

Limit Liability If You Can't Deliver Timely Possession of Premises

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Here's how to keep the tenant and cut your liability risks.

One of the occupational hazards of leasing commercial property is being unable to deliver the space to a new tenant at the start of the lease term. The delay may be because the current tenant is holding over or your contractors have failed to complete the necessary construction work on time. Maybe you're still waiting for the zoning variances or permits you

need to allow the new tenant to use the property for the intended purpose. Or the holdup may be due to a strike, fire, or some other unforeseeable event beyond your control.

Whatever the reason, delays in delivering possession put you in a precarious position. The tenant might be able not only to walk away from the deal but also sue you for major damages.

Standard leases don't do much to protect landlords against these risks. What's needed, attorneys say, is to be aware of and take active measures to minimize your vulnerability. Specifically, you should negotiate for lease language that limits your liability for delays in delivering the premises while enabling you to keep the new tenant bound by the lease for as long as reasonably possible.

Here's how to negotiate and draft a fair and balanced provision, along with a Model Lease Clause that you can adapt.

Consequences of Delay in Delivering Possession

One of a landlord's fundamental obligations to a new tenant is to deliver the leased premises in the promised condition on the date the lease is scheduled to begin. Failure to make good on this obligation typically puts the landlord in default and empowers the tenant to rescind or terminate the lease without penalty. In addition, tenants may be able to sue the landlord for the damages they suffer as a result of not being able to move in to leased space on the anticipated date, which may include:

- Lost sales and other business income due to not being able to operate in the space;
- Costs of inventory buildup and storage;
- Holdover rent the tenant must pay to stay in its current location while the space remains unavailable; and/or
- Additional brokerage fees and moving costs the tenant incurs in finding an alternative location.

The right lease language can safeguard you from these risks while also providing tenants assurance that they won't be totally left out to dry in the event delays occur. Like our

Model Lease Clause, there are 10 things your lease clause should do.

1. Limit Landlord's Liability for Delays

State that the landlord won't be liable to the tenant if it's unable to deliver possession of the leased premises. Defuse the rescission threat by adding that such delays won't affect the validity of the lease or the tenant's obligations under it. Ask your attorney if your state has a statute allowing tenants to rescind the lease and/or sue for damages in the event of a delay by landlord in delivering possession. If so, you'll also need language indicating the tenant's agreement to waive those rights [Clause, par. a].

2. Include "Drop-Dead" Date to Deliver Premises

Expect tenants to resist the idea of giving up their rights against the landlord for delays in delivering possession, especially if it means waiting for a resolution. While landlords will want as much time as possible to free up the space,

there's a limit to how long tenants will allow themselves to be locked into a property that they can't move into. A fair compromise, according to attorneys, is to agree to a "drop-dead date" on which the lease automatically terminates if the landlord hasn't yet delivered possession of the space.

Having a specific date adds a degree of certainty, allowing the tenant to determine when it can move on to other space and the landlord to determine when it can stop preparing the space for the particular tenant's use. Specify that when and if the drop-dead date termination occurs, neither party will owe any further obligations to the other, except for the landlord's duty to return the security deposit and any prepaid rent to the tenant [Clause, par. b].

3. Negotiate Mutually Agreeable "Drop-Dead" Date

The tenant will want a drop-dead date to come as soon as possible after the lease commencement date while the landlord will want just the opposite. The 12-month drop-dead date provided for in the Model Lease Clause is generous to landlords. Factors to consider in negotiating a drop-dead date with your own tenants include:

- How much, if any, new construction is needed to get the space ready for the tenant's use;
- The nature of the improvements, if any, that the landlord still has to make;
- What zoning variances, permits, or other government approvals, if any, are required to prepare the space;
- How likely the current tenant or occupant is to hold over after its lease term ends; and
- Whether the new tenant will be able to make adequate and cost-effective temporary alternative arrangements in the event of a delay [Clause, par. b.]

4. If Necessary, Allow Tenant to Terminate But Still Include Drop-Dead Date

Some tenants may not accept a drop-dead date and insist on retaining the right to terminate the lease unilaterally if you don't deliver timely possession. Other tenants may agree to a drop-dead date only as the outside date for lease termination and demand the option to terminate *before* the drop-dead date so they can get out of the deal early without

having to wait around. And if the tenant has bargaining clout, you may have to accept its demand to avoid losing a favorable deal.

But even where giving a tenant the right to terminate is unavoidable, you should still push hard for a drop-dead date that falls on a date after the tenant's opportunity to terminate expires. Having such a drop-dead date will benefit you if the tenant doesn't terminate the lease by establishing a point in time after which you'll know you're no longer obligated to deliver possession, freeing you up to find a new tenant whose demands might be easier to meet. The arrangement will also benefit the tenant by providing a backup escape hatch in case it doesn't exercise its early termination rights.

5. Set a Waiting Period for Early Termination

You should also set limits on a tenant's right to terminate the lease, whether in conjunction with or as an alternative to a drop-dead date. Start by requiring the tenant to wait for a set period after the commencement date to terminate the lease. Establishing a waiting period gives you a window to deliver

possession before the tenant terminates. Specify that either you or the tenant may terminate if you can't deliver possession by the last day of the waiting period (the “delivery date”).

The length of the waiting period will be subject to negotiation. Use the drop-dead date as a reference point. For example, a six-month waiting period might be reasonable if the drop-dead date is 12 months after the lease commencement date. If the lease doesn't include a drop-dead date, consider the same factors you would have used to set a drop-dead date to determine the length of the waiting period—although the latter will have to be shorter than the former would have been [Clause, par. c].

6. Limit Time Window for Tenant to Exercise Termination Right

Give the tenant the narrowest possible time window to exercise its termination rights—for example, the 10 days immediately before the delivery date. Keeping the termination window short forces the tenant to make a quick decision on termination. Without such protection, the tenant

may dangle you along as it searches for new space or gauges your progress in preparing the space. All the while, you won't know whether you should keep investing time and money to get the space ready for the tenant or start searching for a replacement tenant [Clause, par. c].

7. Get Grace Period to Deliver Possession

The worst-case scenario is that the tenant will terminate the lease when you're just a step or two away from being able to deliver possession. To guard against this contingency, negotiate for a "grace period" giving you the right to void the tenant's termination notice if you can deliver possession of the premises within a certain period after you receive the notice.

Attorneys suggest asking for a grace period of 60 to 90 days while cautioning that tenants may insist on a much shorter time, in the neighborhood of 10 to 15 days. Thirty days might be a reasonable compromise. "Look to the grace period the lease provides the tenant for nonmonetary obligations,"

advises a Chicago attorney. “If you give the tenant 30 days to cure a default, you should get the same leeway” [Clause, pars. c(2) and (3)].

8. Get Right to Void Termination by Paying Tenant's Costs

The foregoing protections still leave you vulnerable to the risk that the tenant will exercise its termination rights and you won't be able to deliver the premises by the end of the grace period. But there still may be one more card you can play to keep the tenant on the hook: Negotiate for language that allows you to void the tenant's termination notice provided that you pay for the losses it incurs while continuing to wait for possession.

This right might prove extremely valuable if you've already spent considerable time, money, and effort preparing the space and/or the space will be ready soon after the grace period ends. In this scenario, paying the tenant's additional losses might be cheaper and easier than starting from scratch and seeking a new tenant for the space.

Be careful to specify that you're responsible for the costs the tenant incurs *after* the grace period runs out. Also state when your responsibility for the tenant's costs ends. The end date should be when the tenant no longer has to wait for possession, defined as whichever of the following things happens earliest:

- You deliver possession;
- The tenant gets your written notice that you can't deliver possession after all and the lease is terminated (we'll discuss landlord termination rights below); or
- The drop-dead date.

Caveat: The tenant's losses may prove hard to determine. To avoid a potential dispute and potential litigation over actual costs, specify an exact amount that you'll pay the tenant for each day or week that you're responsible for its delay-related costs. Call this agreed-to amount "liquidated damages," a legal term that describes the amount one party to a contract agrees to pay the other if the contract is broken. Such clauses are an attempt to estimate damages in advance where calculating actual damages would be difficult

or impossible. Courts will enforce liquidated damages clauses if they're fair, reasonable, and not disproportionate to actual losses [Clause, par. d].

9. Get Your Own Right to Terminate

Recognize that in some delay situations, it might actually be in your own best interest to terminate the lease. For example, you might have underestimated how much time and money it would take to make the promised construction and alterations necessary to prepare the space for the new tenant's use. That's why it's important to reserve your own termination rights so you can cut your losses and get out of deals that turn out not be cost-effective [Clause, par. c(1)].

Again, such a provision is as much about negotiation as drafting. Tenants may object to giving you termination rights, fearing that you won't act diligently to try and deliver timely possession and may seek a better deal with a different tenant. You can alleviate these concerns by agreeing that your termination rights kick in only if you've made all

reasonable efforts to prepare the space for the tenant's possession during the waiting period. Most tenants will agree to this compromise, attorneys say.

10. Require Tenant to Execute Certification After Taking Possession

Delays in delivering possession may create inaccuracies in the original lease that need to be corrected. So, after the delay ends and you deliver possession of the space, have the tenant sign a certificate stating the lease's actual commencement date and restating the expiration date. This will prevent subsequent confusion about these dates and how they affect other provisions in the lease, such as the definition of "lease years" [Clause, par. e].

MODEL LEASE CLAUSE

Get Lease Protections in Case You Can't Deliver Timely Possession of Premises

It may be impossible to deliver leased premises to a new tenant on the date the lease is scheduled to begin. Such delays, even if they're not your fault, put you in default and may give the tenant the right to rescind the lease and/or sue you for the damages it suffers as a result of not being able to move in on the commencement date. The good news is that you can negotiate for lease language that gives you the right to keep the tenant bound, at least for a period of time, and insulates you against liability for delays in delivering possession. Here's a Model Clause that you should speak to your attorney about adapting based on the laws of your state and your business arrangement with the particular tenant.

LANDLORD FAILURE TO DELIVER POSSESSION

a. No Liability. In the event that Landlord is unable to deliver possession because a certificate of occupancy or any other required certificate, permit, or variance has not been procured, or because of the holding over or retention of possession of any tenant or occupant, or because construction, repairs, improvements, or decorations of the Premises or the Building that are required to be performed by Landlord are not completed in the manner set forth in this Lease, or because of any other reason, then Landlord shall not be subject to any liability for the failure to deliver possession. No such failure to deliver possession shall in any other respect affect the validity of this Lease or the obligations of Tenant hereunder, nor shall the same be construed in any way to extend the Term.

[Add if applicable]: Tenant hereby waives any right to rescind this Lease under Section ___ of the Property Law of *[insert name of your state]* or any successor statute or future statute of similar import then in force, and further waives the right to recover any damages which may result from Landlord's failure to deliver possession of the Premises on the Commencement Date, except for Liquidated Damages as defined in paragraph d herein.

b. Drop-Dead Date. Notwithstanding anything herein to the contrary, in the event Landlord has not delivered possession on or before the date that is twelve (12) months after the Commencement Date, then this Lease shall automatically terminate as of the latter day (the “Drop-Dead Date”) and thereafter the parties shall have no further rights and/or obligations to each other except that Landlord shall return all funds deposited hereunder by Tenant within five (5) days after the Drop-Dead Date. If Landlord’s failure to deliver possession on or before the Drop-Dead Date is due in whole or in part to circumstances of *force majeure*, as set forth in Article ____ hereof, then the Drop-Dead Date shall be extended for an additional three (3) months.

c. Right to Terminate. In the event that Landlord has not delivered possession of the Premises on or before the date that is six (6) months after the Commencement Date (the “Delivery Date”), then either Tenant or Landlord (provided that Landlord has theretofore used reasonable efforts to deliver possession of the Premises) may terminate this Lease by giving written notice to the other party, the receipt of which notice must occur no later than ten (10) days after the Delivery Date for termination to be effective.

(1) In the event that Landlord elects to so terminate the Lease, the Lease shall be deemed to be terminated on the date that the termination notice is received by Tenant and the parties shall have no further rights and/or obligations to each other except that Landlord shall return all funds deposited hereunder by Tenant within five (5) days after such termination is effective.

(2) In the event that Tenant elects to so terminate the Lease, the Lease shall be deemed to be terminated on the date thirty (30) days after the date that the termination notice is received by Landlord, provided that: i. Landlord has not delivered possession of the Premises within such thirty (30) day period (the "Grace Period") and ii. Landlord has not voided Tenant's notice of termination in accordance with paragraph d below. Thereafter, the parties shall have no further rights and/or obligations to each other except that Landlord shall return all funds deposited hereunder by Tenant within five (5) days after such termination is effective.

(3) In the event that Tenant elects to so terminate the Lease, but Landlord delivers possession of the Premises within the Grace Period, then Tenant's notice of termination shall be deemed null and void as of the date possession of the Premises is delivered, and the Lease shall continue in full force and effect, except that the Commencement Date shall be deemed to be the date that possession was delivered.

d. Landlord Voids Termination and Pays Costs.

(1) In the event that Tenant elects to terminate this Lease in accordance with paragraph c. above and Landlord does not deliver possession of the Premises on or before the expiration of the Grace Period, then Landlord may, at its sole option, nevertheless void and nullify Tenant's notice of termination upon written notice ("Landlord's Nullification Notice") given five (5) days after the expiration of the Grace Period, provided that Landlord agrees to pay to Tenant, as liquidated

damages, the sum of Five Hundred (\$500) Dollars per day (the "Liquidated Damages") for the period set forth in subparagraph d(3) below.

(2) In the event that at any time after Landlord's Nullification Notice has been given and prior to the Drop-Dead Date, Landlord, in its sole discretion, deems that delivery of possession of the Premises prior to the Drop-Dead Date is not possible, then Landlord may elect to terminate by giving written notice to Tenant.

(3) Landlord shall pay to Tenant the Liquidated Damages commencing on the day after the expiration of the Grace Period and ending on whichever of the following occurs earliest:

(A) the date Landlord delivers possession of the Premises; or

(B) the date Tenant receives written notice from Landlord that it cannot deliver possession of the Premises and

that Landlord elects to terminate the Lease; or

(C) the Drop-Dead Date.

(4) Liquidated Damages in the amount of five thousand (\$5,000) dollars shall be paid by Landlord to Tenant every ten (10) days after the expiration of the Grace Period. In the event that Landlord fails to pay any portion of the Liquidated Damages on the date that it is due, then the Lease shall automatically terminate on the next business day, and Landlord shall immediately return all funds deposited hereunder by Tenant together with all unpaid Liquidated Damages plus interest on all unpaid Liquidated Damages at the rate of _____ (___%) percent per annum.

(e) **Certificate.** Upon delivery of possession of the Premises to the Tenant, Landlord and Tenant shall thereafter execute a certificate indicating the actual Commencement Date and reiterating the Expiration Date of this Lease.

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