

# **A SUCCESSFUL LANDLORD-TENANT RELATIONSHIP; HOW TO OVERCOME NEGOTIATING CHALLENGES**

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## GENERAL INTRODUCTION

- ❖ Negotiating tips : Importance of learning the techniques of negotiating lease deals that will result in win-win situations with many long-term benefits
- ❖ Importance of anticipating market fluctuations in order to determine whether to engage in a short, mid or long-term lease
- ❖ Incorporating lease language that will protect both parties in case of change of circumstances (landlord sells the building, tenant changes personnel) -the person across the negotiating table might not be the person that you will be dealing with a few years down the road
- ❖ When entering into a lease, parties should be looking to anticipate and prevent legal problems and litigation from the start

## A FEW TIPS THAT BOTH PARTIES TO A COMMERCIAL LEASE SHOULD KNOW

### *Pre-negotiating stage*

- ❖ Being aware of the legal status of landlord and tenant: Parties to a lease should know their legal rights and obligations and should have a good idea about the person with whom they are contracting in order to avoid problems throughout the term of the lease
- ❖ Negotiating power depends on whether rental market is hot or cold
- ❖ Preliminary agreements such as Letter of Intent, Tenant's Proposition and Offer to Lease (careful it's binding!): these agreements are a way of "testing the waters"

### *At the negotiating stage*

- ❖ The general law on duty to negotiate in good faith
- ❖ Avoiding jargon and ambiguity at the negotiating and drafting stage: if the lease has not been carefully drafted, a "hiccup" can become a major problem for one of the parties

### Important Elements for the Tenant to Keep in Mind

- ❖ Standard Form Lease: Tenants beware! Terms usually favour the landlord, but all terms are negotiable ( in theory at least)
  - importance of reviewing the lease document: Standard Form Lease usually represents the Landlord's wish list
  - if not appropriately modified, may not serve the tenants' interests when issues arise. On the other hand, a sophisticated tenant will often request changes to the lease that, if not fully understood, can cause unforeseen difficulties for the landlord.
- ❖ In all cases, it is always important to make sure you understand and agree with the basic terms of the lease before you sign it (amount of rent, length of the lease and configuration of the physical space)
- ❖ Making sure the lease fits your business needs: The success or failure of your business may ride on certain terms of the lease which is why it is crucial to carefully investigate the terms of the lease agreement to make sure it meets your business's needs. For example, if your business requires modifications to the existing space, it is important to make sure that one of the two parties (landlord or tenant) will make the necessary charges



Important Elements for the Landlord to Remember:

- ❖ Being conscious of a particularly powerful tenant: a sophisticated tenant will often request changes to the lease that, if not fully understood, can cause unforeseen difficulties for the landlord.

Important provisions to include: For the Tenant and for the Landlord

Tenant :

- ❖ Proper description of premises (area, title of Landlord, due diligence)
- ❖ Rent
- ❖ Additional rent obligations
- ❖ Operating costs and taxes
- ❖ Co-tenancy obligations
- ❖ Penalties
- ❖ Term, options, renewals and extensions
  - When does the Term actually commence?
  - ensure do not surpass 40 years
  - Are there time periods during which the Commencement Date should not occur, from the Tenant's perspective?
  - Are there conditions precedent to be satisfied before the Commencement Date can occur?
  - 10 year term vs 2 years +3 years + 5 years, with the latter two options being exercised at the signing of the Offer;
  - difference between option to "renew" and option to "extend", in terms of the entry into a new lease or the continuance of an existing lease, and how this impacts the obligations as regards how the premises are to be left at the end of the term;
  - rental rate in option period to be "no less than that in the last year of the initial term", and how Allowance payable to Tenant impacts this concept;
  - Is exercise of option governed by *de rigueur* delays and "never been in default" prerequisites?
- ❖ Construction obligations
  - who builds what;
  - how extensive are the construction obligations of the parties (turnkeys, build-to-suit, etc.);
  - whose plans are used, who gets the permits, can the parties do their work together;
  - what happens if work is delayed (e.g. penalties, added time, right to walk and obtain reimbursement of costs incurred);
  - ensure to "carve-out" Quebec construction holiday periods (summer and winter);



- when does tenant's Fixturing Period begin
- ❖ Repairs and maintenance
  - major repairs vs. minor repairs, capital expenses to be amortized over useful life (with or without interest); minimum guarantee periods for elements of Landlord's Work;
- ❖ Operating covenants and ability to "go dark"
  - depends on whether use is retail, office, industrial;
  - what are rights and obligations if tenant wants to, and does, "go dark";
  - if tenant "goes dark", does landlord have the right to terminate after a certain time period, and if so, should tenant have "backfill protection";
  - Quebec law will allow for mandatory injunctions, unlike common law courts;
- ❖ Allowances and inducements
  - how they are dealt with by each of the landlord and the tenant;
  - rights of tenant if amount is not paid;
- ❖ Use, exclusivities and radius clauses
  - important to draft clearly;
  - obligation to verify title to see if anything exists that might affect tenant's use, or to ensure nobody else has been granted same exclusivity;
  - ability to impact adjacent properties;
  - how to ensure will be protected, given Quebec law's refusal to allow for restrictive use easements, unlike common law courts (although recent case of *Demik Properties (Sorel) v. Canada Austin Group Co.*, Superior Court, February 19, 2010, may breathe new life into the concept)
  - legal options available if determine third party breach exists;
  - any uses prohibited on the Property (e.g. affect parking, undue noise, noxious smells, sexual activities)
- ❖ Signage rights
  - can tenant put up its standard signage;
  - any restrictions on size, location and numbers;
  - pylon signs rights (where, how large, both sides);
- ❖ Access and no-build areas
  - to protect visibility of premises from parking lots, roads, and other sight lines, etc.;



- to ensure parking ratios are respected at all times during term (N.B. verify parking ratios in advance, if of importance to tenant);
- ensure no right on part of landlord to eliminate entrances or exits from site, as well as lay-out of parking lot (e.g. donut shop in parking lot of mall in Ontario);
- ❖ Closing of other tenants
  - are there minimum percentages of occupancy required, before the tenant is (i) obliged to open, or (ii) entitled to only pay percentage rent or terminate the offer/lease;
- ❖ Sweeteners:
  - Free rent
  - Tenant inducements
  - Build-to-suit
  - Exclusivities
  - Rights of first refusal
  - Rights to expand
  - Right to pay only % rent if certain occupancy rate not attained, coupled with right to cancel if situation continues for more than a certain number of months
  - Right to “try it out” i.e. pay % rent only for a certain period of time in order to determine if the premises will be successful or not, if not happy can walk, and if happy continue with lease (with Minimum Rent based on % rent paid in trial period)
  - Back fill protection (can’t put back premises of same kind)
  - No shift clause
  - Ability to determine when, and when not, to open premises (in other words if Landlord cannot provide premises prior to certain date, Tenant can postpone opening, which is important in fashion industry); this should be coupled with obligations on the part of the Landlord to pay the Tenant for lost profit of merchandise ordered which could not be sold by the Tenant due to its inability to open
  - Restrictions on the part of the Landlord to do things which could adversely affect the Tenant’s visibility, proximity to majors, entrances and exits
  - Gross rent and/or caps on expenses and/or taxes
  - location, location, location!



## Landlord

Same issues as tenant, in addition:

- ❖ Right to postpone construction if number of tenants does not hit minimum leasing % or right to terminate offer
- ❖ Security deposit, movable hypothec, securities
- ❖ Assignment and sublet;
  - Quebec law provides for novation in circumstances where assignment occurs and nothing stated in offer/lease as regards continuing liability (unlike situation in common law provinces);
  - option to terminate in lieu of consent, with right to take back request;
  - added amounts payable in circumstances of assignment/sublet, and who keeps what;
  - “bump” in rental rate if assignment/sublet;
  - automatic right to assign/sublet if to related person or to public company;
  - change of control clause and exclusions therefrom;
- ❖ Control of the development
  - relocation of premises, at any time, from time to time, at tenant’s cost or landlord’s cost;
  - type of businesses allowed in development;
  - ability of landlord to terminate offer/lease if wishes to demolish or renovate building;
- ❖ Insurance, liability and indemnity;
  - when tenant pays share of landlord’s insurance, considered additional insured;
  - waiver of subrogation, cross-liability and severability of interest;
  - cap on maximum liability;
- ❖ Damage and destruction;
  - maximum time for rebuilding;
  - what if premises not damaged but access to premises is materially adversely affected;
  - termination by landlord of offer/lease despite fact premises not damaged;
  - right to re-lease if termination and subsequent rebuilding within ● years;
  - abatement of minimum rent, additional rent, until landlord finishes work, tenant finishes work, or no abatement if damage caused by tenant;



❖ Default:

- automatic (ipso facto) right to terminate;
- difference between bankruptcy and other defaults;
- notice to cure;
- right to cure at all times or waiver of ability to do so;
- penalty clause if default.

