provides support and coaching on overall project and Lease to ensure that co-op specific items that even an experienced real estate attorney may not be familiar with, like member fundraising, are properly accounted for in the Lease as a contingency. They may also help identify timing issues for things like contingencies, city approvals, design/budget timelines, construction, open, Tenant Improvement (TI) payments.

## What to understand before you start

### Mechanics of Lease Negotiation

Typically, one attorney would write a first draft, and upon receipt, each team will review and their attorney would prepare a redlined (marked up) copy and a clean copy to the other side for their review and markup. Stylistically, communications will sometimes go between the Tenant and the Landlord, but more often through the attorneys. Establish the process and roles up front, so everyone is on the same page. Your attorney should see and hear everything that you do. This process will take at least a few weeks and can take several months, but it is important to get it right. A poorly drafted Lease will cost the co-op money over the length of the Lease, either with legal ambiguity or on unfavorable terms for the co-op. You've heard that an ounce of prevention is worth a pound of cure — this is a perfect example.

The best attorneys are not just issue spotters, but problem solvers and negotiators. They should tell you what changes they would agree to and why, and what you're getting in exchange. They should help you identify impasses and issues that the two parties' attorneys are having trouble understanding and working through. A call with you and your business partner on the other side of the table and your attorneys is often invaluable in helping to resolve issues.

### Tone of Lease Negotiations

Pretend that you are negotiating with the Landlord five years from now. They've sold the property to someone else, and you're no longer negotiating with a person with whom you've built goodwill, you're negotiating based on what's on paper.

Sales of a property to an outside entity, a transfer to others in a family (including multiple fighting heirs), or bankruptcies happen all the time. Negotiate with the assumption that it will happen and that this Lease, and no side conversations or trust, is all you have to protect the co-op. Not only is this an entirely plausible situation, this will help get you out of the "I trust this partner" mindset. Moreover, it's fair to openly bring and remind your negotiating partners of this — "I'm not negotiating with you, I'm negotiating with your successor and on behalf of mine," can be repeated to Landlord throughout the negotiations. They may tell you that they'll hold the property forever, and they may intend to, but no one has the ability to predict the future, and circumstances change. Moreover, expect continued negotiation, even on what's been settled in LOI.

### **Assumptions of Project, Now and in the Future**

What are you assuming happens both for you and for any building or development of which the co-op is a part? What are you relying on? Write it down. As you begin to review the Lease, ensure these assumptions are addressed.

### **Know Your Position, and Your Next Best Option**

There is always posturing during a Lease negotiation, and it's important to understand who needs what more. You both want the Lease to get signed, but at what cost to you? There are times when a co-op has few options but to take some of the terms Landlord may dictate. There are other times that you can be patient or be very firm with a Landlord to get exactly what you want. A common term for this is knowing your BATNA—Best Alternative to a Negotiated Agreement (from *Getting to Yes*, Fisher & Wry 1981).

### **First Draft of Lease and Response**

Your LOI may have explicitly laid out who will provide the first draft of the Lease and by when. If not, clarify with your attorney, broker, and Landlord who will draft it first. While there may be some perceived negotiating leverage with providing the anchor point with the first draft, there is also cost associated with drafting from scratch; moreover, through your negotiation, you will negotiate out many unfavorable points or reject unacceptable concepts.

If Landlord is providing the first draft, your working assumption should be that it is based on a template that's not up to date or reflective of this deal. Read it with a skeptical and discerning eye. Certainly there will be new concepts or ideas in there — that in and of itself isn't bad, but it's your job to cultivate the good concepts and cull the bad ones.

Build a basic understanding of the implications of each section. As a starting point, the last section of this Appendix includes example lease tables of contents that give you some idea of the depth and breadth of topics you will likely cover in your Lease. While leases generally are meant to be written in plain language, it is still a legal document and may have dense language and concepts consistent with legal documents. Work with your attorney to understand language and concepts that are difficult — that's what they are there for. Multiple read-throughs may be helpful to understand how it is structured, the contents, as well as concepts not covered in the Letter of Intent. Some steps below will help lay out a framework for evaluation:

#### **I. Confirm Terms from LOI**

- a. Acknowledge what may have changed
  - b. Note what should not have changed
  - c. Call out clauses that are unexpected
    - Radius restrictions, guarantees, continuous use clauses
  - d. Call out missing LOI terms
2. Review additional terms — walk through each with your attorney and understand what each one means. They will advise, but it will be your decision on where to give, and where to stand.
  3. Ask your attorney questions:
    - a. What other clauses are missing or clauses your attorney would have expected to see?
    - b. ID your assumptions and risks and how to protect yourself. For example:
      - What happens if Landlord goes bankrupt?
      - What if other tenants don't fill the rest of a shopping center?
      - What if there are problems with the construction?
      - Can I rebrand or remodel the interior/exterior of my building a few years, and under what conditions?
    - c. What physical, financial or other changes would be allowed by the lease, and what wouldn't be allowed? For example:
      - Can Landlord move my entrance or make site plan changes without my approval?
      - How quickly could Common Area Maintenance (CAM) costs increase, and what control do I have over it?
      - Can I change my signage?
      - Can I add sales area on the sidewalk?
  4. Identify issues that you want addressed, but may not have all the answers for now.
    - a. Talk to your attorney about how to address within the Lease — will it be required for Lease signature or will it be addressed at a later point, but the issue addressed within the Lease? For example, you may not have a sign plan developed enough for the Lease, but understand when and how it will be finalized.
    - b. If budgets aren't fully built, when will they be, and how and when will you confirm

financial viability of the deal?

5. Identify your signature process with your board and for your Landlord
  - a. If you've not discussed with Landlord earlier, this is also a good time to discuss your needs for signatures.
    - Will your board review before you sign the Lease, and will they need extra time?
    - Will you sign a Lease contingent on your board's approval?
    - How long will that take?
    - Set expectations for Landlord early, even if informally.

You'll now work with your attorney to provide a marked up Lease (and clean copy) back to Landlord — it lists everything you want added, taken out, or changed. Now you're negotiating again. Hold accountable to LOI terms, and go from there. After your first draft is back, you'll know better what's important to the Landlord, and what's not.

## Negotiations

### Framework for Terms

As you're negotiating, understand for each issue, what category it falls into, and where you're willing to trade:

- High likelihood, high impact  
*Example: business terms on rent, rent escalators, competitive/use restrictions, maintenance — should be set (fixed) and clear within LOI to limit downside or confusion.*
- Low likelihood, high impact  
*Example: Condemnation of portion of parking lot or building, Landlord default, Tenant default, Landlord violates use clauses and puts a parking-intensive use (office, education, fitness) in a constrained parking lot.*
- High likelihood, low impact  
*Example: minor co-tenancy violation (restaurant, liquor), minor parking lot repair issue*
- Low likelihood, low impact  
*Example: Minor common area changes, additional tenant signage/design dispute*

## Communications and Involving Partners

As you negotiate, some items may change or be clarified. Ensure that your technical partners review and provide feedback appropriately. Some people like weekly structured meetings to review terms with partners, and other prefer more ad hoc communications, but just ensure that your full team is engaged appropriately.

For example, a site plan change request may render your truck movement non-viable or require major merchandising changes inside. Or they may require further approvals from the city that may cost you additional time or money. Scope of work documentation should be reviewed with your architect and construction partner both for cost and budgeting and also for phasing and feasibility well in advance of signature for any negotiation on scope or economics. Rent, CAM, tax, or budget changes should all be reviewed with your financial analyst and updated in your pro forma.

Other items, like insurance requirements, may require the use of other outside partners.

## Other Considerations

Some other suggestions for common items within a Lease:

- Premises: Call out the building and common area you'd like to include in your area of influence both in words and in the site plan. Assume you have no control outside your premises unless explicitly called out in the Lease language or site plan.
- Common Area Maintenance: Likely allocated to different tenants by square footage and this is usually the fairest way, but:
  - Can Landlord provide estimated costs?
  - Can/should you define criteria for upkeep (number of sweeps per week, number of inches of snow for a plow, etc.)?
  - Could you be overcharged for other tenants' uses? Is another tenant or use (housing above, office) using more than their share? Are you paying, for example, for hallway cleaning in shared space or an elevator for housing/office above you that your customers won't use?
- Control of and Changes to the Common Area: You may be relying on the traffic pattern to the site, and on drive aisles within a development but potentially outside of your premises, as essential to your business. Any change or interruption, temporary or permanent, may impact your members and your sales. You should keep control of changes to the balance of any larger development you are a part of, including major access points and drive aisles.

- **Building Maintenance:** If they built it, it may be best if they are responsible for maintenance. Otherwise, assume it's broken and needs repair on Day 1. The party who maintains building exterior walls (paint, brick condition, graffiti) and windows (clean or break) is often overlooked. It's often useful to retain responsibility, however, for items that are operationally important to you, like refrigeration.
- **Construction of improvements:** Be clear with timing, milestones and flow of funds for Tenant Improvements, and ensure that it's consistent with your pro forma.
- **Insurance:** Type and amount will likely be required within your Lease. Check with your current insurer for a) what insurance requirements should be within Lease for a business of this size and b) what it will cost you (for pro forma). Further, have them look at what Landlord is required to carry as well, both for adequacy and non-redundancy.
- **Performance: Default and Remedy:** Ensure that you understand the full gravity of what could constitute default and what legal actions Landlord can take against you for even minor infractions. Work with your attorney to both understand and guard against overreach here. Monetary and non-monetary default should be addressed differently for you as Tenant.
- **Performance: "Self-Help Rights":** Understand what your remedy is if Landlord doesn't perform (e.g., maintain parking lot appropriately). Self-help rights are useful in this type of instance, so that you can both fix and charge back to Landlord (or deduct from rent) those expenses, but they are often omitted, giving you little leverage to fix. A well-defined mechanism, if nothing else, is good to include here.
- **Condemnation:** This section may include a clause contemplating a scenario where a small portion of the parcel or building are condemned. Many times, the language allows the Landlord to determine if your space is suitable for business and adjust your rent. You'd want to be able to make that determination on whether the space is still adequate: unlike some other commercial space, the layout of your floor plan has huge and expensive ripple effects if changed. Moreover, if a small portion of your receiving dock was condemned, and nothing else, the size of impact might be very small, but operational impact very large. You want to have some say in any decision regarding suitability of the space.
- **Approvals:** Work with your attorney to understand the difference between an approval that is at a party's "sole and absolute discretion" and "not to be unreasonably withheld." Make sure that each is used appropriately throughout the Lease.

- Recording the Lease: Ask your attorney if/what should be recorded to make fully enforceable, like use restrictions.
- Sale of Alcohol: Even if prohibited by current law, if that changes, you would prefer the ability to sell alcohol noted within the Lease right now. It will be harder to negotiate — or even restricted if that right is given to another tenant — if the law changes to allow sale within the store. Get it now.
- Subordination, Non-Disturbance, and Attornment Agreement (SNDA): Discuss this concept with your attorney. This section deals with how you and the Landlord’s mortgage lender treat you in the event that your Landlord defaults on the mortgage. This could result in Lease termination and Landlord obligations like maintenance or Tenant Improvements being extinguished. This lays out the rules of the road and is important to address properly.



## **Don't Wait Until the Last Minute**

Commonly, the drafting of proper site, building or sign exhibits lags behind the legal language and negotiation of the rest of the Lease, or is treated as an afterthought to complete just before Lease signature. This can lead to inadequate exhibits for future legal work or exhibits inconsistent with the most recent draft of the deal. Ensure that it is clear who is responsible for updating the draft exhibits, and on what schedule. The exhibits should be drafted, commented upon and completed along with the rest of the Lease.

### **Before you sign**

#### **Final Spot Checks**

Before you sign the Lease, it's a good practice to ensure that your full team has reviewed sections pertinent to their work. Things may change quickly during negotiations and even the best communicators may miss something. Accordingly, you can set expectations with Landlord that prior to signing, you'll review with your full team for any errors:

- Check site and building plan — do they match exhibits within your Lease?
- Confirm scope of work and update budget with construction partner
- Update pro forma (reflects changes to budget, timing, ongoing operational costs)

#### **Non-Disclosures and Announcing the Lease**

Discuss communication with your Landlord prior to signature if and how any lease announcement would be made. How will you be communicating to your board? Your members? The public? Will you be jointly announcing the signature, or will you wait until after some of the contingencies are met? Will there be just a press release or an event? If there is to be an event, who will be attending? Know what you'd like to have happen and discuss it all before signatures.

## Sample Tables of Contents for Leases

The below lease table of contents may not fully apply to your situation. They are intended solely to illustrate the length and breadth of a lease.

Lease Table of Contents: Example I	
Article 1	Real Property/Project and Premises
Article 2	Lease Term
Article 3	Base Rent
Article 4	Additional Rent
Article 5	Use of Premises
Article 6	Services and Utilities
Article 7	Repairs
Article 8	Additions and Alterations
Article 9	Covenant Against Liens
Article 10	Insurance
Article 11	Damage and Destruction
Article 12	Non-Waiver
Article 13	Condemnation
Article 14	Assignment and Subletting
Article 15	Surrender of Premises; Ownership and Removal of Trade Fixtures
Article 16	Holding Over
Article 17	Estoppel Certificates
Article 18	Subordination
Article 19	Defaults; Remedies
Article 20	Covenant of Quiet Enjoyment
Article 21	Signs
Article 22	Compliance with Laws
Article 23	Entry By Landlord
Article 24	Parking
Article 25	Security Deposit
Article 26	Miscellaneous Provisions
Exhibit A	Outline of Premises
Exhibit A-1	Site Plan of Real Property
Exhibit B	Tenant Work Letter
Exhibit C	Amendment to Lease
Exhibit D	Rules and Regulations
Exhibit E	Form of Tenant's Estoppel Certificate
Exhibit F	Extension Option Rider

<b>Lease Table of Contents: Example 2</b>	
Article 1	Lease of Premises
Article 2	Terms and Definitions
Article 3	Rent
Article 4	Additional Rent
Article 5	Landlord's Construction; Possession
Article 6	Delivery By Landlord; Tenant's Construction
Article 7	Intentionally Omitted
Article 8	Services and Utilities
Article 9	Use, Exclusivity, Common Areas, Vacancies and Licenses
Article 10	Alterations and Installations
Article 11	Repairs and Maintenance
Article 12	Requirements of Law
Article 13	Insurance, Loss, Reimbursement, Liability
Article 14	Damage By Fire or Other Cause
Article 15	Condemnation By Eminent Domain
Article 16	Assignment and Subletting
Article 17	Default
Article 18	Estoppel Certificates
Article 19	Subordination; Non-Disturbance
Article 20	Landlord's Access to Premises; Changes
Article 21	Quiet Enjoyment
Article 22	Waiver of Jury Trial and Venue
Article 23	Rules and Regulations
Article 24	Indemnification
Article 25	Environmental Provisions
Article 26	Security Deposit
Article 27	Option to Renew
Article 28	Notices
Article 29	Waiver
Article 30	Parking
Article 31	Signage
Article 32	Surrender of Possession
Article 33	Holdover
Article 34	Brokers
Article 35	Confidentiality; Contingencies
Article 36	Miscellaneous
Exhibits	
Schedules	

<b>Lease Table of Contents: Example 3</b>	
<b>Article I: Definitions</b>	
1.1	Defined Terms.
<b>Article II: Premises Leased</b>	
2.1	Premises.
<b>Article III: Contingencies</b>	
3.1	Landlord Contingencies.
3.2	Tenant Contingencies.
<b>Article IV: Term</b>	
4.1	Term.
4.2	Option to Extend Term.
<b>Article V: Rent</b>	
5.1	Base Rent.
5.2	Additional Rent.
5.3	Late Payment.
5.4	Security Deposit.
5.5	Net Lease.
<b>Article VI: Taxes</b>	
6.1	Property Taxes.
6.2	Tenant's Personal Property Taxes.
<b>Article VII: Insurance</b>	
7.1	Landlord's Insurance.
7.2	Tenant's Public Liability.
7.3	Tenant's Property and Other Insurance.
7.4	Form of Insurance/Certificates.
7.5	Tenant's Failure.
7.6	Waiver of Subrogation.
7.7	Tenant's Properties and Fixtures.
7.8	Indemnification.
7.9	Damage to Tenant's Property.
<b>Article VIII: Repairs And Maintenance</b>	
8.1	Repairs and Maintenance.
8.2	Utilities and Services.
8.3	Non Liability of Landlord.
8.4	Inspection of Premises.
<b>Article IX: Fixtures, Personal Property And Alterations</b>	
9.1	Fixtures and Personal Property.
9.2	Alterations.
9.3	Liens.
<b>Article X: Use And Compliance With Laws</b>	
10.1	General Use and Compliance with Laws.
10.2	Tenant's Exclusive Use.
10.3	Prohibited Uses.
10.4	Hazardous Materials.
10.5	Signs.
<b>Article XI: Damage And Destruction</b>	
11.1	Reconstruction.
11.2	Excessive Damage or Destruction.
11.3	Uninsured Casualty.
11.4	Mortgagee's Right.
11.5	Damage Near End of Term.
<b>Article XII: Eminent Domain</b>	
<b>Article XIII: Default</b>	
13.1	Events of Default.
13.2	Remedies.
13.3	Landlord's Default.
<b>Article XIV: Assignment And Subletting</b>	
14.1	Prohibition.
14.2	Scope.
14.3	Waiver.
14.4	Change in Control.
<b>Article XV: Estoppel Cert., Attornment and Subordination</b>	
15.1	Estoppel Certificates.
15.2	Attornment.
15.3	Subordination.
15.4	Recording.
<b>Article XVI: Miscellaneous</b>	
16.1	Notices.
16.2	Successors Bound.
16.3	Waiver.
16.4	Subdivision and Easements.
16.5	Accord and Satisfaction.
16.6	Limitation of Landlord's Liability.
16.7	Survival.
16.8	Attorneys' Fees.
16.9	Captions and Article Numbers.
16.10	Severability.
16.11	Applicable Law.
16.12	Submission of Lease.
16.13	Holding Over.
16.14	No Nuisance.
16.15	Broker; Agency Disclosure.
16.16	Landlord's Right to Perform.
16.17	Assignment by Landlord.
16.18	Entire Agreement.
16.19	Financial Covenants.
16.20	Memorandum of Lease.
16.21	Exhibits.
16.22	Time.
16.23	Authority to Bind Landlord.
16.24	Authority to Bind Tenant
16.25	Interpretation.
16.26	Excused Delays.
16.27	USA Patriot Act and Anti-Terrorism Laws.