Extracting Value from Shopping Center Assets

Deploying a Redevelopment and Repositioning Strategy

National Development Advisors, Inc.

A Case Study
Fountains Shoppes of Distinction
Plantation, Florida

Introduction

This publication will use a case study to explore the challenges and opportunities inherent in executing a shopping center redevelopment.

The subject property is the Fountains Shoppes of Distinction in the City of Plantation, Florida, currently owned by Developers Diversified Realty and previously owned by Inland Real Estate Corporation.

As land in urban and suburban areas becomes increasingly scarce, shopping center owners are realizing that there are substantial opportunities to create value from redeveloping and repositioning well-located retail assets. In some markets, expanses of asphalt parking lot at shopping centers may offer some of the single largest infill and redevelopment opportunities in the community. In other instances, the recent economic dislocation and attendant vacancies at previously stabilized and well-performing shopping centers have caused owners to take a fresh look for value creation opportunities. Additionally, new opportunities may exist to strategically assemble adjacent properties for future development that may be overlooked by shopping center operators naturally focused on current operations more than future redevelopment or expansion.

According to Christopher B. Leinberger, visiting fellow at the Brookings Institution, "The largest redevelopment trend of the next generation will be the conversion of dead or dying strip commercial centers in the suburbs into walkable urban places."[1] We posit that redevelopment and repositioning opportunities will exist not only for ailing shopping centers, but also for those that may be stable but are uniquely positioned for densification or intensification.

Regardless of the factors driving the need or opportunity for redevelopment of retail assets, one thing is certain: redeveloping shopping centers can be a complex undertaking requiring a multidisciplinary approach and an experienced team. Intensifying or reconfiguring development on an operating asset that is already ingrained in the neighborhood fabric is particularly challenging for a real estate owner and operator. Accommodating the real and perceived demands of increased density, tenant relocation, dislocation and consent issues, established and needed rights and requirements of adjoining property owners, and restructuring of financing and project governance are just a few of the myriad issues that need to be successfully managed to accomplish a successful redevelopment project. The increasingly relevant issues of "green" building certifications and standards, available water supply and stormwater management may require additional attention to successfully deploy the redevelopment strategy.

1. Leinberger, Christopher B., "Walkable Urbanism", *Urban Land Magazine*, September/October 2010, p. 115.

Background for Case Study

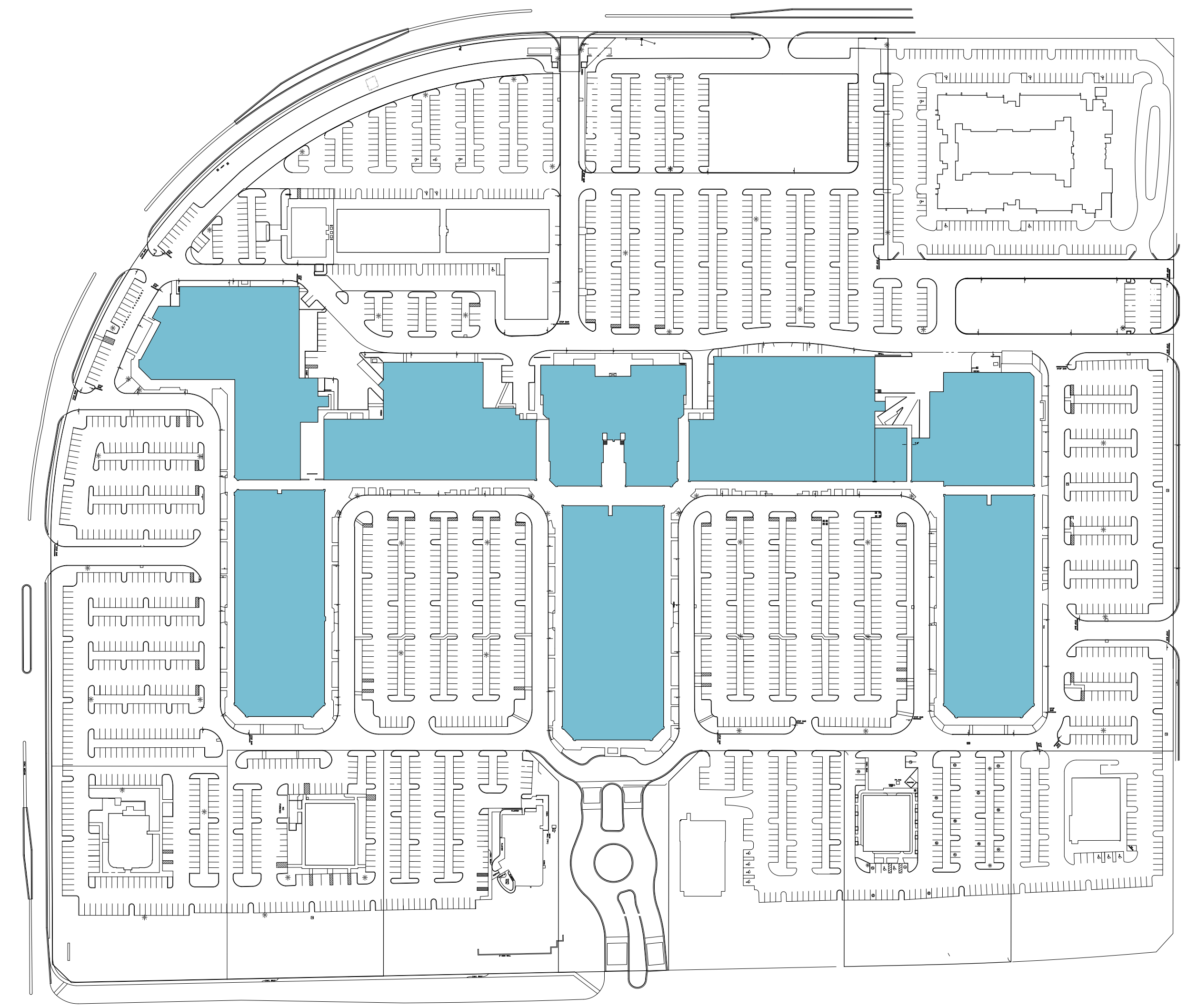
The Fountains as originally constructed was comprised of an in-line shopping center of 430,000 square feet, six outparcels fronting on University Drive, and a professional office complex and Marriott Courtyard at the rear of the shopping center.

The Fountains Shoppes of Distinction ("the Fountains") is a 43-acre shopping center that is a portion of a larger 60-acre tract located on University Drive in the City of Plantation, Broward County, Florida. In 2003, Inland Retail Real Estate Trust, Inc. acquired the in-line shopping center together with three of the six outparcels as the 142nd asset in Inland Retail's Southeast REIT portfolio. Constructed in 1988, the Fountains retained its original configuration at the time it was acquired by Inland Retail, although it had gone through several changes in ownership.

During the years that the Fountains was under previous ownership there had been significant tenant turnover in both the anchors and small shops. Several of the anchor tenants, including Linens N Things, Old Navy and Ross, had relocated to a shopping center in the neighboring Town of Davie, allegedly due to poor management at the Fountains. At the time Inland acquired the Fountains, there was a significant amount of vacancy at the north wing of the shopping center, together with a sizeable space vacated by a gourmet grocery store just south of the middle wing of the center. An eight-screen in-line movie theater at the rear of the center was struggling financially and delinquent on rent.

While it had a pleasing red brick aesthetic and nicely landscaped grounds, Fountains was challenged by poor vehicular and pedestrian circulation both north/south and east/west. Due to its odd configuration that resembled the letter "E" it was not conducive to strolling, and navigation around the shopping center was difficult and confusing for customers who were trying to locate specific tenants.

The Fountains Before Redevelopment



Original layout of the Fountains Shoppes of Distinction with challenging "E" configuration.

The Opportunity

Like many other mature suburban communities, the City of Plantation yearned for a sense of downtown, one that would invite people to live, work and play in a pedestrian-friendly city center.

Established in 1953, the City of Plantation developed as a suburb of Fort Lauderdale and was characterized by residential subdivisions and disaggregated commercial use. While the city boasted great neighborhoods, parks and recreation, and a strong office market that was home to several Fortune 500 companies, it lacked any sense of a downtown core. Retail shopping and services were largely spread throughout the city in a collection of strip and community shopping centers and two regional malls.

During the year prior to acquisition of the Fountains by Inland Retail, the City of Plantation completed a master planning process for an 860-acre area in central Plantation dubbed "Plantation Midtown" that included the Fountains shopping center. The purpose of the master plan was to facilitate redevelopment within the subject commercial district to create a vibrant mixed use town center environment which would include the addition of 3,000 residential units.

Following approval of the Central Plantation Conceptual Master Plan in 2004, the City adopted a new zoning district called SPI-3 and rezoned a majority of the property within Plantation Midtown, including the Fountains, to the new district. The new district was intended to allow for a more urban development pattern. For example, the new SPI-3 zoning provided for shared parking, minimum build-to lines to encourage buildings to be located close to certain street edges, increased heights, and residential density criteria that provided bonuses for advancing other objectives such as open space or developed frontage.

With the residential market still vibrant in 2004, the City's master planning and rezoning effort paved the way for assessment of the Fountains for a mixed use redevelopment opportunity. In addition to portions of the retail space that were underperforming, expanses of surface parking in the rear of the shopping center were the natural focus of initial design efforts to find suitable locations for the addition of multifamily use to the site and to set the predicate for retail redevelopment opportunities.

North Village

Town Center North

Town Center South

South Village (includes the Fountains)

South Business District

Plantation Midtown Subdistricts

Source: Central Plantation Conceptual Master Plan

Merging Community Aspirations with Market Reality

Oftentimes the community has a vision that does not completely align with market realities or with the shopping center owner's business model. That community vision can range from no vision at all (e.g., no growth or change desired) to a grandiose plan for complete revitalization of an area. If there is no vision, then the shopping center owner should be prepared to work hard to convince the local government and other stakeholders that the redevelopment is both appropriate and beneficial to the community.

While local government visioning can be beneficial and can set the stage for property owners to undertake development initiatives, the market ultimately rules. Getting the local government to understand that proposition, however, is not always as simple as it sounds.

The current state of the shopping center in terms of vacancy/occupancy and physical condition can inform the strategy to garner support for the redevelopment concept. Clearly, a center with substantial vacancy and deteriorating physical condition provides a basis to promote the redevelopment as necessary to prevent further decline and blight that can erode both the value of the asset and the value of surrounding areas. If the shopping center is not in declining physical condition, then it may be more challenging to sell the project as necessary to preserve the aesthetic and property values in the area. In this case, the focus may be better placed on the value-added potential of the project, such as increased ad valorem taxes for the local government; increased permanent employment opportunities; temporary construction jobs; or increased shopping, dining, entertainment, or housing opportunities for the community. Providing the local government with an analysis of the economic impact of the proposed project can be helpful in making the case.

On the opposite end of the spectrum, community visioning efforts, charettes, and other master planning processes can sometimes result in a utopian view of what residents or local government planners and elected officials (and their consultants) would like to see occur. This has been especially true over the last decade where the mixed use town center or lifestyle concept where people can "live, work and play" has been in vogue. Tempering an idealistic vision is challenging when applied to redevelopment of an existing shopping center. While the community vision may include wholesale redevelopment of a property, the most that may be feasible for a variety of reasons (including tenant rights or financial constraints) is a partial redevelopment and repositioning.

Achieving a Market-Appropriate Design

The Initial Consensus

The City's Central Plantation Conceptual Master Plan identified the Fountains as the opportunity to redevelop an "iconic town center." It contemplated "the complete redevelopment of the Fountains shopping center" and envisioned that the site, designated the "South Village," would be characterized by vertical mixed use.

> "South Village proposes the most substantial departure from existing development, in that the existing one-story, automobile-oriented retail environment will be replaced with three to four story mixed-use development with a major residential component." (Master Plan p.20)

Because Inland Retail was a retail shopping center owner, they determined that it was best to collaborate with an experienced multifamily developer to introduce residential use on the property. Inland Retail brought to the table as their partner American Land Ventures, LLC, an experienced multi-family developer who was the first developer to introduce multifamily residential into downtown Fort Lauderdale. Together, Inland Retail and American Land Ventures participated in the planning and design effort for integration of the residential component.

In evaluating the shopping center for residential use, a few truths were self evident. First, because of Inland Retail's significant investment in the shopping center, which was not physically deteriorated and had a substantial number of operating tenants, no one was going to tear down all of the existing development to allow a complete redevelopment in the near term. Second, in a suburban market like Plantation, vertical mixed use is not a housing choice that people generally favor. People looking for that type of opportunity generally desire to live in an urban downtown and not a suburban environment. Rather than spread the residential units out over shopping center property as envisioned in the Master Plan, it was ultimately determined that the most suitable location and pattern for the residential development was high-rise residential in 11-story buildings that would replace a surface parking lot at the rear of the shopping center.

The shopping center owner, residential developer and the consulting team spent a significant amount of time working with City staff and local officials to develop a plan that merged that market reality with the City's vision. The third architect on the project, ADD Inc. Architects, delivered the design that was ultimately approved. While the design was not exactly as envisioned in the Master Plan, many of the City's goals were achieved, such as breaking the large property into smaller "blocks" with new east/west and north/south vehicular and pedestrian connections, adding green space in the form of a new linear park, facilitating transit with the addition of an internalized trolley stop, and activation of the Midtown District's designated spine road at the rear of the center by placing the residential buildings close to the edge with live/work units on the ground floor. Even though the City favored redevelopment, as evidenced by adoption of the Master Plan, an economic impact analysis was prepared to help garner political support for the project as proposed.

Evolving Plans with New Ownership

After the site plan was approved for the residential project, Inland Retail sold the vacant 8 acre parcel at the rear of the center to American Land Ventures. Shortly thereafter, the shopping center itself was acquired by Developers Diversified Realty (DDR) who purchased the Inland Retail portfolio of more than 300 shopping centers. As the new owner of the Fountains, DDR immediately began the process of assessing Inland Retail's plan for redeveloping the retail portion of the shopping center, which was sparked by Kohl's interest in locating on the property. Once again the team began the arduous process of merging the City's vision with market reality.

Despite the Fountains being anchored only by Marshalls at the time, and having previously housed an Old Navy, Linens N Things and Ross, some at the City had expectations that the Fountains retail would evolve into an upscale shopping environment. Part of the challenge was that the shopping center's high quality brick exterior and landscaped aesthetic gave an appearance of a higher-end atmosphere and successful center that did not match the operational and economic reality. Nonetheless, there was concern by the City that permitting a large Kohl's to locate at the Fountains would forever establish the project

New Kohl's with substantial façade treatment (south elevation).

Façade treatment on rear of Kohl's store (north elevation).

as a mid-market center with large anchors and trend it away from the upscale town center vibe they desired.

While DDR was convinced that mid-market was exactly what the market demanded in Plantation, particularly in light of the economic dislocation that was occurring and as evidenced by the tenants attracted to the property, the City administration was not easily convinced. Much education, negotiation and design effort ensued over many months to ultimately reach an agreeable accommodation. The City eventually supported demolition of the north wing of the shopping center to allow a two-story Kohl's (with substantial façade treatments over their typical prototype), with the owner agreeing as a subsequent phase to demolish the middle wing and create a new east/west street lined with small shop retail that would culminate in two new park spaces where the new street intersected with the in-line center.

Vision	Reality
Complete redevelopment	Partial redevelopment
Vertical Mixed Use	Horizontal Mixed Use
Mid-Rise Residential (3–4 stories)	High-Rise Residential (11 stories)
Upscale Retail	Mid-market Retail

Additional Adjustments for New Tenant

The third leg in the race to merge vision with reality came near the completion of the Kohl's construction when DDR sought to locate a Dick's Sporting Goods in a portion of the in-line shopping center south of the proposed east/west street. While the City did not have any issue with Dick's as a tenant, they were very concerned with modifications to the previously approved plans that would be required to accommodate Dick's. To provide visibility to Dick's and allow more parking close to the store entrance, DDR desired to shorten the length of the two rows of small shop buildings that were proposed for construction along the new east/west street. The City originally viewed this as somewhat of a bait and switch: now that Kohl's was approved and under construction, the small shops that were promised as the next phase were being compromised. Of course that was not accurate as the shopping center owner was merely seeking to accommodate the needs of an anchor tenant that came to the table after the prior plan and commitments were approved. Further discussion and negotiation ultimately resulted in consensus whereby the City supported the Dick's and the shortening of both small shop retail buildings, and DDR provided additional fountains and landscaping treatment to enhance connectivity and the pedestrian experience between the in-line portion of the center and the reduced small-shop retail buildings.

Takeaway Points

- Visioning is great, but the market ultimately rules.
- The master plan can be an enabler, but flexibility is key.
- Vertical mixed use may not be suitable in a suburban market; horizontal mixed use with connectivity may be more appropriate.
- While everyone wants an upscale new urban town center, a mid-market retail environment may be more market appropriate and sustainable.

City Master Plan vision for the Fountains (the "South Village").

Fountains as constructed.

Going Urban in Suburbia

Suburban land development regulations are often not suitable to create urban development patterns.

The existing land use and zoning regulations that govern a particular shopping center property may not be conducive to either redevelopment with mixed use or to intensification of uses in a more urban development pattern. This is especially true in mature suburban areas where suburban zoning regulations are typically inadequate in terms of allowing an urban form. Key constraints can include excessive parking requirements that don't account for shared parking or mixed use, large setback and buffer requirements (see photo on facing page), permitted use limitations and height restrictions.

In this case a shopping center owner has to evaluate two options. First, can the proposed redevelopment scenario be accommodated under the existing regulatory framework by obtaining variances or other relief as necessary? This requires consideration of the legal basis for the local government to grant relief. If variance approvals typically must be based on demonstrated hardship can that standard be met? If the proposed use is not permitted, do the regulations permit use variances?) The political appetite for granting relief from existing regulations must also be assessed.

Second, if the proposed project cannot be accomplished under the existing regulations, would the local government entertain amending the regulations and/or rezoning/redesignating the property to permit the project? If the answer is yes, the property owner should expect that the local government may seek to have the property owner bear the expense of preparing and processing the required code or plan amendments necessary to facilitate the project. Such code revision efforts often can run concurrently with the project approvals so as not to unnecessarily delay the project.

In some instances only minor, but key, modifications are required make the project feasible. For example, in one complete retail redevelopment project on a constrained site in Palm Beach County, Florida, that included new retail, residential and hotel use, having to provide the code-required parking for the three uses would have been fatal to the project. While the code did contain a variance process, the "hardship" criteria for the variance could not be met. Like many zoning codes with a variance standard based on hardship, the hardship must not be "self-imposed." Redeveloping a property with more intensive use poses a particular challenge in this regard because it is the owner's act of redeveloping the property with greater intensity that usually leads to the hardship. Therefore, the hardship is technically self-imposed. Similar conclusions can be reached relative to the need for relief from setbacks, height restrictions or other similar criteria. In such an instance, rather than pursue a variance that may not be supported due to lack of sufficient hardship or, if supported, may not survive a third party challenge, a code amendment may be more appropriate. In the case of the Palm Beach County mixed use project, the consulting team prepared a mixed use and shared parking standard (with full analysis to support the standard) which the City amended into the zoning code at the same hearing at which the project site plan was approved. Adding clarity and certainty through a code revision, while perhaps more expensive and time consuming, may sometimes be a better strategy than pursuing a variance.

In some cases, the local government with a vision for redevelopment may have already initiated regulatory reform on its own in order to facilitate redevelopment. This can be beneficial if the new regulations accommodate the desired redevelopment scenario. On the other hand, if the new regulations will not accommodate the project as proposed, it can be challenging to persuade staff and elected officials to amend or grant relief from regulations that were just recently adopted after an investment of time and resources by the local government. Again, much will depend on the local government's appetite for the redevelopment.

Using Zoning Waivers for Relief

Analysis of New Zoning District

Fortunately, prior to Inland's acquisition of the Fountains, the City of Plantation had already developed a new set of urban zoning regulations for a zoning district called SPI-3 and then applied them to most of the Midtown district through a comprehensive rezoning process. This was a smart move to set the predicate for redevelopment.

> "Many of the [area's] planning and urban design principles included: large-scale single use properties, low to mid-rise buildings, surface parking areas, auto dependent transportation, wide setbacks, roadways and landscape buffers, segregation of uses. . . . Almost 40 years have passed since the original plans were envisioned. Since then, planning practices, design principles, and market forces have significantly changed. . . . Central Plantation's existing suburban development pattern presents many challenges for redevelopment. . . ." (Central Plantation Conceptual Master Plan and Prototype Site Plans December 2002, p.1)

While new land development regulations—such as those adopted by Plantation—that are geared toward redevelopment can be very useful in advancing redevelopment projects, property owners should anticipate that new codes rarely work exactly as planned and that some refinements or adjustments may be required.

Unlike suburban zoning regulations, which often require large setbacks, urban zoning regulations may have minimum build-to lines to activate the street edge.

New residential building that required waivers.

For example, Plantation's new SPI-3 zoning district contained peculiar provisions for the calculation of density that were limiting and that made it very difficult to determine how many units were allowed without going through design first, and the calculation provisions actually incentivized larger building footprints to the detriment of open space. There were also provisions related to shared parking and parking buydowns that were challenging. Ultimately the Fountains site plan was approved by the City Council with several "waivers" granted from the new code provisions. The City's waiver process, unlike that for variances, is not based on hardship.

Takeaway Points

- Suburban land use and zoning standards are usually insufficient to accommodate mixed use and urban forms. Expect the need to pursue some regulatory reform or relief.
- Even if the local government takes the initiative to adopt new regulations, new codes rarely work exactly as intended. Some relief may still be required for a particular project.

Working with the Neighbors

While most development projects require some level of community engagement and interaction, it can be especially true with the redevelopment of shopping centers.

Shopping centers prime for redevelopment are typically located in established areas and are surrounded by existing buildings and other existing uses. The nature of the uses surrounding a shopping center can affect the types of issues that may be relevant to the potentially impacted parties. For example, if the shopping center abuts a residential neighborhood, any plan to go vertical with multifamily or other uses could raise concerns about privacy for neighbors who may find their homes and yards visible from adjacent high rises. In that case, line of sight studies may be necessary to address concerns. Conversely, neighbors that have previously enjoyed an unobstructed view of the sky may fret at the thought of seeing tall buildings in the horizon. This was the case with two high-rise residential towers constructed on the perimeter of another large shopping center in western Broward County, Florida (as constructed in photo below), that drew the ire of the owners of nearby single family estates who did not want a view of the towers from their homes.

The typical issues of increased traffic, noise, lighting intensity and odors could also be raised by adjacent neighbors who fear the impacts of intensification or change in use. As a typical example, a change in use from strip retail center to a lifestyle center with more restaurants and entertainment can trigger concerns of residents over music or noise from outdoor dining and entertainment venues. In these cases, expert analysis from an acoustical engineer can be helpful in putting the anticipated decibel levels in perspective. Operational assurances regarding hours of operation and noise control may also be important to quell the concerns of neighbors. In addition to fear of potential physical impacts, there may be emotional impacts that are implicated when a long-established shopping center that has been part of local life for many years is facing change.

A community relations strategy to help the neighbors embrace the change as positive is essential. Sometimes design considerations can help assuage the fear of change or impending sense of loss of a piece of the community's history. For example, blending elements of the old design aesthetic with the new look or retaining key features can support the proposition of the project as a necessary but sensitive evolution that retains some of the shopping center's history but responds to new market conditions. In some cases, no amount of design accommodation will pacify the neighbors, but a financial contribution to a homeowner's association to help them meet an unfunded need, or participation in delivering other off-site improvements or amenities of import to the neighborhood can go a long way toward overcoming neighbor concerns. Any agreement by the neighbors not to oppose—or to affirmatively support—a project (including attendance by an association board member or other authorized representative) should be properly documented by agreement and/or resolution of the board as appropriate.

If the adjacent uses are nonresidential in nature, there may be fewer long-term impact issues to address, although concerns many be raised regarding traffic and parking impacts, impacts on view corridors, and other factors. Adjacent commercial uses are often equally or more concerned about the short-term impacts of construction on their operations than they are about long-term impacts. For example, maintaining access and visibility and minimizing noise and dust during construction are some routine concerns of adjacent commercial properties.

Case Study Application

Identifying Issues, Proposing Solutions

Commercial Neighbor Concerns

There were no residential uses adjacent to the Fountains shopping center that would be directly impacted by the proposed redevelopment. However, there was an office condominium complex at the rear of the shopping center and immediately adjacent to the proposed residential buildings that was occupied largely by doctors, dentists and other professionals.

In an effort to be proactive, the developer reached out several times to counsel for the professional office association to schedule a meeting with the board members and owners during the planning process but received no response. However, at the first public hearing before the City Council on the project, doctors with offices in the complex showed up at the hearing to voice their concerns. When the doctors attempted to get the meeting deferred so they could meet to discuss their concerns, developer's counsel was able to produce copies of the receipts from the hand delivery of letters to the association counsel requesting to meet. In light of that effort and association counsel's non-responsiveness, the City Council was not sympathetic to the deferral request.

Nonetheless, once the developer had the attention of the office owners and tenants, in a continuing effort to be a good neighbor, the shopping center owner hosted several meetings with the developer of the residential component of the project and representatives of the professional office association between the initial and subsequent public hearings. The professional office occupants' concerns ranged from construction impacts such as dust to potential impacts on parking from the new uses and visual impacts on the professional offices, which were oriented toward the rear of the retail shopping center.

Successful Solutions

The neighbors' concerns were successfully managed with a written agreement by the residential developer to provide regular car washing and pressure washing of the office building during the course of construction, and to install new signage for the professional office complex that would discourage others from parking on the site (even though cross parking rights existed). Regarding visual impacts, the shopping center owner went to great lengths to provide façade enhancements and landscape treatment for the rear of the new retail buildings, including the orientation and screening of loading areas, to ensure that they were aesthetically pleasing when viewed from the office complex.

Professional offices (on right) facing rear of Dick's Sporting Goods.

Façade detail on rear elevation of Dick's Sporting Goods facing the adjacent professional office complex.

Takeaway Points

- Redevelopment of shopping centers in developed areas will disrupt the status quo.
- The shopping center owner will need to work with impacted neighbors (residential and commercial alike) to address concerns.
- Sometimes mitigating impacts is not as complex as anticipated; other times it is costly.

Project Phasing

Maximizing Flexibility for Project Execution

When entitling a shopping center for redevelopment, it is important to establish a timeline that allows the project to be implemented based on its unique needs. This will most likely require working around tenants who will remain in place as well as tenants who may need to be relocated. The shopping center owner may desire to redevelop only a portion of the center initially, perhaps adding a new use or key tenant to gauge market reaction, and then do the rest of the project if the initial efforts are successful. Many national retailers only open new stores twice a year, typically October and April, so scheduling to meet one of these windows can be critical.

Unlike development of a vacant site, redeveloping a shopping center will most likely require working around existing tenants who will remain in place as well as tenants who may need to be relocated.

It is essential to develop a realistic schedule and have it approved by the local government so expectations are clear. Both the tenants and the local government will be concerned about ensuring that access, maintenance of traffic, utilities, pedestrian safety and other services and standards are maintained throughout the redevelopment process. The local government may require, or the shopping center owner may want to offer, a separate plan to demonstrate how those issues will be addressed.

The local government and the shopping center owner may want (or be required) to enter into a development agreement. Among other things, the development agreement can be useful for memorializing the commitments of the parties relative to development infrastructure and other enhancements, the phasing plan, and the rights and obligations of third parties if portions of the shopping center are being conveyed to others for development.

Redeveloping a shopping center also will likely entail both new signage and an upgrade of existing signage. If the shopping center is older, current sign regulations may be more restrictive so the older signs may be nonconforming. Modifying or upgrading old signs could trigger non-conformance issues relative to size, number, or other standards that need to be maneuvered through the approval process. Because signage is so important to tenants, in many cases it is advisable to seek approval for an entire new sign package at the time of project approval, establishing a master signage plan that provides some certainty for new tenants as the project evolves.

Case Study Application

Planning for a Multi-Phase Buildout

Framework for Managing Expectations During Deployment of Plan

Phasing of the Fountains redevelopment was of critical import for several reasons. First, it was desirable for the residential development at the rear of the shopping center to be approved first as a precursor to retail redevelopment planning since retail tenants are often attracted to locate on a site where they know there is or will be a captive market of customers. In addition, a substantial number of existing retail tenants needed to be relocated from the north and center wings of the shopping center to facilitate retail redevelopment. While the leases gave the shopping center owner relocation rights for many tenants, relocation rights did not exist for others. As such, during the entitlement process it was uncertain how long it would take to negotiate the holdout tenants out of those spaces or, in the alternative, whether the shopping center owner would have no choice but let those leases burn off if tenants were unwilling to come to terms.

A detailed phasing schedule and plan was developed for Fountains and approved by the City, including alternate scenarios that could apply in the event tenants could not be relocated or the process took longer than anticipated.

Second, the City was very concerned about ensuring that in no event would this valued shopping center and component of its Midtown district find itself in a half-finished condition. With each phase and its alternate scenarios significant attention was paid to temporary facades and finishes, including vegetated green screening, that would give the shopping center a finished look at all stages of project.

Temporary façade to maintain aesthetics between phases.

Third, to ensure a consistent look throughout the shopping center, the City required by a date certain completion of façade improvements to the south wing of the center that was not being redeveloped to mimic the new architectural features in the other portions of the project.

Façade improvements on the south wing blend existing buildings with new construction.

And fourth, the new small park spaces that were to serve as the project's focal point were required to be completed as part of the first retail phase and as a condition precedent to issuance of the Kohl's certificate of occupancy, to ensure that the amenity was obtained even if the subsequent phases stalled.

Takeaway Points

- Redeveloping an operating shopping center requires careful consideration of phasing requirements when entitling the project.
- While the local government will be anxious to see the project progress as quickly as possible, the shopping center owner will want maximum flexibility to respond to tenant relocation issues and market conditions.
- The phasing schedule and plan should be well thought out and documented; including them in a development agreement could be useful.

Introducing Residential Use

Balancing Expectations for Mixed Use

Introducing residential use into a commercial environment through a mixed use redevelopment program requires a careful balancing of interests. As with any mixed use project, the desire to provide quiet enjoyment for residents can conflict with the desire for a "24/7" vibrant retail and entertainment atmosphere. Restaurant odors, loud music and lights are just some of the sources of conflict. Resident privacy and security are additional considerations when combining residential and commercial uses on a single site.

Introducing residential use into a commercial environment requires careful balancing of interests.

Depending on placement of the residential uses on the shopping center property, even with horizontal mixed use, the back of house for the commercial tenants may be the front doorstep of the future residents. If that is the case, there may be design challenges to reconfigure and/or screen loading areas and spaces for trash pickup and compactors. In addition, enhanced architectural treatment of the rear of the commercial buildings may be necessary to maintain aesthetics from the residential perspective. If mid-rise or high-rise residential is proposed, screening of rooftop equipment on the shopping center may be relevant if it is visible from the residences. Of course, any of this enhanced architectural treatment to address aesthetics will increase the project's cost.

Case Study Application

Blending Residential and Commercial Uses Horizontally

Striking the Balance

The residential use at the Fountains was proposed to be constructed at the rear of the shopping center. As such, there would be some residential units that would be oriented toward the back of the retail buildings. When the site plan was being processed to redevelop portions of the retail buildings, the City considered several factors related to maintaining the aesthetic for the future residents. These included requirements for enhancement of the rear elevations of the commercial buildings beyond what would be normal for the back of a retail building, including arched brick work and additional landscaping. In addition, screening of rooftop air conditioning units on the top of reconstructed retail buildings was the subject of much debate because they would be visible from the high-rise residential buildings but not from the ground. Ultimately the City and the shopping center owner agreed on a screening method for the units. Signage on the back of the retail buildings was also limited to preserve the view from the residences.

New park areas link residential and commercial uses.

The elevated amenity deck ensures privacy for residents.

Streetscape and plazas provide a strong connection between the residential and commercial areas at the Fountains.

The City also gave significant consideration to establishing strong pedestrian connections between the residential and commercial portions of the project, as well as providing linear park space for use by the residents and public.

Privacy for the residents was partly addressed by locating the pool and amenity deck on the third floor of the residential buildings where it would not be visible or accessible from the retail shopping center.

Takeaway Points

- Preserving views and offering quiet enjoyment for new residents will be important considerations during project planning, but remember that it is still a shopping center.
- Retail's back of house may be someone else's front yard, so be prepared for four wall finishing beyond that in a typical shopping center.

Covenants, Master Declarations, Easements and Licenses

Untying the Ties that Bind and Getting the Rights You Need to Execute

Shopping centers that were part of a larger master development or include outparcels under separate ownership are often encumbered by recorded or unrecorded master declarations; covenants, conditions and restrictions; or other project governance documents. Such documents can restrict or govern such matters as access and cross access, parking, lighting, utilities, uses, CAM and a host of other operational considerations.

Identifying restrictions and their impact early can afford an opportunity to design a work-around before getting too far in the process.

It is very important to audit any and all project governance documents to understand what limitations they may impose on the redevelopment initiative. Identifying restrictions and their impact early can afford an opportunity to design a work-around before getting too far in the process. Alternatively, if modifications to the documents are required, the shopping center owner needs to assess the relative leverage of the parties and develop a strategy to obtain the requisite consent.

Beginning the negotiating process early with the parties that must consent to modification of project governance documents can prevent project delays later. This can be especially true if lender consent is required to amend the documents. Lenders often move slowly to respond to such requests because they typically want to fully evaluate and understand how their security interest might be affected.

Shopping centers also are likely to be encumbered by various easements, some of which may need to be modified in order to accomplish the proposed redevelopment. Existing easements can run in favor of utilities, governmental entities and private parties, all requiring different processes and complexities to modify. Relocation or other modification of general utility easements often requires that the property owner obtain letters of no objection from all utility companies serving the area. Getting a timely response from each one can be challenging.

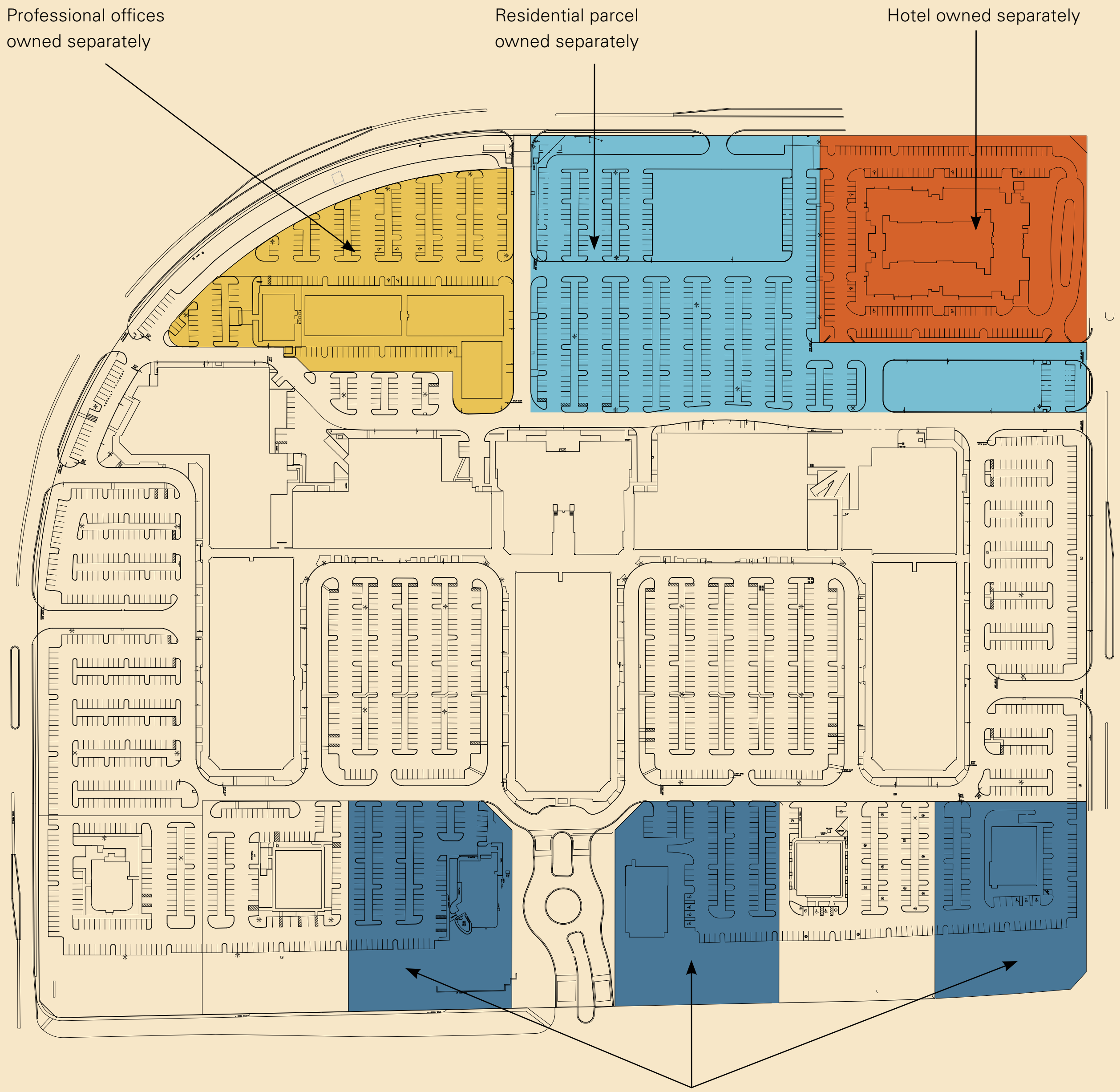
In addition to modifying, relocating or releasing existing easements, it may be necessary to obtain rights over adjacent properties—either on a temporary or permanent basis—to effectuate the redevelopment. The required temporary easements or licenses can include those necessary for construction access, staging, crane swing and the like. Permanent easements can include those for access, parking, utilities and maintenance.

Securing temporary and permanent easement rights can be a lengthy process and may require consent from the grantor's lender. In addition, the grantor may require the shopping center owner to provide evidence of insurance as a condition precedent to granting the easement or license.

Managing Multiple Owners and Parcels

Examination of Master Declaration

The Fountains shopping center and the separately owned hotel, professional office and all outparcels were encumbered by a Master Declaration that was recorded when the project was originally developed. Fortunately, the shopping center owner, as the successor Declarant, had significant flexibility under the Declaration to alter the site, including taking parking lots out of service and reconfiguring access. Nonetheless, addressing the Declaration and separate contractual arrangements was required. For instance, since a portion of the shopping center parking lot was being spun off to a residential developer for multifamily use, allocation of CAM and other provisions needed to be revisited.



Temporary and Permanent Easements Important

To accommodate the redevelopment of the Fountains, temporary construction easements were required from the adjacent outparcels at the rear of the center to allow for the construction of sidewalk and landscaping improvements by the shopping center owner. Temporary crane swing easements were also obtained by the high-rise residential building owners for the cranes that would be needed for their construction.

Several existing easements had to be modified, including utility easements and a government access easement that encumbered all of the site except for the building pads. Because there was a utility easement that traversed the middle of the parking lot that was being acquired by the multifamily developer which would have been directly under the proposed residential buildings, the multifamily developer was hesitant to close on the purchase of the residential development pad without assurance from the City that the easement would be released. Pursuant to the City's standard process, an easement would not be released until a new easement had been granted, the utility facilities relocated and the newly constructed facilities accepted by the City. However, the City understood the timing predicament with the need to close on the land before the utilities could be relocated. As an accommodation to alleviate the developer's concerns and allow the closing to take place, the City Council approved a resolution agreeing in advance to release the utility easement upon developer compliance with the standard utility relocation and new easement requirements.

An easement for crane swing over the adjacent hotel was required to construct the high-rise residential building.

Takeaway Points

- It is important to evaluate all existing easements that burden and benefit a shopping center to determine which ones might need to be modified to accomplish the redevelopment project.
- New easements or licenses—either temporary or permanent—may be required from adjacent property owners. A cooperative neighbor can help smooth the process while an uncooperative neighbor can delay or complicate the project.
- Starting the easement modification or relocation process early can help prevent project delays.

Easements were required from the professional office complex on the right to construct streetscape improvements.

Rights of Existing Tenants

Understanding Who Has Leverage

When it comes to leverage, existing tenants in the shopping center may have the most opportunity to frustrate the owner's redevelopment initiative. This may be especially true if there are national anchor or junior anchor tenants in place as their leases tend to contain more restrictions on the shopping center than smaller tenants.

All leases needed to be carefully audited to identify and evaluate any hindrances on the redevelopment project.

All leases need to be carefully audited to identify and evaluate any hindrances on the redevelopment project. Typical matters identified in the leases that can pose issues include:

- Parking lot no-build restrictions
- Assigned parking fields
- View and signage maintenance requirements
- Use restrictions
- Cotenancy requirements

As any shopping center owner knows, if you have to go back to a tenant to modify a lease or ask for consent, it typically will cost something in return. If the lease provides the shopping center owner with a relocation right, that can assist with execution of the project if tenants must be relocated and also may afford the owner with some negotiating leverage if the tenant does not want to move and the owner can implement the project while still leaving the tenant in place.

Case Study Application

Working with Tenants

Tenant Relocations and Buy-outs

At the Fountains, tenant relocation was a significant undertaking. Many tenants were relocated to accommodate the phased redevelopment of the retail portion of the shopping center. Several tenants from the north and center wings were relocated to the south wing. Others were bought out of their leases or otherwise terminated and relocated off site.

Tenant relocated from north wing to south wing.

Tenant relocated from center to south wing.

Special Considerations for Anchor Tenant

The approval rights of the only remaining anchor, Marshalls, had to be considered and explicitly documented as a contingency in commitments made to the City in the development approvals. For example, modifications to the in-line center to create a new east/west connection that was reflected on the approved site plan was explicitly made subject to consent by Marshalls. That access connection was ultimately not constructed due to later modifications to the plan. Marshalls did receive a new façade through the redevelopment effort.

New Marshalls entry.

Takeaway Points

- Audit leases early in the process to understand the rights of tenants that can impede the redevelopment project.
- Evaluate relocation rights and financial implications of relocating tenants on or off site.
- If tenant consent is required, be prepared to provide concessions or upgrades.

Construction on a Developed Site

Managing Inconvenience and the Need for Speed

Just as planning and designing a shopping center redevelopment can be more complicated than for a vacant site, planning for construction on an already developed site can be more challenging as well. Balancing the needs of existing businesses that will have to endure the inconvenience of the reconstruction effort against the owner's desire for rapid completion of the redevelopment project requires consideration of several factors.

Balancing the needs of existing businesses against the owner's desire for rapid completion of the redevelopment requires careful planning of the construction phases.

Traffic Planning

Planning for the maintenance of safe and adequate vehicular and pedestrian routes to, from and through the shopping center at all times during the redevelopment process will be important to existing tenants, the local government of jurisdiction and the owner. It is likely that the local government will require a plan that details specifically how this will occur. It may be necessary to reconfigure these routes from time to time to accommodate various phases of construction. Any temporary access or circulation modifications are certain to be frustrating and confusing to patrons who frequent the property. Proper signage, fencing, barricades and temporary lighting will be important risk management considerations.

Staging

Construction staging on a shopping center redevelopment project requires careful planning since there are often limited areas that can be used to store materials and equipment. It may be necessary to temporarily take surface parking areas or open spaces out of public use to provide construction staging areas. Naturally, planning staging areas to minimize impact on the tenants' business operations and ensure safety are paramount considerations. If adequate accommodations cannot be made for staging on site, off-site staging arrangements on adjacent or nearby property may need to be secured. This can require lease, easement, license or other agreements with other property owners, provision of insurance and other arrangements that should be planned well in advance of construction.

Extended Construction Hours

Many local governments have established set hours during which construction activities can occur in the jurisdiction. If a shopping center owner is operating under a very tight schedule to deliver the project to market, or needs to engage in construction activities at other than normal business hours to minimize impact on existing shopping center operations, then the owner may want to request approval from the local government for extended construction hours. Extended hours can include beginning earlier in the morning or working later into the evening than otherwise permitted, or additional weekend hours (e.g., Sunday hours that might otherwise be prohibited). The nature of the approval required for relief from construction hour limitations will depending on the nature of the hours restriction (e.g., code requirements v. other policy).

New Anchor Stores Drive Aggressive Schedule

Seamless Coordination Despite Multiple Contractors

The two new Kohl's and Dick's Sporting Goods anchor stores that were constructed from the ground up required the shopping center owner to implement an aggressive permitting and construction schedule to meet required delivery dates. The aggressive schedules had to be maintained while at the same time existing tenants were actively relocating and multiple contractors were working on site. For example, at one point the residential buildings were under construction by one contractor, Kohl's by another, and the small shop retail adjacent to Kohl's by yet a third contractor. Seamless coordination of staging, adequate site access and security was a testament to the skilled development team and cooperative nature of all the construction and operations personnel. While glitches are inevitable on a project of this magnitude (such as the power line that was severed by a contractor on the residential project, knocking out power to the professional office complex for several hours), maintaining safe operations for existing tenants and the public through proper fencing, signage, and management of construction activities was successfully accomplished.

New buildings under construction.

Takeaway Points

- Demolition and construction on an operating shopping center will inconvenience tenants and patrons.
- Careful coordination will be required to manage tenant and owner expectations.

Façade renovation.

Temporary signage.

Future linear park used for staging area.

Not Enough Land for Another Retention Pond

Intensification of development on a shopping center property can raise challenges regarding stormwater management. For shopping center redevelopment projects seeking to create a more dense urban form in particular, adding or maintaining additional surface water retention ponds or areas may not be a viable or preferable option and the proposal to alter the development pattern can therefore require creativity in meeting applicable stormwater regulations.

For example, in another proposed mall redevelopment project in the City of Plantation, an almost three-acre underground concrete stormwater storage vault was proposed to be located under the new open air retail/entertainment plaza in lieu of additional surface retention area. This concept was promoted and supported in part as a sustainable or "green" feature in that the captured stormwater would be used for irrigation and to replenish the project's extensive fountains and water feature system for weeks after storm events, saving potable water resources.

Creatively addressing stormwater needs can require the local government, water management district, and/or other agencies with jurisdiction to support alternative approaches. This may not always be as easy as it sounds given the regulatory framework within which the affected agencies must operate in their evaluation of project compliance. In some instances, pursuing regulatory reform may be necessary if means do not exist for a variance. Pursuing and obtaining such reform can be complicated if the applicable agencies are governed by federal or state regulations, as opposed to local regulations that the local government may be inclined to amend to support a key project.

Creatively addressing stormwater needs can require the local government, water management district, and/or other agencies with jurisdiction to support alternative approaches.

Fortunately, existing on-site and off-site facilities were adequate to accommodate the redevelopment project so there were no particular difficulties related to stormwater at the Fountains Shoppes of Distinction.

Additional Considerations

Accounting for Non-Physical Factors

While not "physical" development issues, a couple of additional points merit mention in terms of potential impact on a shopping center redevelopment project.

Sometimes small details can have a large impact on form or schedule if they are not addressed early.

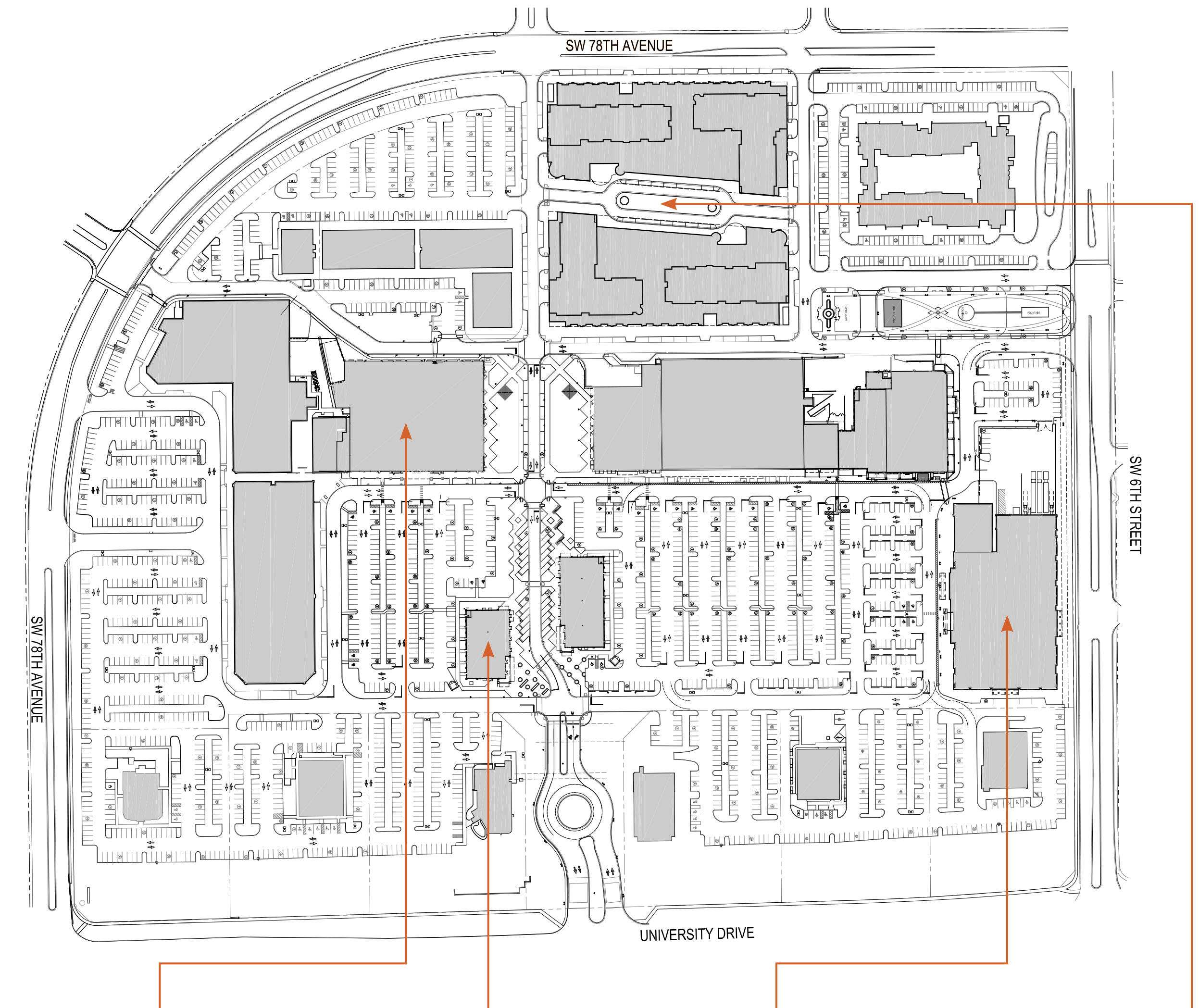
Working with Lenders

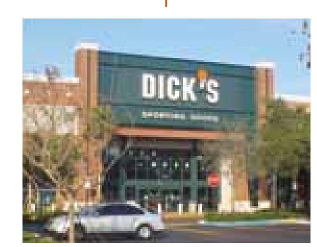
Redeveloping a shopping center may require the owner to engage its lender in the process. This can be challenging for institutional owners if the loan is securitized as it is often not an easy task to get a loan servicer to cooperate. Loan covenants that limit demolition or have other restrictions on activity that could be viewed as a potential impairment of the lender's security can be implicated by the redevelopment plan and will require evaluation. If a portion of the shopping center will be sold to facilitate the redevelopment, then the property being sold will need to be released from any existing loan secured by the asset.

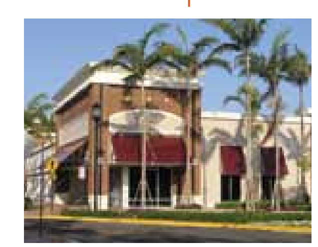
Accounting and Tax Implications

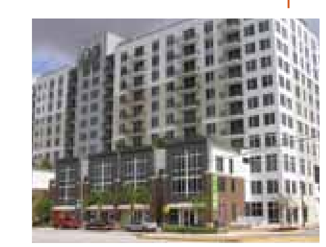
For some property owners, accounting rules may influence the amount of demolition in the redevelopment plan. For example, demolition exceeding a certain percentage of the structures may have adverse tax consequences if it triggers an impairment loss. In general, an impairment can occur if the demolition results in an asset carrying amount in excess of the greater of its net selling price or its value in use. Owners will want to understand the tax and accounting implications of a proposed shopping center redevelopment plan so that any resulting limitations or constraints on the plan can be properly communicated to the design team early in the process.

The Fountains After Redevelopment









Before redevelopment the Fountains had a single anchor tenant (Marshalls), no residential, and poor circulation.

The redeveloped Fountains has three anchors (Kohl's, Dick's Sporting Goods and Marshalls), 478 residential units and excellent vehicular and pedestrian circulation.

Conclusion

As many communities strive to accommodate growth and meet their commercial, residential and civic needs, shopping centers with large surface parking lots offer increasing opportunity for redevelopment, in whole or part, to meet current and projected demand. Opportunities for value creation exist not only in traditional urban core markets but also in suburban communities that initially developed as bedroom communities with strip retail centers and single use properties who are now anxious and struggling to define and develop mixed use areas, town centers or "main street" components.

Balancing the objectives and visions of all the parties requires patience but the rewards can be great—for owners, tenants and the community.

Redeveloping an operating shopping center asset that is ingrained in the community fabric is invariably more complicated than developing vacant land. As demonstrated with the redevelopment of the Fountains Shoppes of Distinction, balancing the objectives and visions of the owner, tenants and the community and executing the project will require a capable multi-disciplinary team and a good deal of patience and fortitude. However, the rewards can be great—for existing tenants who ultimately find themselves in a more vibrant environment, for the community that can enjoy the economic and lifestyle benefits of a successfully redeveloped shopping center, and importantly, for shopping center owners who can extract additional value from their holdings.

About the Author

Paul D'Arelli is President of National Development Advisors and provides development advisory services to retail asset owners nationwide. He was a land use attorney with Greenberg Traurig when he executed on The Fountains project. He has substantial experience with complex mixed use redevelopments, with an emphasis on mall and shopping center assets. He is admitted to practice law in Florida and California and is a Licensed California General Contractor.

pdarelli@ndadvisors.com or 954.647.1363

National
Development
Advisors, Inc.

www.ndadvisors.com