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Capital Cost Struggles

RioCan Holdings Inc. v. Metro Ontario Real Estate Limited, 2012 ONSC 1819, illustrates the ongoing struggle between landlords and tenants regarding the allocation of capital costs and operating expenses. At issue in the case was a clause in the retail shopping centre lease that excluded “expenditures which by accepted accounting practice are of a capital nature” from additional rent charges.

RioCan was the landlord of a commercial plaza in Windsor, Ontario. In 2002, RioCan undertook the rehabilitation of the parking lot pavement, which involved pulverizing the asphalt and the underlying granular base, compacting it and adding a layer of hot asphalt mix on top. The total cost was C\$431,000, which RioCan amortized over 20 years and sought to recover from Metro, the tenant. Metro paid a monthly installment of C\$858 until it reviewed the matter in 2007 and 2008. Subsequently, Metro alleged that the rehabilitation of the parking lot was of a capital nature, and therefore Metro should not be responsible for its share of the cost. When RioCan insisted on payment, Metro began to offset the amounts it had already paid on account of the rehabilitation against the rent owing to RioCan and refused to make further payments in respect thereof.

When the matter came before the courts, RioCan argued that the phrase “accepted accounting practice” in the lease included not only GAAP but also tax accounting practices. Based on the latter, since there were no direct revenues with respect to the parking lot, and since the restoration would not result in a future economic benefit to RioCan in the form of rental income, it should not be characterized as a capital expenditure. On

the other hand, Metro contended that it was not necessary to match particular revenues with an improved asset and that based on GAAP, the reduction in operating costs and extension in the life of the parking lot were sufficient for the rehabilitation to be treated as a capital cost. Furthermore, the very fact RioCan was amortizing the cost over an extended period would suggest that this was a capital cost.

The Court ruled in favor of Metro and found that the rehabilitation was a capital expenditure and must be excluded from additional rent under the terms of the lease. The irony here is that RioCan found itself out-of-pocket by acting in a commercially responsible manner. RioCan could have continued to patch and repair the parking lot and charge the full cost to Metro as it did before. In choosing a more comprehensive and cost-effective solution, which involved rehabilitating the entire lot, the landlord was unable to recoup its cost. This consideration, however, is not relevant when interpreting a lease as the express lease provisions govern, regardless of cost efficiencies or best practices.

This case serves as a reminder of the dangers of broadly-worded terms like “capital costs” and where such terms are used, it is advisable to set out specific accounting standards to follow in the lease. GAAP, as illustrated by the above decision, may not always be the appropriate standard to follow. Furthermore, landlords ought to include a provision, which precludes tenants from challenging additional rent payments after a stated period of time. This case is scheduled to be heard on Appeal later this year.

Damage caused by “Normal Wear and Tear”

NWS Holdings Inc. v. Oceanex Inc., 2011 NLTD 43 examines the issue of damage to the premises as a result of “normal wear and tear”. The tenant, Oceanex Inc., vacated the premises in November 2005. Pursuant to the lease, the tenant was required to leave the premises in a state of good repair, subject to reasonable wear

and tear. The landlord, NWS Holdings Inc., brought an action against the tenant for violation of its covenant to leave the premises in a suitable condition. The landlord claimed damages for lighting and furnace repairs, repairs to the insulation and steel columns, and replacement of exterior siding. Oceanex Inc. maintained that it left the premises in as good or better condition than they were at the start of the lease, that any modifications would result in a betterment and any damage fell within the normal wear and tear exception.

The Court rejected the tenant’s claim of betterment. The Court stated that the tenant must produce evidence to establish a claim of betterment, subject to limited exceptions. The exception did not apply in this case since the tenant failed to produce any evidence to support the claim of betterment. Additionally, the Court stated that the landlord must first prove on a balance of probabilities that the tenant caused damage to the premises. Once damage is established, the onus then shifts to the tenant to prove that either it was not responsible or that the damage resulted from normal wear and tear, considering the condition of the premises at the outset of the lease.

The Court dismissed the landlord’s claim for damages with regards to the lighting and furnace repairs, as the landlord failed to prove that the tenant caused any damage and the landlord’s claim for damages to the siding was dismissed as the landlord failed to produce evidence of such damage. However, the Court did rule that the landlord was entitled to compensation for the cost of repairing insulation and steel columns, as it was caused by careless operation of heavy machinery rather than normal wear and tear.

The lesson for landlords is that in a claim for physical damage to a leased commercial building, it is necessary for the landlord to establish sufficient evidence of damage to shift the onus to the tenant to show that it was not negligent or that it was due to the normal wear and tear of the occupancy.

Who is Responsible for Leasehold Improvements after a Fire?

In *Excelsior Properties Ltd. v. Cosentino Developments Inc. and 1089920 Alberta Ltd.*, et al., 2011 ABQB 666, then defendants (subtenant) operated a restaurant and bar called “Grinder” at the premises they subleased from the tenant (Cosentino Developments), which was owned by the plaintiff (landlord). Under the Sublease Agreement, the subtenant assumed all of Cosentino’s obligations under the lease documentation.

On May 8, 2006, a fire occurred at the leased premises, damaging the building and the leasehold improvements inside. The landlord brought an action against Cosentino and the subtenant, alleging that the defendants breached their contractual obligations to compensate the landlord for loss of the improvements damaged by the fire and Cosentino subsequently issued a third party notice against the subtenants seeking indemnification pursuant to the Sale of Specified Assets Agreement. The subtenants brought an application for summary judgment dismissing the landlord’s claim (and Cosentino’s third party claim).

The issue was whether the subtenant had an obligation to indemnify the landlord for fire damages to leasehold improvements. The subtenant submitted that lease does not impose this duty on the tenant and they argued that, to the contrary, the lease explicitly makes the landlord responsible for carrying fire insurance. The subtenant admitted that the lease required them to carry “property damage insurance”, however, they submitted that the property insurance is separate and distinct from fire insurance. The subtenant also relied on the Supreme Court of Canada decision in *Smith v. T. Eaton Co.*, [1978] 2 S.C.R. 749, where the SCC held that a landlord’s covenant to provide fire insurance protects a tenant against a claim for damages, even where the fire is caused by the tenant’s own negligence. In contrast, the landlord submitted that the lease obliged the tenant to carry “property damages insurance”,

which included the obligation to insure leasehold improvements against damage by fire.

In order to make a determination, the Court had to resolve several questions. First, the term “building” was not defined in the initial lease, making it unclear whether it extended to leasehold improvements inside the building. The Court relied on the principle that landlords and tenants routinely treat the building and the leasehold improvements as separate objects under insurance coverage, and found that the term “building” may be distinct from leasehold improvements. However, as the lease lacks a definition, the term is ambiguous.

Second, the Court found that the term “property damage insurance” is sufficiently broad that it *may* include damage by fire. According to *Ross Southwards Tire v. Pyrotech Products*, [1976] 2 S.C.R. 35, allocations of risk as between the landlord and tenant must be determined on the basis of the lease and not by reference to insurance policy considerations. Furthermore, the rights and obligations between landlord and tenant are to be determined on the basis of their express intentions in the lease.

Third, the Court stated “there is room for argument with respect to what the parties meant by the demised premises,” but that the initial lease definition would suggest that the term describes the structure itself, excepting any leasehold improvements.

Finally, the Court considered the indemnity clause and noted that it was unclear whether the parties intended the clause to cover only third party claims or whether it made the tenant liable to compensate the landlord for any damage to property. The Court noted there was an argument that the indemnity clause in the initial lease could entitle the landlord to compensation for leasehold improvements, but the clause was ambiguous and required interpretation.

In the end, the Court found that both leases contained ambiguous clauses and

required interpretation of both fact and law in order to properly ascertain the parties’ intentions in the leases. Therefore, the subtenant’s application for summary judgment was dismissed.

Refresher on the Tests for an Injunction

In *Target Brands, Inc. v. Fairweather Ltd.*, 2011 FC 758, the plaintiffs applied for an interlocutory injunction to restrain the defendants from operating a retail store in association with a trade-mark or trade name comprising of TARGET or a bull’s-eye design, and from displaying, advertising or using these trade-marks to direct public attention to the defendants’ business as to cause confusion between the businesses of the defendants and the plaintiffs.

The plaintiffs, Target Brands, Inc. (“Target”), are a large chain of retail department stores in the US. The defendants, Fairweather Ltd. (“INC”), sell private label clothing and accessories to mid-to-low income customers in Canada. One of the names under which INC sells clothing is “Target Apparel”. On January 13, 2011, Target publicly announced its intention to purchase leasehold interests in up to 220 stores owned by Zellers Inc., which would be converted into 100 to 150 Target stores by 2014.

Target brought an action against INC for a permanent injunction preventing it from operating its business under the “Target” name, as well as using the bull’s-eye design. Additionally, Target claimed damages for infringements of its trade-marks. INC issued a counterclaim against Target for infringement of its registered trade-mark “Target Apparel”. In the meantime, Target brought an application for an interlocutory injunction to restrain INC from using the “Target” name and logo.

In order to be successful, Target had to meet the test for an injunction as adopted by the Supreme Court of Canada in *RJR-MacDonald Inc. v. Canada.*, [1994] 1 S.C.R. 311, by satisfying the following three questions: (i) is there a serious issue to be tried; (ii) would Target suffer

irreparable harm if the injunction was refused; and (iii) in whose favor does the balance of convenience lie. The applicant must succeed on all questions.

The Court determined that Target had genuine concerns for the well-being of its brand and the confusion arising from two target brands, and thus the issue to be tried was not frivolous or vexatious. With respect to the second prong of the test, the Court noted that irreparable harm cannot be compensated by way of damages. The Court analyzed the concept of irreparable harm in the context of Target's claim that INC was passing off its operation under Target's name. The three necessary components of a passing off claim are: (i) goodwill; (ii) deception of the public or confusion; and (iii) actual or potential damage to the plaintiff.

Based on Target's evidence about its significant Canadian customer base, the Court found that Target established a certain degree of goodwill in Canada. The Court found, however, that while there was some confusion at the outset, confusion would dissipate once Target stores opened in Canada. With regards to actual or potential damage, the Court determined that Target's submissions were based on a marketing theory about "sincere" brands, which was difficult to assess without a full trial.

The court further held that the balance of convenience favored INC, which already had stores across the country. If the application was granted, INC would have to remove and replace the signage for all of its stores, at great expense. As a result, the Court found that the tests had not been met by Target and dismissed Target's application for an interlocutory injunction. The matter was consequently settled by the parties and did not proceed to trial.

Limitation Period – Authority for Landlords

When the *Limitations Act, 2002* came into force in Ontario on January 1, 2004, it replaced Parts II and III of the former *Limitations Act*. Part I of the old act (dealing with real property interests) was renamed

the *Real Property Limitations Act (RPLA)*. The focus under the old *Limitations Act* was on the date a "cause of action" arose. The new *Limitations Act* shifted the focus to the existence of a "claim" as defined as "injury, loss or damage". The new *Limitations Act* was designed to simplify the application of limitation periods by providing, subject to some exceptions, a basic limitations period of two years based on the principle of discoverability.

Given the dual limitation regimes, the obvious question that arises is which act applies — the new *Limitations Act* with a two-year limitation period, or the *RPLA* with a six-year limitation period? Leases are not specifically dealt with under the *RPLA*, although **rent** is defined under s.1 to include "all annuities and periodical sums of money charged upon or payable out of land" and Section 17(1) of the *RPLA* refers to "arrears of rent". For several years, commentators were divided on the question of whether disputes regarding leases would fall under the *RPLA* or the new *Limitations Act*.

Despite the lack of case law, over time support grew for the position that the six-year limitation period under the *RPLA* would apply to landlord claims for arrears of rent, whereas the two-year limitation period under the new *Limitations Act* would apply to a tenant's claim for overpayment of rent. A recent case *Ayerswood Development Corp. v. Western Proresp Inc.*, 2011 ONSC 1399, [2011] O.J. No. 1052 (Ont. S.C.J.), now provides judicial authority for this position.

Ayerswood involved an action by a landlord for arrears of rent and cost of restoration of leased premises. In 2001, the tenant, Western Proresp Inc., entered into a five-year lease with the plaintiff landlord's predecessor. At the end of the lease term, the tenant remained in the premises during negotiations of a renewal agreement. The tenant continued to pay rent, including estimated charges and taxes for maintenance of the common areas ("CAM") as per the following provision in the lease:

"Whenever under this lease the Tenant is to pay its proportionate share, the amount thereof may be estimated by the Landlord for such period as the Landlord may from time to time determine...As soon as practicable after the end of such period, the Landlord shall advise the Tenant of the actual amounts for such period ..."

The lease was not renewed and the tenant was evicted from the premises in 2007. The landlord brought an action against the tenant for the balance owing after reconciliation of the CAM charges and taxes from 2001 to 2007. The tenant argued that the landlord could not recover the charges because the landlord did not prove the charges, failed to bill the charges "as soon as practicable", and failed to bring the claim within the appropriate limitation period under the *Limitations Act* or the *RPLA*.

The Court rejected the claim by the tenant that the landlord could not prove the CAM charges and taxes, and held that the tenant was required to pay the balance owing. The Court further found that under the lease, the landlord was required to make adjustments at the end of the "period". Since the term "period" was not defined in the lease, the tenant should have expected that adjustments would be made at some point in the future.

Without addressing the dual limitation regime, W.A. Jenkins J. simply stated "The limitations argument can be disposed of briefly" and then applied the six-year limitation period under the *RPLA*. The Court held that the landlord's claim was not barred by that limitation period as it provides that arrears of rent must be claimed within six years after they become due. The amount of adjustments for the CAM charges was not due until billed in 2007, and thus the limitation period did not start to run until 2007. The Court also rejected the tenant's estoppel claim, stating that the tenant was aware that there would be a reconciliation of charges in the future

and did not rely on landlord's failure to charge CAM to its detriment.

Implied Duty of Good Faith? Duty to Mitigate Damages?

The fundamental premise of the good faith doctrine is that the parties to a contract must deal with each other fairly and in good faith. The covenant of good faith assists courts in interpreting the intention of parties to a contract. Typically, it is used to "fill in the blanks" where the scope of the parties' rights and obligations are unclear as a result of contractual silence or ambiguity. Thus, it protects the contracting parties' reasonable expectations.

Although the doctrine of good faith in contractual dealings is thoroughly entrenched in Australia and the United States, there is still some debate as to whether there is an independent doctrine of good faith in Canada. Canadian courts have adopted a more cautious approach to the implication of duties of good faith as a separate doctrine in contract law. There is currently no positive duty to negotiate a (new) contract in good faith in Canadian law. Generally, parties negotiating a contract expect that each will act entirely in the party's own interest and imposing a positive duty to negotiate in good faith would be incompatible with the activity of negotiating and bargaining.

Manufacturers Life Insurance Co. v. Executive Centre at Manulife Place Inc., 2011 ABQB 189, involved an application by the plaintiff landlord for summary judgment against the defendant tenant. The case explores the potential duty of a landlord to act in good faith and to mitigate damages. The landlord, Manufacturers Life Insurance Co. ("Manulife"), entered into a ten-year lease for the premises with the tenant, Executive Centre at Manulife Place Inc. ("Executive Centre"). Since commencement of the lease on July 30, 2001, Executive Centre paid in excess of C\$3.5 million in rent. In August 2010, Executive Centre approached Manulife seeking rent concessions and proposed

a consolidation of its operations on the 11th floor and vacation of the 10th floor as of September 30, 2010. Furthermore, commencing January 2011, it would pay additional rent under the 11th floor lease in an amount equivalent to the rent payable under the 10th floor lease. Under this proposal, Manulife would lose approximately C\$150,000 in lease payments. The proposal was not accepted.

The tenant failed to make its rental payments as of October 1, 2010, under the lease and vacated the premises on September 30, 2010. The tenant was served with a notice of termination by the landlord. The tenant argued that the landlord breached its implied duty to act in good faith and duty to reasonably renegotiate payment of rent for the remaining year of the lease. The tenant further contended that the landlord failed to mitigate damages by not agreeing to the tenant's proposal to pay lower rent than the amount stipulated in the lease.

The Court followed jurisprudence purporting that there is no generalized duty of good faith that is independent from the terms expressed in the contract, but the Court did recognize "there are situations in which terms, including an obligation of good faith, could be implied in a contract. However, in the situation here, there is an entire clause term in the written contract for a commercial lease between sophisticated parties; therefore, no term can be implied beyond the written terms of the agreement. Moreover, the breach here is one of payment of rent, not of some obligation to act in a way which may require good faith ..."

Furthermore, the Court held that while the landlord has an obligation to mitigate its damages once the lease is terminated; however, that duty does not extend to requiring the landlord to accept the tenant's proposal to pay less rent. While the lease is still in effect, a failure to renegotiate a lease with a defaulting tenant cannot properly be described as a failure of mitigation since the lease is still in effect and mitigation is not therefore required.

Has the Option to Renew/Extend been Invalidated by Tenant Default?

In the case of *1556724 Ontario Inc. v. Bogart Corp.*, [2011] O.J. No. 1940 (Ont. S.C.J.), the tenant's renewal right was contingent on the tenant being in good standing and "having not been in material default under the lease". The tenant, 1556724 Ontario Inc., leased spaced from the landlord, Bogart Corp., to operate a small take-out restaurant. In 2008, the landlord delivered a notice of termination to the tenant for breach of various covenants under the lease and the tenant applied to the Court for relief from forfeiture. The tenant was allowed to resume business, subject to conditions pursuant to a court order.

On November 30, 2009, the tenant attempted to exercise its option to renew the lease for an additional five years. Throughout the term of the lease, the tenant had committed numerous defaults; however, at the time the tenant purported to exercise the renewal option, all prior defaults had been cured. The tenant argued that because it had cured all previous defaults, that they were "spent breaches" that should not interfere with its right to renew.

The Court found that the tenant's previous breaches constituted "material breaches" under the terms of the lease, and therefore did not grant the tenant the right to exercise the renewal option. Despite the fact that the tenant had cured all defaults prior to exercising the renewal option, the failure to comply with the condition precedent precluded the tenant from relying on the renewal provision. The Court based its decision on the facts of the case and did not provide a method for determining what type of conduct would constitute a material breach. However, it is clear that the court will scrutinize a tenant's conduct closely and will consider a wide range of actions when making a determination with respect to a default under the terms of a lease.

Firkin Pubs Metro Inc. and Flatiron Equities Ltd., 2011 ONSC 5262, [2011] 8

R.P.R.(5th) 312, involved an application by the tenant for a declaration that an option to extend the lease was validly exercised and compelling the landlord to arbitrate the basic rent amount. The respondent landlord submitted that the notice was invalid because the applicant tenant was in arrears of rent when it was delivered, the applicant had parted with possession and the premises and the notice to extend did not come from the applicant.

The applicant, Firkin Pubs Metro Inc. and Firkin Hospitality Inc. (“Firkin”), entered into a commercial lease with the owner of the Flatiron Building in Toronto (“Flatiron”), for a term of 10 years, beginning January 1, 2001. The lease contained an option to extend for two terms of five years each. Prior to the commencement of the lease, the applicants entered into a franchise agreement with Kimbrook Investments, granting it a license to operate a restaurant and bar in the premises for the term of the lease and any renewals under it.

On April 7, 2010, the Firkin wrote to Flatiron’s agent confirming the applicant’s intention to exercise the option to extend the term. As stated in the lease, the base rent to be paid for the extended term was to be agreed upon between the parties, or determined by arbitration if negotiations failed. Negotiations continued into 2011. May 20, 2011, Flatiron alleged a default by Firkin because it was in arrears of “additional rent” in addition to permitting a franchisee to occupy the leased premises without the written consent of the landlord. Flatiron was of the view that Firkin’s exercise of its option to extend was invalid and sought vacant possession.

The tenant’s application was granted. The fact that Firkin was not operating in the leased premises did not amount to it having parted with possession and should not deprive it of the right to exercise the right to extend the term of the lease. Firkin maintained legal possession of the premises through its complete access to the premises, its continuing dealings with the landlord regarding operational issues

involving the premises, its exercising of the option to extend and negotiation of the terms of the extended lease. Even if a breach occurred, the option to extend provided that a default or breach constituted an “event of default” only when it remained unremedied after a specified time in a written notice of the breach. Flatiron declined to exercise its rights under the lease by not giving notice of the breach to Firkin.

The Court further held that even if rent arrears were owed by Firkin, that was insufficient to invalidate the Firkin’s exercise of its option to extend as Flatiron did not give Firkin written notice of default in the payment of rent until long after Firkin had exercised its option to extend and did not give it an opportunity to remedy the default. The Court found that the equities of the case required that relief from forfeiture be granted.

Overholding Tenant

In *Aim Health Group Inc. v. 40 Finchgate Ltd. Partnership*, 2012 ONSC 169 (Ont. S.C.J.), the Court considered the issue of overholding and the application of a month-to-month provision in the lease following the termination date.

In February of 2007, the tenant leased space from the landlord to operate a chronic pain management facility for a term of five years, expiring on December 31, 2011. The lease contained an overholding provision stating that at the expiration of the initial term, the tenant “shall continue to occupy the Leased Premises without further written agreement ... and the tenancy ... thereafter shall be from month to month only and may be terminated by either party on one month’s notice.”

In the spring of 2011, the tenant informed the landlord that it intended to relocate its business, but not until it passed a College of Physicians and Surgeons of Ontario (the “CPSO”) inspection, which would take several months to complete. In October of 2011, the tenants informed the landlord that it would require a further extension of the term until February of

2012. In mid-December of 2011, the tenant notified the landlord of further delays created by the CPSO inspection and made a written request for a three-month extension.

Despite these communications, the landlord rejected the tenant’s request, secured a new tenant and terminated the lease effective December 31, 2011. The landlord offered an alternative space, which was not a viable alternative as any relocation would be subject to approval under the CPSO regime. The tenant did not vacate the premises by the termination date, causing the landlord to change the locks at the premises and move the tenant’s property to a storage facility three days after the termination date. The tenant brought an application against the landlord for a declaration that the termination of the lease was unlawful.

The Ontario Superior Court determined that the landlord was aware that the tenant was delayed in relocation and held that at the termination date, the overholding provisions of the lease applied and the lease became a month-to-month tenancy. Furthermore, the Court found the landlord in breach of the lease terms by changing the locks at the premises and removing the tenant’s property, and therefore, the tenant was entitled to re-enter the premises. The judge was satisfied that the lease became a month-to-month tenancy as set out in the lease and may be terminated by either party on one month’s notice.

Repairs and Maintenance and Occupier’s Liability

In *Musselman v. 875667 Ontario Inc.*, 2012 ONCA 41, [2012] O.J. No. 649 (Ont. C.A.), the outcome of the case turned largely on whether the respondent landlord was an occupier of the rented premises within the definition of “occupier” in the *Occupiers’ Liability Act*.

The plaintiff incurred a slip and fall on the stairs of a restaurant, leading to severe injuries, allegedly due to the construction and condition of the stairs. The plaintiff sued the restaurant, its proprietor and the

landlord, as well as the City of Toronto for negligence in ensuring that the stairs were constructed in a manner that would provide for safe use.

The trial judge found the proprietor and the City jointly and severally liable for the plaintiff's damages, but found the landlord not to be an occupier for the purposes of the Act. Since, the landlord had no responsibility for or control over the activity on the premises or who was allowed on the premises, the landlord owed no duty to the plaintiff under the Act.

The challenge on appeal was not the trial judge's legal interpretation of "occupier". The plaintiff appealed on two grounds: (i) the judge misunderstood the evidence of the tenant proprietor establishing that the landlord had the requisite responsibility and control of the premises; and (ii) the judge misunderstood the operative lease terms in respect of the landlord's responsibility for inspection and repairs.

The Ontario Court of Appeal dismissed the appeal, ruling that the trial judge's interpretation of the proprietor's evidence was reasonable. Furthermore, the interpretation of the operative lease terms at trial was deemed correct and sufficiently put the responsibility for repair and maintenance on the tenant. The judge considered the following factors: (i) the exclusion of "wear and tear" from the proprietor's responsibility for maintenance and repair did not place an obligation on the landlord to repair and inspect the property; (ii) the lease was only one factor in the assessment of the entirety of circumstances; and (iii) the conduct of the parties over the course of several years.

The lesson from this case is that landlords are not automatically deemed "occupiers" of the premises under the *Occupiers' Liability Act*. Rather, the determination will be made on the totality of circumstances including the operating provisions of the lease and the conduct of the parties.

Landlord was Liable to Tenant for Damages for Loss of Business

In *1302207 Ontario Limited v. 1517979 Ontario Limited*, 2012 ONSC 3680, the Court held that the landlord acted precipitously to close down renovations being undertaken by the tenant. The landlord made the same mistake when it began to demolish the premises while waiting for a decision of the court that was to determine whether the tenant had breached the lease. The landlord was ordered to pay damages for those failings. On the other hand, the tenant cannot guild its damages by failing to act to minimize its loss, particularly when the path to do so is made clear by order of the Court.

1517979 Ontario Limited (the "Old Tenant") operated a night club. The principal assets of the business included the lease of club space, a liquor license, and certain equipment. The Old Tenant sold its assets to 1727299 Ontario Inc. (the "New Tenant"), a corporation owned by Frank Piniccia. Piniccia agreed to close the transaction before consent was provided by 1302207 Ontario Limited (the "Landlord"). The Landlord withheld consent to the assignment due to outstanding rent allegedly owed by the Old Tenant.

Piniccia wished to renovate the nightclub. The lease required that "no alterations" be made to the premises without the written approval of the landlord. Even though the Landlord had learned that the night club was purchased without its consent, there was an e-mail exchange between them, the upshot of which was that it was understood that renovations were to take place, that the approval of the Landlord was required, but that some work could begin in advance of the approval being given.

On April 10, 2008, the Landlord visited the site and was not happy with what was found. She expected that the work that was being undertaken to that point would be cosmetic. The Landlord demanded that the New Tenant's workers stop their renovations.

On September 24, 2008, the Superior Court issued a judgment against the Landlord, declaring that the Landlord unreasonably withheld its consent to its assignment of the lease to the new tenant. The Court further stated that the Old Tenant was not in default of the lease. The New Tenant refused to pay rent on the basis that it was entitled to set off against the rent owing based on the damages it had suffered due to the Landlord's refusal to consent to assignment and its stopping the renovation work.

On October 28, 2008, the Landlord delivered its consent to the assignment of lease to the New Tenant. The New Tenant continued to refuse to pay rent and instead deposited the rent money in their lawyer's trust account. On November 10, 2008, the Landlord terminated the lease. On April 2, 2009, the Superior Court ordered that upon payment of all rent owing, relief from forfeiture would be granted, and the lease would remain in force. Rent was never paid, however, and consequently no relief of forfeiture was granted. A trial was ordered with respect of damages for loss of business.

Damages of C\$1,417,000 were awarded to the New Tenant. The Court found no basis on which to justify the Landlord's actions in stopping the renovations and in purporting to expel the New Tenant from the premises. Prior to the termination notice being issued in November, the Landlord began to demolish the premises, making it impossible for the New Tenant to renovate. The resulting destruction of the premises led to the Landlord being held liable for damages for the full term of the lease, or C\$1,500,000 less the C\$288,000 in rent owing. The Court noted that the New Tenant's conduct in refusing to pay rent suggested that it was attempting to maximize damages, rather than paying rent and obtaining relief from forfeiture. Therefore, the New Tenant was not entitled to damages for the loss of equipment.

The lesson here for landlords and tenants is the importance of abstaining from actions which can be perceived

as an attempt at maximizing damages. Landlords cannot act precipitously so as to close down renovation and begin to demolish premises while waiting for a decision of the Court. Conversely, tenants cannot sit back and do nothing in order to avoid their obligations under the lease.

Leave Nothing Behind – the Defense of Abandonment

In the case of *Dean v. Kotsopoulos*, 2012 ONCA 143, serves as an illustration of the tort of conversion and the defense of abandonment.

In January 2006, Ronald James Dean and 1083994 Ontario Inc. (“Tenant”) leased premises from Steve Kotsopoulos (“Landlord”), in order to operate a restaurant. The Tenant also purchased previously owned restaurant equipment from the Landlord for C\$40,000.00 (the “Equipment”). In June 2006, the Landlord sent notice to the Tenant that no insurance had been obtained and that the lease would be terminated on June 30, 2006, if this default was not rectified.

On July 1, 2006, the Tenant vacated the premises and began to remove the Equipment, making four separate trips to the premises with a truck. On July 2, 2006, the Tenant claimed to have returned to the premises to remove the remaining Equipment, but found the locks to the premises changed. On July 6, 2006, the Landlord put a “For Rent” sign in the window of the premises and placed an advertisement in the *Toronto Star* newspaper stating: “restaurant and equipment for sale”. On July 13, 2006,

the Tenant’s lawyer notified the Landlord that the Tenant wanted an opportunity to access the premises to remove the Equipment.

On August 30, 2006, the Landlord entered into a new lease for the premises, which included the Equipment. On November 10, 2006, the Tenant’s solicitor notified the Landlord that the Tenant required access to the premises to claim the Equipment. The Landlord’s solicitor responded on November 15, 2006, stating that the Equipment had been abandoned and the Tenant had no claim.

At trial, the Landlord defended the Tenant’s claim for conversion on the grounds of abandonment. Justice Pitt (the “Trial Judge”) considered each of the four factors and determined that the Tenant had made minimal efforts to recover the Equipment (as evidenced by the sending of only two letters to the Landlord). Justice Pitt also noted that the Equipment was a part of the business, which the Tenant had left when they abandoned the premises on July 1, 2006. In addition, Justice Pitt stated that there was no evidence to demonstrate that the Equipment had any significant value. When taken together, the Trial Judge concluded that the Tenant had indeed abandoned the Equipment and dismissed the Tenant’s claim.

On appeal, Justice Feldman found that the Trial Judge had erred in his decision, and that there was sufficient evidence to demonstrate that the Tenant had not abandoned the Equipment and, accordingly, awarded the Tenant damages for conversion.

In making this determination, Master Justice Feldman found that the Trial Judge had failed to take the following evidence into consideration: (i) the tenant obtained an auctioneer to inspect and appraise the Equipment with a view to having it sold; (ii) the tenant had begun moving the Equipment out of the premises and only stopped when the locks were changed; (iii) the tenant caused its solicitor to write two letters to the landlord asserting its right to the Equipment; and (iv) the landlord failed to make efforts to contact the tenant prior to disposing of the Equipment.

In addition, Master Justice Feldman found that the Trial Judge had erred in finding that the Equipment had no significant value, as the tenant had paid C\$40,000.00 for the Equipment only five months earlier. Further, the fact that the equipment was included in the landlord’s lease to the subsequent tenant also demonstrated that the Equipment still retained value.

Dean v. Kotsopoulos provides both landlords and tenants with a roadmap as to how to handle the issue of a tenant’s equipment and chattels in the case where such items are left on the premises. A tenant must always be diligent in asserting its right of ownership by taking steps to recover the items, by notifying the landlord of its ongoing interests and by preparing all relevant documentation to demonstrate the value of its items. A landlord should take care to provide notice to the tenant of what items are in its possession and provide periodic updates as to the landlord’s intentions in respect of those items. ■



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