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Commercial Leasing Bulletin:

Landlord Redevelopment Rights – The Details Matter!

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Introduction

Commercial landlords often try to maintain as much flexibility with their tenants as possible in order to allow themselves the opportunity to redevelop their properties in the future. The method for achieving such flexibility typically comes in the form of a demolition or "demo" clause contained in the landlord's standard form of lease. The "demo" clause is intended to give a landlord the unilateral right to terminate the lease if the landlord wishes to demolish, alter, or redevelop the property.

Landlords and tenants alike have probably already seen, heard, or read about the surge of redevelopment in the industry. Thanks to the pandemic, the trend is bound to continue well into the future. As a result, now is a good time to take a closer look at the "demo" clause.

A Material Term

It is well established in law that for an agreement to lease to be binding, the following essential elements need to be clearly identified:

1. the parties;
2. the premises;
3. the commencement date;
4. the duration of the term;
5. the rent; and
6. any other material terms (which have subsequently been defined by case law).

Parties often spend a lot of time negotiating these elements as part of an offer to lease before entering into a formal lease agreement. Canadian case law has established that any material terms that are not incidental to the landlord-tenant relationship must also be included in an offer to lease for a landlord to insist or rely on such terms in a formal lease agreement.[1] A "demo" clause is one such material term. A landlord cannot subsequently introduce a "demo" clause in their standard

[1] *Canada Square Corp. et al. v. VS Services Ltd. et al* (1982), 34 O.R. (2d) 250 (C.A.)

lease form when a binding offer to lease did not include one.[2] A prudent landlord should therefore consider one or both of the following:

i) include in the offer to lease a provision that the parties agree to execute the landlord's standard form of lease with an express acknowledgement that the standard form of lease contains a demolition clause in favour of the landlord (and which standard form is sent to the tenant prior to signing the offer); and/or
ii) include the actual "demo" clause in the offer to lease.

Not What You Expected?

The "demo" clause is generally intended to broadly apply to a number of different events and not necessarily just the demolition of a property. For a "demo" clause to have such a broad application, it needs to be drafted to that effect. The following two cases are cautionary examples which show how a "demo" clause can fail to have the intended effect.

In the British Columbia case of *0723922 B.C. Ltd. v. Karma Management Systems Ltd.*,[3] the lease included a renewal option in favour of the tenant. The renewal clause indicated that "the option period shall contain a demolition clause with one hundred and eighty (180) days written notice to be provided"[4] if the landlord chose to demolish the premises. The tenant never actually exercised the renewal option but the lease continued past its original expiry date as a month-to-month tenancy. The landlord attempted to terminate the lease on the basis of the "demo" clause and gave the tenant 180 days' notice to vacate. The Court found that the "demo" clause was not a valid basis upon which the landlord could terminate, as the tenant never exercised its renewal option. As a result, the landlord's termination notice was not effective.

The case is paradoxical as it was open to the landlord to terminate the lease on one month's notice since the tenancy was month-to-month. Nevertheless, it's an example of how a "demo" clause failed to have its intended effect.

In the recent Ontario case of *Meridian C C Intl Inc. v. 2745206 Ontario Inc.*,[5] the lease contained a "demo" clause whereby the landlord had the right to terminate on 180 days' notice if the landlord desired to remodel or demolish any part of the premises "to an extent that renders continued possession by the tenant impracticable." The landlord relied on the "demo" clause in terminating the lease and provided the tenant with the requisite notice. The tenant resisted the termination. At first instance, the Ontario Superior Court found that the landlord was entitled to rely on the "demo" clause and properly terminated the lease. The tenant appealed the decision and the Ontario Court

[2] *Goh v. M.H. Ingle & Associates Insurance Brokers Ltd.* [1987] O.J. No. 1341 (S.C.)

[3] 2008 BCSC 492

[4] *Ibid.*

[5] 2022 ONCA 12

of Appeal held that the lower court failed to determine the factual question of whether the landlord's proposed renovations rendered "continued possession by the tenant impracticable." The matter was referred back to the Superior Court as a result. Although this case is not finally determined, the qualified "demo" clause referred to above provides an example of how a seemingly innocuous few words can backfire on a landlord.

Conclusion

Redevelopment is a natural part of the commercial leasing landscape. Without careful planning around "demo" clauses, landlords can face major challenges in carrying out their redevelopment plans in the time and manner they envisioned.

It is critical for landlords to ensure they have an enforceable "demo" clause drafted to have the intended effect that is consistent with future redevelopment plans. Unfortunately for tenants, it is generally an uphill battle when it comes to "demo" clauses as they are often presented as a "take it or leave it" part of the deal. Tenants can still try to negotiate the "demo" clause to be as specific as possible in order to apply only in rare or limited circumstances.

We will continue to provide regular updates on commercial leasing issues in Canada. If you have any questions or would like to obtain legal advice on any leasing issues or commercial leasing litigation, please contact any lawyer in our **Commercial Leasing Group**.

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