Commercial Property Leases - Friend or Foe?

Leasing of premises are commonplace in business and the process involves negotiations between the **'Landlord'** and **'Tenant'** who agree **'Heads of Terms'** which are expressed in the formal lease for signing. The relationship between a landlord and a tenant of a business premises is set out under the **Landlord and Tenant (Amendment) Act 198**0 as amended by the **Landlord and Tenant (Amendment) Act 1994.**

Leases are generally contracts under seal and are therefore legally enforceable. Most are drafted using standardised Law Society templates for familiarity in structure and that nothing important is omitted. A word of warning though! Don't assume that all leases are alike – every document needs to be read and understood in its own context. The composition of the lease provides definitions of, inter alia: The **Parties** involved, the **'Demise'** (the premises to be transferred by lease) the **'Covenants'** on the part of both the Landlord and Tenant together with various **'Conditions'** applying overall. Appending you will also find bespoke elements or **'Additional Schedules'** which might include: inventories of assets, assignments, deeds of variation, photographs etc. These additions are referred to throughout the main body of the lease and, accordingly, the lease must be read and interpreted as a whole.

A tenant might occupy an entire **Building,** however in many cases they occupy only a portion of a Building; i.e. **'the Premises'.** Most leases are written on a **'Full Repair & Insuring basis'** (FRI). This refers to the Tenant's obligation to maintain/ repair the premises for the duration of the agreement but also the requirement to pay the Landlord's insurance premium. Many professionals misinterpret the meaning of an FRI lease to suggest that the Tenant has responsibility for actually arranging the Buildings insurance policy but this is very rarely the case. The tenant, of course, will have arranged a separate policy of insurance in respect of their own business assets.

The Landlord will have covenanted to arrange a Buildings insurance policy for **'Specified Risks'** which are each listed in the agreement. Thus, when an insurable loss occurs, the tenant is not obligated to repair that damage and furthermore a **'Cessor of Rent Clause'** removes the obligation for payment of rent until such time as the premises are again fit for occupation. Deficiencies in the insurance arrangements, whether voluntarily assumed by a client or due to poor advice by the client's professional advisors, usually only come to light when a loss occurs, and this very often results in undervalued claim settlements accompanied by customer dissatisfaction. In most, if not all cases, such issues could have been easily avoided had the lease been referred-to when evaluating the client's insurance requirements. Some typical examples that we have encountered in our handling of losses both small and multi-million Euro value include:

- The specified risks insured by the landlord may exclude an important peril exposing the tenant who is responsible under the lease for all repairs.
- The tenant may have undertaken **'alterations and improvements'** to the premises but the landlord may not have insured them if the lease did not stipulate, and the tenant might have required **'Tenants Improvements'** cover separately.
- Rents are sometimes turnover-rated or subject to revision after year one. The sums insured might be inadequate, thus affecting claim entitlements or may be overstated thus overcharging premium.
- A **'quiet enjoyment'** covenant that imposes special reinstatement obligations for the landlord might constitute a material fact requiring disclosure or may impact the Value at Risk.
- The **Cessor of Rent** clause may be restrictive e.g. all aspects of rent might not be relieved or the rent might become payable again when the premises are **fit for occupation** irrespective of whether they are fit for use (fitted out) by the tenant.
- Whilst the Landlord is obliged to reinstate **with reasonable speed,** what does that mean and how long is that? The tenant has no control over that situation when a loss occurs. Many assume that the landlord will drop everything and that the building insurers will pay out immediately. The reality, from our experience, particularly high value losses, is that there are often very lengthy delays before liability is accepted. This 'period of claim investigation' is often overlooked when calculating the timeframe for reinstating a property. Indeed, the landlord may have the option in the lease not to reinstate at all or perhaps planning objections may delay or prevent reinstatement altogether, which would warrant special insurance arrangements for a client.

John Davis BIO: John's career in insurance commenced in 1990 with Church & General/Insurance Corporation of Ireland (now Allianz), working in underwriting and claims. In 1997 he joined a leading loss adjusting firm Scully Tyrrell & Partners (now Sedgwick Ireland), with ultimate responsibilities in the adjustment of large and complex property losses. He joined Associated Loss Adjusters (now Davies Ireland) in 2010, where he became a director of the company. John has also served as president of his local Insurance institute in 2001 and has supported his professional institutes over the course of his career. He is a Chartered Insurance Practitioner (ACII) and a Chartered Loss Adjuster (ACILA) and is also a Fellow of the International Federation of Adjusting Associations (FIFAA). He has a particular interest and expertise in the management of all types of commercial and industrial complex property losses and is experienced in the constructive interpretation of policy wordings and clauses.

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John Davis, Chartered Insurance Practitioner, Chartered Loss Adjuster, Owens McCarthy

When a loss occurs as a result of negligence then all third parties who have incurred a resulting loss will want to recoup their losses if they can.

Consider: Mark Rowlands v Berni Inns Ltd., 1985

The plaintiff leased his basement to the defendant. The building was destroyed by fire caused by **negligence** of the defendant and the plaintiff's insurer, having paid under their policy, sought to recover from the defendant. It was ultimately concluded that ***'...The intention of the parties... must have been that... whether due to accident or negligence, the landlord's loss was to be recouped from the insurance moneys and that, in that event, they were to have no further claim against the tenant for damages in negligence'.*** This case has been relied upon as a defence to various recovery actions arriving before the courts but has also prompted a re-think of lease wordings by the artistic legal minds out there.

Consider: High Points Estate Ltd (HPE) v Prezzo 2018.

High Point Estates Ltd (HPE), leased part of the ground floor and basement to **Prezzo Ltd**. A fire, caused by negligence of Prezzo, caused substantial damage to the premises (portions of the building occupied by Prezzo) but also spread to the rest of the building. HPE's insurers indemnified them for damage to the entire building and subrogated to recover from Prezzo. Prezzo immediately claimed immunity under **'Berni Inns',** however, it was discovered that, in the lease wording, HPE had only agreed to insure the '**Premises**', otherwise they would have included the word 'Building' instead. The immunity established in **'Berni Inns'** therefore only provided protection to Prezzo in respect of the **Premises** that they occupied and HPE recovered their losses for damage to remainder of the whole Building. The decision in this case supports the crucial importance of the terms of the lease in deciding whether the principle of **Berni Inns** applies and highlights potential exposures for both Landlords and Tenants which cannot be overlooked by Brokers and underwriters alike when considering the risk and covers required.

We can say with certainty that a copy of the lease is, without exception, always sought by the Insurer when a claim is being considered. In the same vein, Brokers and Agents should retain a copy of the lease on their own file, having first considered the respective obligations and creation of insurable interests that potentially arise therefrom. Similarly, the absence of the lease on underwriting files, might exude recklessness leading to potential exposures as seen in HPE v Prezzo. In our experience, as Policyholder Advocates, better claim outcomes are often achieved where the Insured's Broker/Agent has engaged with their client (pre loss) and reviewed the details and obligations created by the commercial lease. Moreover, settled case law would suggest that there is indeed an obligation upon Insurance Brokers to consider and clarify terms of leases for their commercial clients in order to ensure that the insurance ultimately arranged coincides with the needs created within this critical contract.