

DOLLARS TO DOUGHNUTS, EXCULPATORY CLAUSES IN COMMERCIAL LEASES ARE A GOOD BET

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Every lease is a calculated gamble. Will the tenant perform its end of the bargain? What will the tenant contribute to the property or center? Will the terms of the lease protect the landlord from the myriad of scenarios which could potentially arise, including unreasonable exposures to liability? Landlords depend heavily on their lease (yes, even the boilerplate!) to improve the odds in their favor.

According to a recent California case, it is a winning bet for commercial landlords to include good exculpatory clauses in their leases. An exculpatory clause generally states that the landlord is completely exempt from liability to its tenants for a variety of reasons, including negligence and many other possible claims against the landlord.

Frittelli's Doughnuts and Coffee, the tenant in this case, sold its gourmet goods from leased property located a few blocks from the famous Rodeo Drive boutiques in Beverly Hills. The high-end "designer doughnut" shop, incredibly popular with the Hollywood crowd, was featured in articles published in the Los Angeles Times, In Style, In Touch, Star, Angelino and Imbibe magazines. Its reputation soared through the blogosphere.

In 2008, Frittelli's landlord began renovation of the shopping center's façade, which was anticipated and permitted under the terms of the 2006 lease. Shortly thereafter, the "doughnuts-to-the-stars" shop stopped paying rent and closed its doors forever. It then sued the landlord for damages generally based upon lost business caused by the façade renovation. Although the evidence established that the tenant had been losing money for some time, Frittelli's alleged that the landlord's renovation "completely destroyed" its business, and the landlord should compensate them for the loss. The theories raised in the lawsuit were that the

landlord was negligent in the manner and duration of construction and had breached various provisions of the lease.

Fortunately for the landlord, the lease contained an exculpatory clause stating that notwithstanding the landlord's negligence or breach of lease, the landlord would not be liable under any circumstances for, among other things, injury to the tenant's business or any loss of income or profit. Further, the lease specifically proscribed that the tenant's sole recourse for such damages was to file a claim on the insurance policies that the tenant was required to procure and maintain during the lease term. [As an aside, there is probably no insurance policy that provides coverage for a loss of business due to landlord's renovation of the center]. The Court carefully analyzed and interpreted the terms of the lease, and determined that the exculpatory clause protected the landlord from all liability to the tenant for breach of lease, breach of the covenant of quiet enjoyment, rescission and negligence. The court concluded that in a commercial setting, when the contracting parties knowingly bargain for certain protections, the protection should be enforced. This particular lease also contained a specific exemption for any landlord liability arising out of the remodeling of the shopping center, including damages for any inconvenience or disruption to tenant's business, other than rent abatement, which further defeated tenant's claim for breach of the covenant of quiet enjoyment.

This case once again demonstrates that a properly drafted exculpatory clause in a commercial lease can protect the landlord from the risk of potential liability to tenants. As a landlord, be very cautious when negotiating leases not to allow such clauses to be deleted except in limited situations where insurance would cover any loss.