

The Six-Minute Commercial Leasing Lawyer 2017

**RELOCATION PROVISIONS: GETTING IT RIGHT.
HOW MUCH CERTAINTY IS TOO MUCH?**

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With sincere thanks to our then articling student, Hoi Ki Cheung, for her research.

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Introduction

The landlord's right to relocate its tenants is arguably a necessary part of the landlord's arsenal to properly manage, develop, operate and renovate its property – a necessary evil, so to speak. That said, unless the lease specifically grants the landlord the right to relocate a tenant's premises, the landlord is not permitted to do so. There is no common law right in favour of a landlord permitting it to compel a tenant to surrender its premises and relocate to other premises. As such, the precise wording of the relocation clause in the lease will define the landlords' relocation rights, including the manner in which the relocation will take place, the location of the relocated premises, and the features that the relocated premises must possess.¹

Understandably, the landlord's proposed right to relocate is a source of much discussion and dialogue – unless there is no discussion at all and the tenant either does not care, or does not realize the ramifications of signing the landlord's standard provision or does not enjoy the leverage to address it. On the other hand, some tenants seek to so constrain the location to which the premises can be relocated and the required features of the relocated premises as to negate the landlord's right.

This paper tries to canvas the concerns that should be addressed, or at least considered, in discussing the scope and terms of a relocation provision. That said, the specific concerns of a particular tenant are as unquantifiable as the possible attributes of any particular space and the wants and needs of the occupier, but hopefully this paper gets the thought processes started, keeping in mind the bargaining power of the parties will also vary and this in itself will dictate the extent to which these rights are negotiated.

Part 1: The Landlord's Perspective

Why is a relocation provision necessary? Without it, a landlord would not have the right to require a tenant to relocate its premises at the landlord's behest. When a landlord enters into a lease, it grants the tenant exclusive possession of the premises. Landlords want/need relocation rights in order to provide them with the freedom to reconfigure and redevelop their properties, to accommodate new tenants and the growth of existing tenants, to change the tenant mix and to remerchandise the centre. Landlords are looking to ensure that they have the flexibility to operate the property to maximize value. To this end, landlords should ideally aim for the absolute right and discretion to move tenants to any location at a moment's notice for any reason.²

¹ Annette Lambert & Shanlee von Vegesack, "Protecting Your Tenants: Tips for Negotiating Demolition and Relocation Clauses", *The Retail Newsletter* (2014) 3 at 3.

² Diana Sanders, "Move it lose it: relocation provisions in commercial lease agreements" (August 20 2015), online: Mondaq <<http://www.mondaq.com/unitedstates/x/421854/landlord+tenant+leases/Move+It+Or+Lose+It+Relocation+Provisions+In+Commercial+Lease+Agreements>> [Sanders].

To achieve this objective, landlords will want to:

- avoid making representations about or agreeing in advance to required characteristics of the relocated premises (e.g. do not specify the location, the size, the configuration, visibility, access of the relocated premises)
 - If the tenant insists on describing the characteristics of the relocated premises, limit them to objective criteria such as the size, the frontage, and the configuration of the relocated premises.³
 - Subjective criteria like visibility, exposure, and traffic, should be avoided⁴ as what is reasonable will depend on the party's perspective.
- avoid having to provide significant advance notice periods to the tenant
 - If the tenant insists on a long notice period, this must be balanced against the possibility/probability the landlord will forfeit the business opportunity it is pursuing.⁵
- state that the landlord has the right to relocate the tenant - do not elaborate on the circumstances when this right may be exercised by the landlord
- limit the compensation to be paid to the tenant
 - ideally, no compensation
 - if the landlord agrees to provide compensation to the tenant, carefully describe the amount to be paid (e.g. consider limit the amount to the then unamortized cost of the tenant's leasehold improvements)
 - if the landlord agrees to reimburse the tenant its costs, limit these costs to direct costs, specifically exclude all indirect costs and require the tenant to substantiate its costs through receipts or paid invoices
- include a right, in favour of the landlord, to terminate the lease if there are no suitable alternative premises to which to relocate the tenant.⁶

³Deborah Watkins & Joseph Grignano, "A few operating issues: relocation and go dark rights" in The Law Society of Upper Canada, *Casting the Net Commercial Lease* (2001), online: Daoust Vukovich Baker-Sigal Banka <<http://www.dv-law.com/docs/default-source/Articles/pdf-3-6.pdf?sfvrsn=2>> 1 at 2 [Watkins].

⁴ *Watkins, Ibid.* at 4

⁵ *Ibid.*

⁶ *Ibid* at 5.

a. The Implications of *Bhasin v. Hrynew*⁷

There has been much discussion and conjecture about the implications of this important decision on all commercial contracting. In *Bhasin v. Hrynew*, the Supreme Court of Canada confirmed that the common law in relation to good faith performance of contracts is piecemeal, unsettled and unclear. The Court found that two incremental steps are in order to make the common law more coherent and just. The first step is to acknowledge that good faith contractual performance is a general organizing principle of the common law of contract and the second is that, as a manifestation of this organizing principle of good faith, there is a common law duty which applies to all contracts to act honestly in the performance of contractual obligations. While the parties are permitted to vary the “precise content of honest performance”, they are not permitted to contract out of the, as yet undefined, “minimum core elements”. So what does this mean in the context of a relocation right in a commercial lease?

Firstly, there is no standalone duty of good faith. An allegation of bad faith must relate to a particular term or obligation in the lease. In this case, a relocation right will presumably be included in the lease and thus the duty of good faith will apply. That said, a landlord will not be able to use *Bhasin* to argue that a relocation right should be read into the lease.

The Supreme Court is clearly requiring parties to perform their respective contractual obligations honestly and reasonably. In the case of the exercise of discretion, this discretion must be exercised honestly and in good faith, even if the lease says it may be exercised in the party’s “sole” discretion. The landlord is permitted to act in self-interest but not capriciously or arbitrarily or in a way that eviscerates or defeats the objects of the lease.

What it means to “be honest” and “reasonable” will depend on the context – including not only the kind of contract in question, but also the nature of the relationship between the parties. As such, while the landlord has the right to pursue its own interests, it must not lie or knowingly mislead the tenant about matters directly related to the performance of the contract.

“Capricious” or “arbitrary” behaviour is contrary to the duty to act honestly. One writer has suggested that the parties document their decision-making processes.⁸ I completely agree and suggest that landlords ensure that minutes be kept of meetings discussing the need to exercise the right to relocate including the reasons behind the choice of which tenants are to be moved and why.

⁷ *Bhasin v. Hrynew*, 2014 SCC 71

⁸ Hayley Peglar, WeirFoulds LLP “A Leap of Good Faith” *Practical Implications of the Supreme Court of Canada’s Decision in Bhasin v. Hrynew for Contracting Parties* on-line www.weirfoulds.com/a-leap-of-good-faith-practical-implications-of-1

A lease is not a one-off contract. It represents a long-term relationship that is quite co-dependant. As such, I suggest that it is very likely that a court will require a high level of honesty and reasonableness.

b. Early Termination for Demolition and Redevelopment

No discussion about relocation rights can be complete without mention of the often present demolition and redevelopment clause in the lease. This provision typically gives the landlord the right to unilaterally terminate the lease, without recourse, if it intends to demolish or substantially renovate the property. While advance notice is generally provided for, there is typically no compensation provided to the tenant as a consequence of the landlord's exercise of this right. As such, this right must be examined in the context of relocation rights. While this right would not assist the landlord where it wants to relocate a tenant in order to accommodate another tenant, it is very useful in the context of the redevelopment of the property.

c. Unilateral Non-Contractual Early Termination by Landlords

Alternatively, a landlord may choose to terminate the lease and compensate the tenant in full based on the common law doctrine of "efficient breach of contract". Under this doctrine, a landlord may elect to voluntarily breach the contract and compensate the tenant for the breach since doing so is less costly than fulfilling the contract.

However, tenants can protect their interest in the leased premises by seeking an injunction from the court to prevent the landlord from terminating the lease. In deciding whether the injunction should be granted, the court will consider the following three questions:

- (i) Is there a "serious issue to be tried?"
- (ii) Will the party seeking the injunction suffer irreparable harm (harm which cannot be adequately compensated by damages? For example, the leased premises has unique features that cannot be found in the relocated premises);
- (iii) Is the balance of convenience in the favour of the party seeking the injunction (i.e. the inconvenience of not granting the injunction outweighs the inconvenience to the other party of granting the injunction)?

The court will consider all of the equities between the parties, and is unlikely to grant an injunction that has the effect of permanently barring the landlords from developing their lands.⁹ In addition, the court will more likely award damages to the tenant rather than an injunction.¹⁰

Part 2: The Tenant's Perspective

Generally, a tenant's aim is to exclude from the lease any right by the landlord to relocate the premises, and if this is not possible, to agree to a relocation clause that:

⁹ *Paquin*, supra note 12.

¹⁰ *Ibid.*

- ensures a seamless transition from the leased premises to the relocated premises with as little disruption to their businesses as possible
- clearly specifies the required characteristics of the relocated premises
- fully compensates the tenant for the relocation, including being reimbursed by the landlord for all direct costs incurred by the tenant to relocate to the new premises (including removing, re-installing, and replacing its leasehold improvements and trade fixtures), and for the anticipated interruption to their business.

Not only will a tenant's concerns vary from tenant to tenant, office tenants will have different concerns than retail tenants. Section 1 of this Part 2 considers the concerns shared by both retail and office tenants. The following sections 2 and 3 canvas the matters to be considered when discussing a relocation right for retail space and office space, respectively.

1. Considerations Shared by Both Retail and Office Tenants

The following are a list of considerations that both retail and office tenants share.

a. Consent

Some writers have suggested that the tenant insist that the landlord's right to relocate be made subject to the tenant's consent. In my experience, this is almost never acceptable to the landlord as it essentially negates the benefit of the relocation clause from the landlord's perspective. In addition, it leaves open what is a "reasonable" in the circumstances. As such, I suggest that if this approach is adopted, that the parties still discuss and stipulate the grounds on which it would be reasonable (and perhaps unreasonable) to withhold consent to a requested relocation.

b. Size

Like Goldilocks, all tenants will want to be sure that the new space is neither too big, nor too small. There are two considerations in relation to size – the usable area and the rentable area.

The tenant will want to ensure that the new premises are not too small. To address this, the tenant will want to stipulate that the relocated premises have a usable area that is not less than *% of the usable area of the existing premises.

From both a budgetary and functionality perspective, the tenant will also want to ensure that the new premises are not significantly larger than the existing premises. That is, that the "rentable area" of the new premises will not be more than 1**% more than the rentable area of the existing premises.

Ideally, the tenant will also want the landlord to agree that if the rentable area of the new premises is greater than that of the existing premises, neither the tenant's basic rent nor its proportionate share of operating costs or realty taxes will be increased i.e. they will be determined as if the rentable area

of the leased premises had not increased. By way of example, the relocation clause should include the following:

“The relocated premises shall have a usable area (measured in accordance with ***) of not less than 95% of the then usable area of the Leased Premises and a rentable area of not more than 105% of the then rentable area of the Leased Premises.”

The relocation clause will need to specify the method for measuring the floor area. Generally speaking, the same measurement standard as applies to the existing premises should be adopted for this purpose.

For added clarity, the tenant should include a statement in the relocation clause that if the rentable area of the relocated premises is less than that of the existing premises, the tenant’s basic rent and proportionate share shall be likewise reduced.

c. Advance Notice

All tenants need sufficient advance notice to make a seamless transition from their existing premises to the new space. What is sufficient will vary from tenant to tenant depending upon a myriad of personal circumstances.

The following should be considered when determining the notice requirement:

- the form of the advance notice (e.g. the notice should be in writing)
- the length of the notice period – 60 to 90 days is quite common if the landlord is doing the build out of the new premises
- the information that the notice must contain. For example:
 - the location and suite number of the relocated premises
 - the proposed date of the relocation
 - the floor plan of the relocated premises
 - a measurement certificate disclosing both the usable and rentable areas of the relocated premises.

In determining the length of the notice period, tenants should consider the time required to:

- advise its clients, customers and suppliers of its impending move
- prepare construction plans for the relocated premises and complete the build-out the new premises (if not done by the landlord)
- physically move from the existing location to the new location¹¹

¹¹ *Watkins, supra* note 2.

- whether the tenant should stipulate any dark periods during which it cannot be required to relocate

d. Leasehold Improvements and Trade Fixtures

The cost to fit-up the new premises may be costly. It will involve replicating the tenant's existing leasehold improvements in the new premises and relocating or replacing its trade fixtures. The parties will need to consider who will be responsible for the cost of doing this work and whether and to what extent trade fixtures are to be relocated and re-used. The landlord will want to avoid any obligation to replicate the tenant's leasehold improvements in the new premises and many landlord standard form leases limit the tenant's rights in this regard to being reimbursed the then unamortized cost of the tenant's initial leasehold improvements. Clearly, this will result in a significant shift of the burden of the cost of the relocation to the tenant. Tenants will likewise want to ensure that, while cooperating with a relocation right, there is no cost to the tenant to do so and that all of these costs will be borne by the landlord.

In any event, the parties will want to consider and address the following:

- stipulate who is to be responsible for (i.e. who will do the actual construction) and who will pay to the cost for the improvements and the trade fixtures
- the scope of the work
- the quality of the trade fixtures and the quality of the materials used to complete the leasehold improvements (e.g. "improved to a standard and using materials of the same or better quality as the leasehold improvements which exist in the leased premises at the time of the landlord's relocation notice")
- the time in which the improvements need to be made (e.g. before the tenant is required to surrender its existing premises and relocate to the new premises)

e. Tenant Compensation

Tenants should be cognizant of the other costs it will likely incur as a consequence of being relocated and should try to have the landlord pay for them. These costs include:

- direct costs – e.g. the cost of physically transporting the tenants' equipment and merchandise, space design, replacement of stationary and business cards, temporary signage telecommunication setup, computer, telephone and IT disconnection and re-connection costs
- business interruption - depending on a tenant's bargaining power, a stipulated rent-free period may be negotiated in compensation to the tenant for this interruption
- costs for damages suffered in connection with the relocation¹²

¹² Randy Shapiro & Arthur Opalinski, "Demolition & Substantial Renovations – The 90 Day Demo Memo!" (2015) ICSC – Canadian Law Conference 2015 at 1-2 [*Shapiro*].

f. Tenant Right to Unilaterally Terminate the Lease

Tenants may also want to consider negotiating for the right to terminate the lease in lieu of relocating if they are unsatisfied with the proposed relocated premises. In that case, the tenant will also want to ensure that they are reimbursed for the undepreciated capital cost of their leasehold improvements.¹³

g. Constraints on the Timing of the Relocation

Tenants who are concerned about the disruption that the relocation may have on their business may consider seeking the following terms:

- the relocation cannot occur during the first or last year of the term of the lease¹⁴
- the tenant will not be required to vacate its existing premises and relocate to the new premises until the construction of the leasehold improvements and installation of the trade fixtures are complete and the relocated premises are ready to be opened for business
- the relocation will be scheduled outside of the tenant’s normal business hours and key business periods (e.g. Christmas or an office tenant’s year-end)
- the landlord is restricted from relocating the tenant more than once during the term of the lease, or not more than once in a specified number of years.

h. Adjusted Rent for the Relocated Premises

There are various reasons why, after being relocated, a tenant may be unwilling to pay the same base rent as was payable for their original premises.

For example:

- the tenant is relocated from a new building (with a higher base rent) into an older building with higher per square foot operating costs
- the tenant is relocated to a new building where the realty taxes are higher
- the tenant is relocated to less desirable space

2. Retail Tenants’ Additional Considerations

a. Parameters of the Relocated Premises

A retail tenant will want to ensure that the relocated premises are substantially similar to the existing premises in terms of size, configuration, visibility, and frontage. In addition, it may be important to

¹³ *Watkins, supra* note 2 at 6.

¹⁴ David N Ross, “So you want to redevelop your property? Don’t forget about those (pesky_ tenants” (July 2013) *McMillan Real Estate Bulletin*, online: *McMillan*

<http://www.mcmillan.ca/Files/156954_so%20you%20want%20to%20redevelop%20your%20property.pdf> [*McMillan*].

the retail tenant that the new premises have the same level of accessibility as their current premises (e.g. the relocated premises have similar proximity to major tenants, entrances, and escalators). Such tenants will need to seek as much specificity as possible regarding the features of the relocated premises when negotiating the relocation right.

i. Configuration

Retail tenants will want to maintain the functional configuration (e.g. the shape of the premises, the ceiling height and visibility) of their existing premises to be sure that the new space will meet their needs.

Consider the following examples of the concerns a retail tenant may have:

- the tenant paid a higher base rent for leased premises with a rectangular configuration that have a lot of frontage and windows that face a busy street and exterior door permitting direct access from the street
- the length of frontage is highly valued for maximizing visibility of the retail space and for providing window display space
- the rectangular shape is effective for providing a large centralized area for the tenant to display their goods that are readily visible from all angles of the retail space

To maintain the preferred configuration, tenants can:

- identify the street(s) that the relocated premises must front
- limit where in the mall/centre the new premises must be located and those areas that they cannot be relocated
- specify the minimum linear feet of frontage that the relocated premises must possess and to what extent this frontage must be open (versus enclosed)
- specify whether the premises must continue to have direct street access.

ii. Visibility

Retail tenants will want to stipulate that the relocated premises must enjoy the same level of visibility or traffic flow or pedestrian traffic as the original premises. You will want to be clear, however, what visibility means to this specific tenant in order to avoid ambiguity.

- For example, visibility can merely refer to an unobstructed view of the tenant's storefront, or it can refer to an unobstructed view of the entire premises (e.g. storefront and any exposed

side of the exterior), as well as any exterior signage on the premises from adjoining sidewalks, parking facilities, and streets.¹⁵

To alleviate any possible ambiguity, the parties will want to:

- specify the degree of interference required for the tenant to rely on the visibility covenant. For example, the landlord will want the obligation to be limited to specify that “landlord will not permanently, materially, adversely affect visibility...”
- clearly define the part of the premises which is the subject of the visibility covenant (e.g. “landlord will not permanently, materially, adversely affect visibility of the storefront of the premises...”)
- clearly define the vantage point from which visibility will be protected (e.g. “landlord will not permanently, materially, adversely obstruct the visibility of the storefront of the premises from the parking facilities located within fifty (50) feet directly in front of the storefront of the premises”)
- identify the street(s) that the relocated premises must front
- address whether to stipulate a liquidated damage claim or other specific remedy for a breach of the obligation.

iii. Frontage

Frontage refers to the length of a property line on the front side of the property. Retail spaces with the benefit of a large frontage enjoy improved visibility and exposure of the premises and serve as advertising space. Naturally, tenants will want to ensure that the frontage of the relocated premises is not less than that of their existing premises. To achieve this objective, tenants should consider:

- specifying the minimum frontage length that the relocated premises should possess, including the length of the window frontage
- stipulating a rent reduction if the frontage of the relocated premises is smaller than the desired minimum length.

For example, the tenants may opt for the following in the relocation clause:

“The new premises shall (i) front ABC Street or XYZ Street, (ii) have either street window frontage or mall window frontage of not less than ■ (■) linear feet, (iii) if either the street window frontage of the new premises or the mall (i.e. interior) frontage is less than ■ percent (■%) of the then street window frontage or mall window frontage of the then Leased Premises, the annual rate of Basic Rent per square foot of the Rentable Area of the new

¹⁵ Jamie Paquin, “Do You See What I see? Most Likely Not! Visibility Covenants in Commercial Leases” (July 30, 2014), online: Daoust Vukovich LLP <http://www.dv-law.com/docs/default-source/Articles/visibility_covenants_in_commercial_leases.pdf?sfvrsn=0> [Paquin].

premises shall be reduced by ■ percent (■%) for each ■ percent (■%) or portion thereof that the frontage is reduced below such ■ percent (■%).”

iv. No-Build Zones

Retail tenants may have negotiated to include certain stipulated no-build zones in their lease, as well as restricted covenants from the landlord protecting the visibility of the tenant’s signage and premises, unimpeded access to the premises and stipulations regarding the ratio and location of the available parking spaces.

In negotiating the location of the relocated premises, retail tenants will need to take the current location of the no-build zones and stipulated rights regarding visibility, access and parking into account in the context of the possible location of the relocated premises and make the necessary adjustments.

v. Access and Proximity Issues

Maintaining the same level of access will often be extremely important to retail tenants. Tenants who are located in areas with a high amount of foot traffic, such as on the first floor of a mall or who are located near the mall entrance or by the elevators, will want to ensure that the relocated premises to be similarly situated. Likewise, it may be important to a retail tenant that its premises remain in close proximity to a particular tenant or that they remain part of a particular retail hub. Below are some issues that such retail tenants should consider in their negotiation of the landlord’s relocation rights:

- the manner in which their customers will get to the space (e.g. whether the property needs to be on the ground floor, by a major entry way, by the elevators, escalators, or stairs)
- the number of access points that the relocated premises must have
- the location of those access points
- whether the relocated premises are handicapped accessible¹⁶
- the quality of the access corridors e.g. that the interior access be commercially reasonable and with appropriate décor so as not to appear to be a service corridor
- maintaining proximity to particular tenants or remaining part of a particular retail hub.

b. Parking Ratios

Commercial leases may contain a clause addressing the number of parking spaces available to the tenant by using “parking ratios.” This term describes a ratio of allocated parking spaces per square foot leased (e.g. 1:1000 means one parking space for every 1000 square feet of leased space).

¹⁶ Paquin, *supra* note 13; ABA Relocation, *supra* note 12.

Tenants should consider stipulating that the relocated premises maintain the same parking ratio and proximity to available parking as their original premises.

3. Office Tenants' Additional Considerations

a. Parameters of the Relocated Premises

Office tenants will want to ensure that the relocated premises are substantially similar in terms of size, configuration, visibility, and frontage to the existing premises. In addition, an office tenant may want to ensure that the relocated premises will enjoy the same level of accessibility as their current premises to suit the needs of their clients. They may be concerned about natural light, vista and a host of other characteristics that made them decide to lease their existing premises.

As such, office tenants should seek as much specificity as possible regarding the features of the relocated premises when negotiating the relocation clauses.¹⁷

The following sections will explore the specific parameters that are frequently negotiated.

i. Configuration

Even office tenants want to maintain the configuration (e.g. the shape of the premises, the height, the vista, access to windows) of their existing leased premises so that the arrangement of their new space will continue to suit their needs and the needs of their clients/customers. When acting for an office tenant, you will want to canvas what attributes of the existing premises need to be preserved and replicated in the new premises.

For example:

- most office tenants will want to ensure that the new premises maintain the amount of natural light in their space
- where the space is located in the building will impact, either positively or negatively, on the views enjoyed from the premises, you may want to identify what side of the building the relocated premises can be relocated to in order to preserve certain vistas and to provide that the relocated premises cannot be relocated to a floor below a stipulated floor of the building
- it may matter to the tenant where on the elevator bank the premises are relocated in buildings with low/high rise elevator banks
- the actual configuration of the space will often matter – some office tenants require a large amount of core space, while others do not

¹⁷ Paquin, *supra* note 13; ABA Relocation, *supra* note 5; Watkins, *supra* note 2 at 3-4.

- office tenants may not want to be relocated to crossover floors to avoid losing valuable office space

ii. Vista and Other Attributes of the Existing Premises

Tenants whose premises enjoy a particular vista (e.g. Lake Ontario, Parliament Hill, a sports venue) will want to ensure that the landlord must maintain this vista in selecting the alternative premises, particularly if the desirability of the view has been reflected in a higher rent.

vi. Access

It may be important to certain office tenants that the relocated premises maintain the same level of access in order to best serve their clients' needs. For example, an OB/GYN may be concerned that it not be moved from the ground floor if the building is not serviced by an elevator, and that its offices remain as close as possible to the elevator lobby so that pregnant patients are not climbing stairs or having to walk long distances to access their doctor's office.

b. Parking

Parking rights are sometimes provided for in the lease on the basis of a ratio of parking spaces to rentable area. As such, if the new premises are larger, the tenant should also be entitled to more parking but this is not always the case (and may not be the tenant's desired result) and should be specifically addressed. Often parking rights are dealt with by licensing to the tenant a specific number of parking spaces that it is not tied to the area of the premises.

Conclusion

For some tenants, the location and configuration of their premises will not be very important. But for those tenants whose space is particularly suited to their requirements, a landlord's right to relocate raises a myriad of issues. Even if the tenant understands that the landlord requires this right in order to properly manage the property, those tenants with sufficient bargaining power will contest the scope and breadth of the landlord's proposed right to relocate. The challenge is to find the "right" balance between these competing interests.

The comments contained in this article provide general information only. They should not be regarded as or relied upon as legal advice or opinions. Gowling WLG (Canada) LLP would be pleased to provide more information or specific advice on matters of interest to the reader.