

# LEASING LESSONS LEARNED FROM THE ALBERTA FLOOD

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As the New Year has begun, it is a good time to ponder the major events over the past year and the lessons learned from them. The most significant event for Calgarians and those in Calgary's surrounding area was the flooding that occurred in June of 2013. The flood was coined as a "100 year flood" and, though unlikely to reach the same magnitude in the near future, has resulted in people grappling with issues they never thought would arise. Among those impacted were commercial landlords and tenants who are now reviewing and re-considering their leases in light of the substantial losses from the flood. As well, those who are negotiating new leases are carefully considering provisions that may not have been of much concern in the past. Some of the leasing issues that have arisen and should be considered for the future are set out below.

## **Damage and Destruction**

The most obviously applicable clause is the damage and destruction clause. The typical commercial lease has a provision dealing with the effect of damage to, or destruction of, the leased premises and the building in which they are located. Usually these provisions are drafted such that if the premises are damaged to the extent that all or a portion of the premises are not usable by the tenant, the rent abates, either fully or in proportion to the percentage of the premises damaged, until the premises are repaired. This provision may also allow one or both of the parties to terminate the lease if the premises cannot be restored within an agreed upon period of time.

It is also very common to have a separate provision that provides that if the building, but not the premises, is damaged such that the building cannot be restored, the landlord has the right to terminate but the tenant does not.

The flooding resulted in the unforeseen situation for many tenants whereby premises located above the flood waters were not damaged while the electrical and mechanical servers on the bottom floor were damaged extensively. This has resulted in significant periods of time where tenants were unable to use their premises but, as their premises were not damaged, they did not have the right to terminate their leases. Going forward it would be wise for landlords and tenant to consider what they want to happen should the building be damaged to the extent that the premises are unusable but, not themselves, damaged.

### **Force Majeure Clauses**

As many landlords and tenants can attest to, the flooding led to the increased importance of the *force majeure* clause. While many contractors were involved with the flood recovery, it became very difficult to get tenant improvements or other work completed within agreed upon time constraints. A properly drafted *force majeure* clause should allow for delays of this nature and set out the rights and obligations of the parties in the event of unavoidable and unforeseen delays. Thus both landlords and tenant should be taking a second look at standard *force majeure* clauses to ensure they are sufficient to deal with delays for all unforeseen circumstances.

### **Business Interruption Insurance**

The flood had a significant impact upon a number of businesses, whether due to damage to the premises or inaccessibility for their customers, and some of them were not able to recover and ultimately went out of business. This obviously impacted landlords as they were losing tenants at a time during which much of their attention was focused on restoring their buildings. For those landlords whose leases contained a requirement that the tenant maintain business interruption insurance, the losses were reduced significantly, as the tenants were not put in a position where they were unable to pay rent, and thus the landlords still had income from rents while they were restoring their buildings.

### **Landlord's Insurance**

Many tenants do not concern themselves with whether or not their landlord has the obligation under the lease to maintain adequate insurance. Overlooking this area of the lease could prove to be extremely costly as the tenant may have adequate insurance to cover the damage to its premises but this will be of little benefit if there is no electricity or other services to the premises because the landlord did not maintain adequate insurance.

### **Damage Deposits**

To the extent that tenants had provided landlords with deposits to cover any damage done to the premises during the term of the lease, there have been disputes as to whether the deposit was recoverable by the tenant where the premises were damaged due to flood. From a tenant's perspective, the tenant would argue that the deposit is to cover damage actually caused by the tenant and thus, the landlord could not retain the deposit. From the landlord's perspective, there was damage to the premises during the term and the landlord should have the right to access the deposit to offset the cost of restoring the building including, where required under the lease, the premises. An adequately drafted deposit clause should clearly provide if and when the damage deposit is accessible.

### **Provision of Services and Utilities**

Quite often a landlord is obligated under its leases to provide certain services and utilities to tenants. Catastrophic events such as a major flood may interfere with a landlord's ability to meet this obligation. Leases often contain a clause to the effect that the landlord is not responsible for any losses suffered by the tenant as a result of the landlord's inability to provide these services. Landlords and tenants would be wise to review this provision and its consequences in future negotiations.

### **Conclusion**

Although these issues have come to light due to the flooding in southern Alberta, they are not specific to Alberta. These issues should be considered by all landlords and tenants as there is the potential for substantial losses when overlooked.

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### **A cautionary Note**

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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