COVID-19 and the landlord/tenant relationship

March 20, 2020

As COVID-19 makes its way around the world and wreaks havoc on our daily lives, businesses are scrambling to respond appropriately to governmental orders, advisories and recommendations. They are also trying to keep safe their employees, customers and others with whom they interact. We are dealing with unprecedented challenges that are changing on a daily, and sometimes hourly, basis.

The measures that have and will be implemented or recommended to slow the spread of COVID-19 are requiring business owners to make difficult decisions. Business owners are wondering whether they should reduce their hours, request or require employees to work remotely, layoff employees, limit services or temporarily close operations.

Questions like these raise significant legal issues with material ramifications for all businesses, including landlords and tenants. Can a landlord insist a tenant continue to pay rent when that landlord has closed its building down, prevented access, or ceased providing services? Can a tenant choose to shut down operations? If a tenant stops operating, do they still have to pay rent? Are there specific remedies available to landlords and tenants arising from COVID-19 related defaults? Business owners need to consider how their decisions will impact their existing contractual obligations, and for landlords and tenants that includes the lease agreement.

A comprehensive lease endeavours to contemplate every reasonable eventuality that may impact the landlord/tenant relationship. Understandably, few leases anticipated COVID-19 and the worldwide disruptions it is causing. However, answers to the questions landlords and tenants are asking may still be found in their leases.

Relevant lease provisions

Force majeure (a.k.a. unavoidable delay)

A *force majeure* clause typically deals with situations where a particular covenant cannot be performed by the landlord or the tenant due to an event beyond the control of either party. Usually leases include a list of specific *force majeure* events, and that list may or may not include a pandemic.

In a typical lease, the *force majeure* clause does not allow for the lease to be terminated, but rather excuses performance of an obligation for so long as the *force majeure* event is ongoing. One usual and important exception to excused performance is that the tenant remains obligated to pay rent.

Continuous operating covenant

In a typical retail lease, the tenant has an obligation to carry on its business from the premises in an active and continuous manner. It is often noted that a failure to demonstrate continuous operation is an event of default that can result in the tenant being required to pay increased rent for each day the tenant is not operating. Such a default can also permit the landlord to terminate the lease.

Compliance with applicable laws provisions

Leases typically require both parties to carry out their obligations under the lease in a manner that complies with applicable laws. In the current circumstances, this may be a particularly problematic provision when different levels of governmental authorities may issue conflicting directives. If there is a conflict between the continuous operating covenant and the compliance with laws clause, where governmental orders require the tenant to close, it is likely the compliance with laws clause will trump.

Quiet enjoyment/possession covenant

This is one of the more fundamental lease provisions. Through this provision, a landlord covenants to grant its tenant quiet enjoyment of the premises. This means that the tenant has exclusive possession of and access to the premises without material disruption from the landlord or any person claiming through the landlord. This clause is generally operative so long as the tenant complies with its obligations under the lease.

Control of project clauses

These clauses allow the landlord to shut down parts or all of a project, but usually only in circumstances where repair and maintenance is necessary or desired.

Health directives of the landlord

Although not yet common in standard form leases, some landlords have started including a requirement that tenants comply with health and safety directives of the landlord, which are imposed for the benefit of the project as a whole.

Factual circumstances

To address any particular COVID-19 question, in addition to the precise language of the lease, consideration must be given to other relevant factual circumstances, such as:

- the nature of the development (is it a multi-tenancy or single tenancy project; is it a retail, office or industrial project);
- how important the tenant is to the project;

- how important the location is to the tenant;
- the willingness and ability of the landlord and the tenant to weather the COVID-19 crisis together, bearing in mind the landlord may have mortgage payments to make, operating costs and property taxes to pay, and shareholders and investors to satisfy, and the tenant may have employees and suppliers to pay, and also shareholders and investors to satisfy;
- the optics of the situation from a public relations perspective; and
- the moral and ethical values of the parties in an unprecedented global crisis.

The pivotal question

Of the many questions asked, the most pressing is whether a landlord can require a tenant to continue to pay rent, notwithstanding that the tenant is not conducting business from the premises. Assuming that a review of the lease does not provide a clear right of the tenant to abate rent or cease operations during a pandemic or a situation where the premises or the building has been ordered closed by governmental authorities, or any other unique factual circumstances:

1. It is unlikely a court would allow a tenant to withhold their rent during the relevant period. However, if the landlord is not meeting its obligation to provide the tenant with quiet enjoyment of the premises, or if the landlord is unable to provide the services required in order for the tenant to use the premises, then there may be an argument for rent abatement. Even in a situation where the premises or entire project is closed by governmental requirement, it is questionable whether that scenario amounts to a breach of the landlord's covenant for quiet enjoyment. In that circumstance, the government ordered closure is more likely an event of *force majeure*. A typical *force majeure* clause does not excuse the tenant from paying rent, even though it may excuse the landlord from the obligation to provide services and access.
2. Notwithstanding the foregoing, given the far-reaching impact on so many businesses being required to pay rent when they are unable to meaningfully occupy their premises, there is a possibility that: (i) government assistance may be available to backstop the rent that tenants are required to pay during this period; (ii) there may be a legislative response that could have an impact on the lease; or (iii) a court may even seek to evolve equitable doctrines to suit the circumstances at hand.
3. Further, it is worth it for landlords and tenants to carefully review their business interruption and rental loss insurance policies to determine if rent is covered during the closure period. The majority of such policies typically cover payments during a period of property damage that interrupts tenants' businesses. Some may also cover business interruption from government ordered closures, though that coverage is less common and many business interruption policies specifically exclude business interruption caused by bacterial or viral infections.

Paying attention to the details

We anticipate that there will be a number of situations where landlords wish to close their retail or office projects and still seek rent from tenants. We also anticipate that there will be a number of situations where tenants wish to temporarily cease operations

and either cease paying rent or pay a reduced or deferred rent until they are fully operational again, without the landlord terminating their lease for default.

In the context of COVID-19, a number of circumstances must be taken into account as to whether a landlord can seek rent from its tenants, and whether a tenant may be able to cease operations without terminating the lease or paying rent. Consideration must be given not just to the applicable lease provisions discussed above, but also the applicable laws for their particular jurisdiction, as well as the current orders, directives, advisories or recommendations from Ministries of Health, municipal governments and local health authorities.

These matters are not static. New issues will arise and new and relevant circumstances will emerge. Landlords and tenants considering their options need to be prepared to reassess in this rapidly changing landscape.

This is not a legal opinion. For landlord/tenant legal advice arising from COVID-19, please reach out to our contacts listed below, who are ready and available to assist with navigating through these unprecedented times.

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