

3 Considerations As Amazon Eyes JC Penney, Sears Spaces

By **Andrew McIntyre**

Law360 (September 1, 2020, 11:10 AM EDT) -- Amazon is reportedly seeking to use former J.C. Penney and Sears stores as distribution warehouses, and experts say mall owners and smaller tenants should keep some key points in mind as the e-commerce giant looks to move in.

Shopping malls may have hundreds of tenants and thus hundreds of leases, and experts say it's critical that landlords thoroughly study all of those contracts — since leases at malls are highly interconnected — before inking a deal with Amazon.com Inc.

But just as landlords need to understand the consequences, so too do all the smaller tenants, since Amazon replacing a big-box store could have positive or negative implications for a mall as a whole when it comes to things like foot traffic and aesthetics.

"Clearly, Amazon is not afraid of expanding its real estate footprint," said Jason Grinnell, a partner at Thompson Coburn LLP. "From a pure warehouse use, Amazon will be looking to find efficiencies in their delivery models."

Here, Law360 looks at three things to keep in mind.

Landlords Need to Analyze Every Lease

While it's one thing to work out an agreement for Amazon to lease space that had been occupied by a big-box anchor, that change of tenancy could have ripple effects across the entire mall, and lawyers say mall owners need to carefully study all other leases to avoid problems.

For one, certain leases for smaller tenants may actually require that anchor tenant to be there, since anchors draw customers to the mall and increase foot traffic.

"A number of their other tenants may complain because they may have entered into their lease under the expectation that you're going to have an anchor department store there," Grinnell said. "A Cinnabon opens up ... because they want to be next to the Sears or the Macy's."

"Some leases will have co-tenancy clauses, so landlords who are looking at this potential shift may have some real headaches as things shift," Grinnell said.

Those clauses are often spelled out in rental agreements' CC&Rs, or covenants, conditions and restrictions.

And while co-tenancy is one issue, timing is another.

Landlords, lawyers say, should also be aware of when leases for smaller retailers are due for renewal and weigh that as part of the calculus for courting Amazon to their mall.

"The landlord's going to have to really look at its entire portfolio of leases in these centers, see when terms are expiring," said John Goldstein, an officer at Greensfelder Hemker & Gale PC. "What are their terms, renewal rights, purchase options? Are there any conflicts?"

Zoning Could Be Tricky

While one hurdle for landlords is making sure there are no conflicts with other retailers at the mall, owners generally also need to get a zoning change in order to replace a big-box retail store with an Amazon warehouse. That comes with a separate set of challenges.

Putting an Amazon warehouse in a mall will likely require a zoning change from retail-only to industrial. And the big question is how open municipalities will be to such a change, said Rob McPeak, a partner at McDonald Carano LLP.

He said securing zoning changes could be a drawn-out process depending on the local government and how much opposition there is from residents in the surrounding neighborhood and other tenants in the mall.

Parking and traffic are also major issues. Semi-trucks may be coming into the warehouse during the middle of the night, which would create more traffic and noise. And the appearance of the mall would also change with semi-trucks parked at the facility.

Of course, cities have to weigh these considerations with the question of tax. While the presence of semi-trucks may not on its own be terribly appealing, cash-strapped cities may approve a deal in part thinking they'll get more tax revenue.

"The tax implications are different depending on where you are in the country. If you just have vacant retail space, that might entitle you to a reassessment of your property value," McPeak said. "Your taxable value might change if you bring in Amazon, and it could turn into an increased property tax valuation."

Clearing a path for Amazon could also ease city leaders' minds about the possible alternative of spaces sitting empty.

"For Amazon, it makes absolutely perfect sense for them to go into these locations," said David Tabibian, a partner at Jeffer Mangels Butler & Mitchell LLP. "This would solve a major issue for Amazon, to help them get to that next level of deliveries within a few hours."

An Amazon spokeswoman told Law360 the company could not comment on its "future roadmap" or "specific operations plans."

Smaller Tenants Also Need to Study Leases

Just as landlords need to be aware of their rights and obligations regarding leases with smaller tenants, so too do smaller tenants need to study their leases to see if they can take action.

Many leases actually allow for smaller tenants to stop paying rent in the event of an anchor leaving, and those tenants need to be aware of those provisions and exercise them should an anchor leave, lawyers say.

"Having the right to stop paying rent or paying a reduced amount of rent for six to 12 months, that's generally what we see," Tabibian said. "If the landlord is not able to replace [the anchor] with a suitable anchor, then that tenant would have the right to terminate. That can pose very difficult issues and challenges for any property owner of a center that's losing an anchor."

Of course, not all leases have those provisions. For smaller retailers without such safeguards, the

change of use could spell trouble, since those tenants depend on foot traffic.

But all is not necessarily lost in that regard if an Amazon warehouse replaces a big-box retailer, since the Amazon employees may spend their money in the mall, particularly at food businesses, Goldstein said.

"These [Amazon] employees will want places to go to eat lunch; will want gyms, health clubs; will want retail. There's a new set of target people that [mall owners are] looking at," Goldstein said. "They're starting to say, 'Hey, we've got a new market.'"

--Editing by Aaron Pelc and Rebecca Flanagan.