

# New Jersey Law Journal

VOL. CLXXIX – NO. 10 – INDEX 980

MARCH 7, 2005

ESTABLISHED 1878

## REAL ESTATE & TITLE INSURANCE

### 'Going Dark' Provisions: Making Clients See the Light

Addressing continuous operation concerns during the lease negotiation stage is critical

By Marc C. Singer

In this economic climate of uncertainty, many storefront enterprises operating in shopping centers and malls are looking for cost-saving mechanisms by which they can increase revenues through streamlining operations and reducing costs. Whether the mechanism of choice to achieve those goals involves consolidation, merger, a reduction in workforce or moving toward Internet-based commerce, all such mechanisms usually involve (to some degree) the elimination, reduction or relocation of the retail space utilized. Many times it is just too costly for a retail tenant to continue operating in the leased premises. Other times, a tenant can reduce its costs by relocating its store to a better situated or cheaper location.

Regardless of the reason for the tenant's decision to shut its operations

---

*Singer, a partner with Saiber Schlesinger Satz & Goldstein of Newark, practices in the areas of real estate, business and complex commercial litigation.*

and "go dark," landlords can be faced with numerous economic problems that extend beyond the mere loss of the rental income from the individual tenant who has decided to leave. In particular, because shopping centers are essentially symbiotic in nature – i.e., each store or tenant relies on others to draw customers — the loss of one tenant (especially a large anchor tenant) can have devastating effects on the economic prosperity of the other tenants, as well as the landlord.

In light of this, it is critical for lawyers to counsel their clients in any lease negotiation (whether they represent a prospective tenant or landlord) on the ramifications of a tenant "going dark" during the term of the lease and the legal options available. These issues can often be addressed up front through carefully negotiated "continuous operation" clauses and "going dark" provisions. Even where these issues are not adequately addressed explicitly, both tenants and landlords have certain rights and remedies that must be understood before any landlord-tenant relationship is instituted. Accordingly, an analysis of the applicable law and a consideration of the business practicalities attendant to "continuous operation" clauses and "going dark" provisions are set forth below.

#### Express Provisions

Often an issue of contention in the negotiation of a lease is the inclusion of a "continuous operation" clause. Such clauses should be specifically bargained for and expressly identified in the lease and often require tenants to continue to operate during specified days and times (usually the ordinary business hours of the shopping center or mall). See Emanuel B. Halper, *Shopping Center and Store Leases*, (Revised ed. 1992) § 9.02(3), 9-80. Landlords want such clauses included in the lease to ensure the shopping center attracts customers and business flourishes. Also, where the landlord's rental income is linked to the tenant's revenue (such as in a percentage lease), the landlord has an economic interest in making sure the tenant stays open for business. Tenants, on the other hand, may not want to be tied down and want the ability to close an unprofitable store or to move to a better location should the need arise.

In negotiating these conflicting interests of the tenant and landlord, a compromise can sometimes be achieved. Often times, when a blanket provision prohibiting a tenant from shutting its operations during the lease term cannot be agreed upon, landlords will seek alternative protections against "going dark" through provisions requiring, among other things, (a) adequate notice of an intent to close the store, (b) a requirement the tenant utilize best efforts to locate a suitable replacement tenant, (c) an agreement not to relocate within a particular radius of the existing

location, and (d) reimbursement of costs incurred by the landlord attendant to the cessation of operation. Whether all, some or none of these or similar provisions are included in the lease ultimately depends on the negotiating power of the parties. While landlords sometimes have the upper hand in negotiation when they have a uniquely prime location, large retailers, who can serve as anchor tenants drawing other high value tenants to the location, can often shift the balance in their favor. Indeed, often central to a shopping center's success is the fundamental idea that a bellwether tenant (such as a supermarket or other large, well-known retailer) stabilizes the economic viability of the shopping center by serving as an "anchor" to which other smaller stores are connected. See, e.g. *Berkeley Development Co. v. Great Atlantic & Pacific Tea Co.*, 214 N.J. Super. 227, 239 (Law Div. 1986). Therefore, at a minimum, when counseling a client during the negotiation of "going dark" provisions, such considerations must be recognized.

#### Implied Provisions

Because the concept of continuous operation of stores is so fundamental to the existence of a shopping center, New Jersey law (and that of some other jurisdictions) will, under certain circumstances, imply such obligations into a lease even where no express provision concerning continuous operation or "going dark" is contained in the lease.

In doing so, the courts will often look to a number of factors: (1) the language in the lease; (2) the intention of the parties; (3) whether such a provision is justified by a legal necessity; (4) whether parties would have included it had they called attention to it; (5) whether the tenant is required to pay a percentage lease; (6) what affect it will have on the entire shopping center; and (7) whether the lease prohibits other shopping center leases from competing with the tenant. See *Cordonier v. Central Shopping Plaza Associates*, 147 Cal. Rptr. 558, 564

(Cal. Ct. App. 1978) (citing *Lippman v. Sears, Roebuck & Co.*, 280 P.2d 775, 779 (Cal. 1955)). In New Jersey, the courts pay particular attention to the intent of the parties, which focuses on the attendant circumstances to the negotiation and execution of the lease to determine the parties' intent. See *Silverstein v. Keane*, 19 N.J. 1, 12 (1955). Along these lines, New Jersey courts have adopted the theory of "interdependent economic units" which holds that an implied covenant to operate can be found where there is an economic interdependence between stores in a shopping center. See *Ingannamorte v. Kings Supermarkets, Inc.*, 55 N.J. 223, 229 (1970). This is particularly common (although not limited to) percentage leases where the landlord's rental income is dependent on the tenant's operations. See *Silverstein*, 19 N.J. at 12. Where the basis for seeking an implied covenant of continuous operation is a percentage lease clause, the courts will generally look to see how dependant the landlord is on the percentage rent.

In *Ingannamorte*, the New Jersey Supreme Court held that even in the absence of an express continuous operation provision, where the supermarket occupied one-third of an 11-store shopping center and the lease contained a use restriction prohibiting the landlord from leasing space to another supermarket competitor, the tenant could not simply pay rent and cease operations because stores are "interdependent economic units and the landlord has an obvious interest in the continued active operation of the leased premise far beyond mere payment of fixed monthly rent." *Id.* at 227. The Court in *Ingannamorte* went on to explain that despite the fact that the lease was not a percentage lease, there were other circumstances (i.e., the nature of the supermarket as a strong attraction for shopping center customers) sufficiently evidencing the intention of the parties that the lease will be under a mandate to operate reasonably within the terms of the lease. *Id.* at 228.

#### Remedies

Despite the best efforts of counsel in negotiating and drafting a lease on behalf of his or her client, what options and remedies are available for landlords and tenants when faced with the reality of "going dark"? For landlords the answer is generally tied to the language of the lease. Where the lease provides for a right of termination or liquidated damages, courts generally prefer to enforce such provisions as long as they are reasonable. Where no such provisions are present, injunctive relief tends to be the primary remedy available. While a majority of courts in other jurisdictions are reluctant to grant injunctive relief (such as specific performance) because it often requires court supervision, which conflicts with the general principles of the free alienability of property, New Jersey courts hold that these difficulties are outweighed by the inadequacy of money damages.

For example, in *Dover Shopping Center, Inc. v. Cushman's Sons, Inc.*, 63 N.J. Super. 384 (App. Div. 1960), when a tenant-bakery closed its store but continued to pay rent, the landlord-shopping center sought an injunction based on an express operating clause requiring the tenant to "keep [the] store open for the regular conduct of its business therein during same hours at least as customarily employed by other similar stores in [the] neighborhood of the demised premises..." The court granted the landlord injunctive relief based on the cooperative nature of the shopping center, the speculative nature of money damages and the fact that no request for judicial supervision beyond the initial order requiring the store to reopen was requested.

Tenants, on the other hand, are best advised to deal with continuous operation concerns up front in the lease negotiation. That can be accomplished through the negotiation of exceptions to continuous operation clauses for such events as: (a) causes outside the tenant's control, (b) where extensive repairs or alterations are required, (c) store damaged by fire or other casualty, (d) failure

by landlord to provide essential services, (e) during vacation periods and holidays, (f) where manager or owner-manager is sick, and (g) during riots, strikes or other labor disturbances. See *Shopping Center and Store Leases* at § 9.02(3), 9-85. Counsel also should discuss with a tenant, to the extent feasible, the possibility of negotiating a choice of law provision utilizing the law of a jurisdiction that does not favor or significantly limits implied covenants for

continuous operations. Such a tactic, however, can prove very difficult unless there are sound reasons for the application of such law; particularly, where there is little or no nexus between the parties and that jurisdiction.

Given the complexity of the landlord-tenant relationship in the shopping center context, and the many external and internal economic factors that can influence that relationship, careful consideration of these issues during the

lease negotiation and drafting stage is critical. As most lawyers know and often remind clients, litigation can be expensive and the results are sometimes unpredictable. As such, lawyers should counsel their clients, keeping in mind the proverbial phrase that the "best defense is a good offense." Planning for these issues in the initial stages can go a long way toward saving a client the expense and aggravation of litigation in the future. ■