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**Urban Land
Institute**
Sacramento

Land
Link

SB 375: Will It Work?

In 2008, Governor Schwarzenegger signed Senate Bill 375, a sweeping environmental law which seeks to reduce greenhouse gas emissions by curbing suburban sprawl. When fully implemented, SB 375 will provide regional goals for the reduction of emissions related to vehicle use, and a sustainable land use plan designed to achieve those goals for each region. Most importantly, SB 375 will provide incentives for local governments and developers to follow these new plans—the bill carves a path around decades of fiscal and regulatory obstacles for development projects that meet the right criteria. But in practical terms, SB 375 may exclude some of the most vital sectors of the building industry and, in doing so, create new barriers to the emergence of a truly integrated community. Despite recent corrective legislation, planners and policymakers continue to debate the potential flaws in this system, and the long-term consequences of their persistence.

SB 375 creates an incentives-based scheme for homebuilders and local planners to reduce vehicle miles traveled through development patterns that integrate land uses and provide multiple transportation options, such as public transit. Metropolitan planning organizations will develop a voluntary land use plan for each region, called a Sustainable Communities Strategy. The Strategy should identify areas sufficient to accommodate housing needs for an eight-year projection and forecast a development pattern which, when incorporated with the transportation network, will reduce greenhouse gas emissions from vehicle use. If feasible, the Strategy must achieve specific targets, assigned by the State Air Resources Board, for the reduction of vehicle-related emissions. The adoption of a land use Strategy will involve a rigorous process of public outreach and deliberation, involving community groups, local leaders,

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Real Property Law: Lease Renegotiations with Troubled Commercial Tenants (Part 1)

Financially troubled commercial tenants are looking for ways to get through the tough economic times by scaling back their workforces and cutting back on expenses. Some of these tenants are also trying to renegotiate the terms of their leases. Landlords may be willing to renegotiate with certain tenants for various reasons, including a good tenant history and strong past relationships, the desire to avoid any “dark” spaces or to maintain a certain tenant mix in retail centers, and the difficulty of finding a new tenant for the space in this market.

This article is the first of two parts regarding a landlord’s renegotiation of leases with troubled tenants. Part 1 will discuss common lease workout terms. Part 2 will address the landlord’s due diligence and third party approval considerations before proceeding with the lease workout.

TENANT PROVISIONS:

Fixed Rent Reduction or Deferment. A common lease workout term is the reduction of the tenant’s fixed monthly rent. The landlord may agree to reduce monthly rent for a short period or through the end of the term, temporarily abate rent, or defer rental payments to a later date. Such deferred rent would be paid back later with interest either all at once on a specific due date or spread out over multiple months by being collected with future rents. The landlord could also turn the deferred rent into a loan by having the tenant sign a promissory note.

Percentage Rent & Gross Sales. In the retail context, the landlord may be willing to eliminate the requirement to pay minimum monthly rent altogether and only require the tenant to pay a percentage of its gross sales. Other alternatives are to reduce the tenant’s percentage rent or increase the breakpoint (i.e., the threshold of gross sales the tenant must reach before its obligation to pay percentage rent kicks in). The landlord should confirm that the lease contains adequate operating covenants to maximize the gross sales numbers and require the tenant to regularly deliver financial statements and sales reports.

CAMs or Operating Expenses. The parties may also consider reducing the tenant’s obligation to pay common area maintenance charges (CAMs) or operating expenses, or putting a cap on such amounts.

Space Reduction or Relocation. If the tenant has lost employees, reduced its stock of inventory or has fewer customers than it did when it entered into the lease, the tenant may request a reduction in the size of its premises, either by reducing the space the tenant currently occupies, or relocating the tenant to a different, smaller space. The landlord will need to carefully evaluate the construction costs and other expenses required to accommodate the reduction or relocation, as well as the tenant’s ability to pay for its moving costs and any impacts the space reduction or relocation may have on other tenants, such as whether other tenants would also need to be moved to make the relocation work. If the landlord agrees to reduce the tenant’s existing premises, it should confirm that the size and shape of the leftover space is adequate for leasing to a new tenant. The tenant may also be required to pay the landlord back for unamortized tenant improvement costs and leasing commissions.

Other Workout Terms. A troubled tenant may also benefit from a more flexible permitted use provision or relaxed assignment and subletting requirements. If the landlord’s due diligence reveals that the tenant would not be able to recover financially despite any reasonable lease modifications, and that the landlord will not likely



Catherine M. Oh

PROGRAM CALENDAR

ULI Sacramento Upcoming Events

- ▶ **YLG Special Focus Group Forum**
“Creating a new Park Neighborhood in Sacramento with integrated Urban Farming”
Tuesday, February 16
5:30 - 7:30 p.m.
Mulvaney’s B&L
- ▶ **Think Tank Series for Members**
Thursday, February 18
12:00 noon - 1:30 p.m.
McDonough Holland & Allen
Speaker: Heidi Begeot, CW Capital
Topic: Non-traditional Sources of Capital in our New Economy
- ▶ **Current Trends Forecast TOD Success**
a program presented by the ULI TOD Advisory Council
Friday, February 19
7:30 - 10:30 a.m.
Rancho Cordova City Hall
- ▶ **YLG Mixer**
Wednesday, March 10
5:30 - 7:30 p.m.
deVere’s Irish Pub
- ▶ **Think Tank Series for Members**
Thursday, March 18
12:00 noon - 1:30 p.m.
McDonough Holland & Allen
- ▶ **YLG Book Club Discussion**
Book Focus: *Who’s Your City?* by Richard Florida
Friday, March 19
7:30 - 9:00 a.m.
Old Soul Coffeehouse
- ▶ **Strategies to Implement AB 32 and SB 375: University Think-Tanks Offer Realistic Solutions**
a program presented by the ULI Sustainability Council
Friday, March 26
7:30 - 10:00 a.m.
SMUD Customer Svc Ctr, Rubicon Room

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For more information on these programs, please visit www.sacramento.uli.org or contact Mary Sater, District Council Coordinator at marysater@comcast.net.

recover adequate damages in court, then the landlord may want to cut its losses by terminating the lease and negotiating a lease termination payment from the tenant, including any past due rents, unamortized tenant improvement costs and leasing commissions.

LANDLORD PROVISIONS:

Modifications to Lease. In exchange for the workout terms in favor of the tenant, the landlord should consider negotiating additional rights to the extent not already in the lease, such as relocation rights, radius restrictions or any other provisions that the landlord did not get when the lease was originally negotiated. The landlord may also consider deleting or limiting any exclusive use rights, co-tenancy provisions, options or rights of first refusal, or any other significant tenant provisions. The landlord may also want to tighten up the default provisions, extend the lease term or give the landlord the right to terminate the lease during any reduced rent period. This termination right will give the landlord flexibility to replace the troubled tenant if the landlord can find a new tenant that can pay full rent for the premises.

Additional Security, Workout Expenses. In addition to modifying the lease terms, the landlord may require additional security from the tenant, such as a personal guaranty, increased security deposit or a letter of credit. The tenant may also be required to pay for some or all of the landlord's expenses related to the lease workout, including legal fees.

Before committing to any lease workout terms, the landlord should do its due diligence and carefully weigh the pros and cons of the modified terms. This preliminary step includes an evaluation of how the lease workout will impact agreements with third parties, including loan documents, other leases or use restrictions. These issues will be discussed in Part 2 of this article in the next LandLink.

Note: This article is for general informational purposes only and is not intended to be legal advice.

- contributed by Catherine M. Oh, Murphy Austin Adams Schoenfeld LLP

and took an extensive discussion tour of the facility.

The team then went to work, taking a comprehensive look at all the data and information they had collected, organizing and framing all of the key issues, and, finally, coming up with specific recommendations. On December 1, 2009, the panel returned to the zoo to make a final PowerPoint presentation of their findings and recommendations to City staff, zoo management, and its Board of Directors (the final presentation can be viewed at ulisacramento.org/tap.html). Now, the zoo will consider and appropriately incorporate the TAP's recommendations into its ambitious plans moving forward.

- contributed by Peter Castles (HDR), Mike Notestine (Mogavero Notestine Associates), Jeff Goldman (AECOM)

TAPs & Advisory Services At-a-Glance

Technical Assistance Panels (TAPs) are part of the ULI Advisory Services Program run and implemented by the ULI District Councils. These advisory services range from project analysis sessions, fellows advisory panels, on-site analysis sessions, one to five-day panels, technical assistance programs, advisory workshops, and special services. All of these services seek to provide:

- A scope defined by the sponsor to ensure that their needs are met
- An objective team of seasoned professionals who have addressed similar issues
- Recommendations that build on what sponsors have already done
- The high-quality outcomes for which ULI is known.



David Zehnder and Gene Endicott developing funding strategies.



The panel being briefed by zoo director Mary Healy.