

October 5, 2015

## EVERYTHING OLD IS NEW AGAIN

Many years ago, in 1999, the Canadian shopping centre industry endured the previously unthinkable: the Canada-wide closure of the venerable Eatons chain of department stores. A proposal under the CCAA was sanctioned by the Ontario Superior Court of Justice. In due time, the process culminated in bankruptcy. The Eatons CCAA Order had a novel impact on other occupants' leases: for the first time, a CCAA Order prohibited other tenants of shopping centres formerly anchored by Eatons from exercising any co-tenancy rights under their leases, that would otherwise have been triggered by Eatons' closure.

Here we are in 2015 dealing with the recent closure of 143 Target stores and facing a similar threat looming on the horizon for Canadian shopping centre landlords. Since 1999 the incidence of co-tenancy clauses in shopping centre leases has significantly risen. Theoretically, there are 143 locations at risk of rental income loss, as it is now a fair assumption that there are tenants in the subject properties whose leases contain co-tenancy provisions that allow them, among other things, to reduce the rate of rent payable during a prolonged period of Target's store closure.

### Stay Provision of Target CCAA Order

Once again, the Ontario Superior Court of Justice has intervened. Paragraph 18 of the Target CCAA Order dated January 15, 2015, states that "... during the Stay Period, no Person

having any agreements or arrangements with the owners, operators, managers or landlords of commercial shopping centres or other commercial properties (including retail, office and industrial (warehouse) properties) in which there is located a store, office or warehouse owned or operated by the Target Canada Entities shall take any Proceedings or exercise any rights or remedies under such agreements or arrangements that may arise upon and/or as a result of the making of this Order, the declarations of insolvency by the Target Canada Entities or as a result of any steps taken by the Target Canada Entities pursuant to this Order and, without limiting the generality of the foregoing, no Person shall terminate, accelerate, suspend, modify, determine or cancel any such arrangement or agreement or be entitled to exercise any rights or remedies in connection therewith."

On August 14, 2015, the Stay Period was extended by the Court so that it now expires on November 16, 2015. Most pundits are of the view that the Stay Period will be extended into 2016, although beyond that, all bets are off.

### Rationale for Stay Provisions

What is the rationale for this term of a CCAA Order? Co-tenancy clauses are not uncommon and although they vary in impact, they typically allow tenants to terminate their lease or cease operating in their premises or pay a reduced rental. The economic harm of a Target store closure



on a landlord is already significant; the purpose of this term of an Order must be to prohibit other tenants from adding insult to injury. Indeed, Paragraph 18 of the Target CCAA Order represents judicial interference in freedom of contract, but this is not unusual in insolvency proceedings, the purpose of which is to allow for concurrent failure and rehabilitation while minimizing, as reasonably as can be managed, the damage to affected parties.

### **Next Steps**

What is next for landlords? They should consider approaching tenants holding potentially dangerous co-tenancy rights to negotiate new terms. Many landlords believe that tenants will not risk exercising their termination rights where those tenants have invested significant capital in a property. But the right to pay a reduced rental can be significant. Moreover, replacing a Target store is not necessarily going to be as easy as it was to replace Eatons stores in 2000.

Tenants at a given shopping centre may not experience a decrease in sales as a result of Target's store closure, but then again, that does not mean they will experience a sales increase either (as was commonly the case after the Eaton stores closed and

were re-tenanted). To some landlords and tenants, renegotiating the terms of the co-tenancy clause during the current CCAA Order stay period may represent an opportunity for both sides to eliminate clutter and obtain something they want in exchange for certainty.

Alternatively, we may see that after the CCAA Order expires and the stay is lifted, some tenants will invoke their co-tenancy rights whereupon their landlords will contest the applicability of those rights. South of the border there has been a significant level of litigation concerning disputed interpretations of those rights (which are often expressed in double-negatives that suffer from a lack of clarity). It is not unheard of for courts to re-write some lease provisions that are perceived to be vague or commercially absurd.

It remains to be seen where all of this will lead. Target's departure from Canada coincides with some difficult economic times and the steady gains of online retail activity. Inevitably, as shopping centre owners strive for profitability, shopping centres change their merchandising mix. In this case, they may not be able to control their own destiny, but it can't hurt to try.



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