



Uninsured risks for the uninitiated – demystifying the drafting

Including drafting in leases to cover situations where damage occurs to the premises as a result of a risk which is not insured against is often a point of negotiation. This is a complex area and this article sets out, in simple terms, the key points for parties to consider when introducing this concept into a lease.

Insured or not?

The standard position in a commercial lease is that the Landlord insures at the Tenant's expense for:

- > damage to the premises caused by an insured risk; and
- > loss of rent for a specified period.

A summary of the risks which are usually insured against is in the glossary box.

The Landlord typically covenants to make all insurance claims and to use the insurance proceeds to reinstate the premises within a specified period.

Landlords are sometimes willing to take on some of the risk of uninsured liability and it is increasingly common for tenants to insist on this being included in leases. This is when complex drafting relating to uninsured risks is introduced. *A summary of what the term "uninsured risks" usually means is in the glossary box.*

This aim of this article is to focus on the specific provisions in leases which need to be carefully considered when uninsured risks language is being introduced and specifically the interplay between the repair, rent suspension and reinstatement clauses as well as the issue of termination rights.

Repair

Traditionally, unless damage is caused to the premises by an insured risk, the Tenant takes full responsibility for keeping the demised premises in good repair. Therefore, where damage is caused by an uninsured risk, the Tenant will be required to repair it.

This is often not an acceptable position for Tenants. Landlords are increasingly permitting Tenants to exclude their liability for repairing damage caused by uninsured risks by carving out such damage from the Tenant's repairing obligation (unless such damage is caused by the Tenant's default).

Rent suspension

Where damage is caused by an uninsured risk, depending on how the lease is drafted the rent may be suspended in the same way as it would be on the occurrence of damage or destruction by an insured risk. *A summary of what the term "rent suspension" usually means is in the glossary box.*

Where the damage is caused by an insured risk, loss of rent is covered by insurance such that the Landlord's loss is made good by its insurer; the rent suspension mechanism is therefore usually limited to the period for which loss of rent is insured.

Glossary: Understanding the key terms

- > **Insured risks:** The "usual" insured risks will usually be set out in the Lease and typically include things like fire, natural disasters, burst pipes and civil disturbances. Landlords should check that the list of insured risks matches up to those that are insured under the current insurance policy for the building. There is often a "catch all" sweep provision which allows the Landlord to insure "any other risk" that the Landlord reasonably wishes to cover.
- > **Reinstatement period:** The period in which the Landlord must reinstate the premises. If reinstatement is not completed during this period, the Tenant often requires a termination right. Landlords should consider, in light of the nature of the building, what the length of this period should be.
- > **Rent suspension:** In the event of damage by an insured risk, the basic rent (and usually service charge and other rents) is typically suspended for a period known as the "loss of rent period". This is sometimes also known as the "rent cesser" clause. Landlords usually take out insurance to cover their lost income while the rent is suspended.
- > **Uninsured risks:** This will typically be defined to include risks which are not insured, either because cover is not available or the risk is not included in the scope of the insured risks set out in the lease.



However, where the damage is caused by an uninsured risk and a rent suspension mechanism has been included in the lease, **loss of rent will be an additional cost** for the Landlord as no insurance is in place.

Reinstatement and termination rights

Where damage is caused by an insured risk, the Landlord is typically obliged to apply the insurance proceeds to reinstatement of the premises and to reinstate the premises within the rent suspension period.

Traditionally, leases often include the following termination rights:

- > for Landlords, where reinstatement within an agreed period would be impossible or impracticable; and
- > for Tenants (and sometimes the Landlord too), where the Landlord has not completed reinstatement by the end of the rent suspension period.

In leases which include drafting to cater for uninsured risks, there is likely to be an additional right for the Landlord to elect to either:

- > reinstate the premises within a particular time period; or
- > terminate the Lease.

Electing to reinstate uninsured damage

Where the Landlord makes an election to reinstate damage caused by uninsured risks, there are several points worth noting:

For Landlords:

- i. the Landlord will be reinstating at its own cost - there will be no insurance proceeds to apply to reinstatement. It is therefore generally accepted to be fair that the Landlord has only an option to reinstate rather than an obligation to do so;
- ii. the length of the election period should be carefully considered – this should allow the Landlord enough time to evaluate the extent of the damage and identify the likely cost; and
- iii. the Landlord will usually want to ensure the Tenant is standing by ready to move back in and resume rental payments when the premises are reinstated. Landlords should therefore ensure that the Tenant's termination right will not arise until such an election has been made and if so, on expiry of the relevant reinstatement period if reinstatement is not complete by such time – see below for further detail.

For Tenants:

- i. if the Landlord fails to make such an election within a specified time period, or elects to reinstate the premises but fails to do so quickly enough, the Tenant may terminate the Lease – this is to protect the Tenant against exposure to rental liability after expiry of the rent suspension period whilst waiting for the Landlord to finish reinstating; and
- ii. the ability to terminate on expiry of a long stop period prevents Tenants being locked in to a lease of premises that can no longer use be used. It also offers an incentive to Landlords to complete the reinstatement expeditiously.

The bottom line

Whether or not Landlords will accept liability for damage caused by uninsured risks depends on the nature of the transaction and the bargaining position of the parties. It is worth considering the commercial position at the outset and seeking legal advice to avoid time-consuming and complex negotiations later on.



Hannah Day
Associate, Real Estate
Tel: +44 20 7456 5276
hannah.day@linklaters.com

January 2021

[linklaters.com](https://www.linklaters.com)

This publication is intended merely to highlight issues and not to be comprehensive, nor to provide legal advice. Should you have any questions on issues reported here or on other areas of law, please contact one of your regular contacts, or contact the editors.

© Linklaters LLP. All Rights reserved 2021

Linklaters LLP is a limited liability partnership registered in England and Wales with registered number OC326345. It is a law firm authorised and regulated by the Solicitors Regulation Authority. The term partner in relation to Linklaters LLP is used to refer to a member of Linklaters LLP or an employee or consultant of Linklaters LLP or any of its affiliated firms or entities with equivalent standing and qualifications. A list of the names of the members of Linklaters LLP and of the non-members who are designated as partners and their professional qualifications is open to inspection at its registered office, One Silk Street, London EC2Y 8HQ, England or on www.linklaters.com and such persons are either solicitors, registered foreign lawyers or European lawyers.

Please refer to www.linklaters.com/regulation for important information on our regulatory position.