

## Considerations When Developing Outparcels in Retail Projects

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Adding outparcels or pads to a retail project can add significant monetary value to the development. In many instances, end users may also prefer acquiring an outparcel in an established retail project over acquiring and developing a standalone site or purchasing or leasing land as part of a new development. The ability, however, of a developer to ultimately sell an outparcel for its maximum value, or an end user to use an outparcel successfully for the end user's business, often depends mostly on the legal status of the outparcel, and the rights, appurtenances and restrictions granted to, or imposed on, the outparcel as part of the initial development of the project. This article provides suggestions for developing retail projects in a manner that will help facilitate the sale or ground leasing thereof without unexpected delays or costs. In many instances, if the specified suggestions are not followed at the initial development stage, the ability to sell or ground lease an outparcel may be precluded entirely or require great difficulty or expense to accomplish.

### **Legal Lots**

Often it is not legally necessary as part of the initial governmental entitlements for a retail project to cause any outparcels included therein to be legal lots. However, at the initial stage of development, the costs of

creating legal lots are usually relatively inexpensive when coupled with the applications for the rest of the needed entitlements or approvals. In almost all instances, when developing a retail project, it is also a good idea from a value and future development perspective to create a legal lot through the recordation of a plat or map, or other jurisdictionally dictated process. Among other things, legal lots or parcels are required in some states to obtain entitlements needed for the operation of a business. In other states, like California, land cannot be sold lawfully unless the land being conveyed is a separate legal parcel. Legal parcels are also helpful, and sometimes necessary, to cause the land in question to constitute a separate tax parcel and/or to ground lease it. Having multiple legal lots as part of a retail project (as opposed to having a project made up of a single legal parcel) can also provide a developer or owner with additional flexibility if the developer needs or wants project financing.

To avoid future development issues, the boundaries of outparcels constituting legal lots should take into account local zoning requirements, including those relating to required building setbacks and/or floor area ratios (FARs). Future issues with development of an outparcel in a way that negatively affects the parking for the remainder

of the project can also be avoided, or lessened, by causing each legal lot to be designed so that the uses thereon are capable of being “self-parked” without reliance on cross-parking rights.

### **Project Documents**

With respect to maximizing the value of out-parcels, perhaps the most important thing a developer or landowner can do when developing a project is to make sure that all the land within the project is encumbered by one or more well-drafted project documents, such as a Declaration of Covenants, Conditions and Restrictions, an Operation and Easement Agreement, Easements with Covenants and Restrictions Affecting Land or similar project documents. Among other reasons, project documents are necessary to tie separate legal lots in a project together so as to continue into the future in a manner that allows for the improvement, operation and use of the project as an integrated development, even if the project is owned by two or more different entities or individuals.

In general, the project documents should, inter alia, (i) address the creation, protection from material changes in, and maintenance of the common area for the project; (ii) grant easements for cross access and parking, as well as easements for utilities and drainage; (iii) provide for project signage, including specifying the right of various owners or tenants to maintain signage on multi-tenant signs located on or otherwise serving the project; (iv) contain protections that prohibit the development and use of a parcel in a way that would depreciate the value of other parcels or the project as a whole; (v) dictate minimum liability or other insurance requirements for the owners and/or occupants of the project; (vi) require adherence to a common design criteria for all buildings and

other project improvements; and (vii) ensure that buildings and other non-common area improvements located within the project are maintained in a first-class manner. Such project documents are often very difficult to negotiate and record after the initial development stage.

To make sure that such project documents can be used to accomplish their desired purposes, all leases for the project should provide that they are subject to the applicable project documents, including any amendments or modifications thereto. Similarly, all deeds of trust, mortgages, and other lender liens should be expressly subordinate to or junior to the project documents.

### **Avoiding Problems With Project Documents**

If drafted incorrectly, project documents can also, however, be a material impediment to the development, sale or ground leasing of outparcels. To ensure that outparcels can be used in the manner required or desired by future end users, one should be mindful when drafting and negotiating project documents to provide flexibility with respect to permissible building areas, design criteria and height restrictions (e.g. architectural features should be excluded from the pertinent calculation). Specifying exactly where future buildings can be constructed on a site plan attached to the applicable project document is often problematic for future development. Even if the building areas so specified work for the initial set of end users, it is unlikely that the building footprint, including such related improvements as drive-through lanes, will be identical for any successor user or desired successor user of the outparcel in question. A better practice is to describe what the building areas shown on the site plan are intended to show

or set the permitted approximate location of such improvements so that minor variances therefrom do not require amendments to the project documents. It is also a good idea from a developer's point of view to show building areas expansively or only to require other restraints on future development, such as height limitations, view corridors or minimum parking ratios to provide maximum flexibility for future improvements that cannot currently be envisioned with any certainty.

Similar to the above, a developer or property owner should, to the greatest extent possible, be cautious with what control/approval rights it grants to anchor tenants/occupants of the subject shopping center or other retail project under the project documents, especially with respect to outparcels that should have minimal impacts on the operation of any anchor's business. To allow for a viable outparcel development, a developer or property owner should resist where possible granting design review approval to multiple parties, anchor tenants/occupants for the project, or at least include in the project documents safe harbor design specifications or criteria.

In today's world, despite the above, a developer or owner may not have the leverage to minimize anchor or third-party approval rights. In such instances, such control can be mitigated to some extent through provisions providing for "deemed approval" after specified notice periods if approving party does not respond in a timely fashion and to require that any such approval rights be subject to a "reasonable" standard, as opposed to one that can be withheld or granted in a party's sole and absolute discretion.

To avoid future development issues, it is also a good practice to make sure that:

- The project documents are clearly drafted and not in conflict with each of the various provisions contained therein;
- The project documents' exhibits are attached thereto (i.e., avoid the use of site plans referenced in the project documents, but only retained by one or more of the parties to the project documents, and not actually attached thereto ("Site Plan is on file with party X"));
- All exhibits to the project documents are clearly legible, particularly any building areas shown thereon;
- The project documents contain language allowing for amendments, if necessary, in a way that is not impossible to effectuate;
- Any construction blackout dates in project documents should be limited in duration; and
- Use restrictions in project documents are avoided where possible, and where not, limited to non-duplication of primary uses or true competitors that are clearly defined, which restrictions expire if the benefited party goes dark.

### **Limiting Project Control Through Leases**

The failure to limit or at least mitigate anchor control in the project documents is likely to lead to delays in any planned future sale or development of an outparcel and increase the costs thereof. Few anchor tenants or occupants will give their consent free. And, of course, the sale or ground lease of an outparcel is not a priority for anybody other than the parties directly involved in the sale or leasing thereof. For these reasons, the same caveats on granting third-party approvals within project documents apply with respect to granting approval rights to any anchor tenants under their leases for the project. If approvals or use restrictions are contained within any project leases, a mem-

orandum of the same should be put on record against the project or affected parcels to provide notice of the restriction to all affected parties.

### **Utilities Availability**

One of the biggest issues regarding whether an outparcel will work for an end user is the availability of utilities. Ideally, all necessary utilities should be stubbed to the boundaries of the applicable outparcels as part of the initial development of the project or otherwise reasonably available to be extended thereto from the public street or other land over which the initial developer has control. If the utility lines serving an outparcel will need to run across other parcels, as part of the initial development, easements for such lines should be created whether as part of the project documents or otherwise. Such easement should allow for the utility lines not only to be maintained, but also to be upgraded or replaced when necessary. The project documents or other recorded instrument should require that affected parcel owners allow for the recordation of utility easements required by utility providers serving businesses being operated on the outparcels in question. As a condition of service to a parcel where the utility connection runs through adjacent land, utility providers often require that an easement be granted to the

provider over the adjacent parcel on the provider's standard form.

### **Entitlements**

Where possible, the value of outparcels will be enhanced and any future transfers thereof expedited, if the initial developer can limit off-site entitlement conditions, such as signals or roadwork, to that required for the initial development, and lock in the fees that may be imposed as a condition of developing outparcels for a reasonable period through the use of development agreements or similar land use contracts. At a minimum, a developer would be wise to make sure that the applicable zoning code permits a wide variety of potential uses on the outparcels in question, including the installation and maintenance of customary building, pylon or monument signage, and appurtenant improvements, such as drive-through lanes. In connection therewith, the project should be planned and entitled in such a way so that future entitlements and permits granted to the owners or end users will not adversely affect any existing entitlements, such as by causing the entire project to be underparked per code.

In sum, the key to being able to sell or lease an outparcel successfully may often turn on the care that was taken by the initial developer of the subject project.

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