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FUNDAMENTAL BREACH
~ ADDING TO THE TENANT'S ARSENAL

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- Shopping Center Legal Update, Vol. 20, Issue 3
Winter 2000

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use of land and improvements. The court also rejected the lessee's argument that it only had to provide the required information if the county requested it. Saying that it sympathized with the lessee, the court nevertheless dismissed the petition for failure to provide the information within the statutory period. *Northwest Airlines, Inc. v. County of Hennepin*, File Nos. TC-25905, TC-26905, TC-27651, Minn.Tax Ct. 4th Jud.Dist., August 29, 2000.

Tort Liability

An individual was injured when he slipped and fell on snow and ice in a walkway between two leased premises. There was evidence that the lessees on both sides of the walkway had shoveled and salted the walkway at times prior to the accident. The court found that the tenants had failed to meet their initial burden of establishing they had no constructive notice of the allegedly dangerous conditions. There were snowdrifts up to the plaintiff's mid-calf and beneath the drifts, according to the plaintiff's deposition and the record showed the walkway had not been cleared of snow or ice in weeks. Consequently, the defendants had not demonstrated that the allegedly dangerous condition was not visible and apparent for a sufficient amount of time before the accident to allow them to discover it and remedy it. The order dismissing the complaint was reversed. *Mikolajczyk v. M.C. Morgan Contractors, Inc.* 709 N.Y.S. 2d 283 (N.Y.App.Div.2000).

A group of people were assaulted in a shopping center parking lot after being in a nightclub in the shopping center. They sued the owner of the center and the tenant-nightclub, claiming there was inadequate security and lighting. The court acknowledged a landlord's duty to protect tenants from third-party criminal acts when prior experiences with substantially similar crimes provide reason for a landlord to anticipate criminal acts. In this case, the landlord was not aware of any reports of crimes against persons or property. The plaintiffs themselves admitted that they had no knowledge of prior criminal incidents in the area and did not consider the area dangerous. The court concluded that the attack was not foreseeable by either the landlord or tenant and, thus, granted summary judgment for the landlord and tenant. *Habersham Venture, Ltd. v. Breedlove*, 535 S.E. 2d 788 (Ga.Ct.App.2000).

Legislation

Idaho—2000 New Laws, H.B. No. 681, expands the meaning of "just compensation" in eminent domain cases to include damages to businesses of more than five years' standing which are located on or adjoin property being taken.

From Canada

In Depth

Fundamental Breach—Adding to the Tenant's Arsenal

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In 1971 the Supreme Court of Canada, through the decision of *Highway Properties Limited v. Kelly, Douglas and Company Limited*, [1971] S.C.R. 562, acknowledged the hybrid nature of commercial leases. Not only are they conveyances of real property, but they are also commercial contracts allowing for the application of contract principles in their interpretation and enforcement. In Canada, the doctrine of "fundamental breach" has become a significant remedy available to tenants when faced with a material breach of lease by the landlord. This remedy is key to those tenants who are not considered to be "800 lb. Gorillas," which have the strength to negotiate multiple termination rights due to landlord breaches in their leases.

What Is Fundamental Breach?

Canadian law recognizes that in certain instances, a claim for damages against a defaulting party may not be sufficient. Accordingly, when a defaulting party has committed a breach of such significance so as to deprive the innocent party of the very essence of what it contracted for (a "fundamental breach"), the law provides the innocent part with the additional remedy of treating the contract as at an end. Fundamental breach has been described as a breach "going to the root of the contract" and as a breach that deprives a party of "the very heart of what it bargained for."

Adoption of the Remedy in Canada

In *Lehndorff Canadian Pension Properties Ltd. v. Davis Management Ltd.* (1989), 59 D.L.R. (4th) 1 (B.C.C.A.), the contractual remedy of fundamental breach was applied in a commercial lease setting for the first time (although it had been alluded to in a 1985 case—*Bramalea Ltd. v. Canadian Safeway Ltd.* (1985) 37 RPR 191 (Ont. H.C.J.). In Lehndorff, a law firm attempted to assign its lease of office space, but required the landlord's consent under the terms of its lease. After the landlord unreasonably refused to provide its consent, the tenant went to court to obtain relief. The British Columbia Court of Appeal concluded that, in unreasonably refusing to provide its consent, the landlord prevented the assignment and thereby "deprived the tenant of the entire economic benefit" of the lease. The landlord was found to have committed a fundamental breach of the lease, which entitled the tenant to treat the lease as at an end.

What makes this case even more interesting is the fact that it dispelled the notion that there could be no fundamental breach by a landlord unless the tenant was deprived of the right to physically occupy the space that was the subject matter of the bargain.

Subsequent Development of the Case Law

Just over a year after rendering its decision in *Lehndorff*, the British Columbia Court of Appeal was given the opportunity to consider another fundamental breach-of-lease claim. In *Wesbild Enterprises Ltd. v. Pacific Stationers Ltd.* (1990), 14 R.P.R. (2d) 25, the tenant operated a stationery and office equipment store. The landlord altered the means of access to the rear of the premises such that it became extremely difficult to deliver merchandise. A majority of the Court was of the view that the landlord's alterations constituted a fundamental breach of the lease because the tenant's business depended on easy access to the rear of the premises. Also

noteworthy were Lambert J.A.'s comments to the effect that the courts must take a tenant-oriented approach in each particular case in assessing whether or not a particular breach entitles the tenant to treat the lease as at an end:

"...I think that it is possible that one landlord can make identical leases with two tenants and then breach the lease agreement with the two tenants in the identical clause and that could be a fundamental breach in relation to one tenant and not a fundamental breach in relation to the other. It is the particular business that has to be looked at to decide whether the breach is a fundamental one in relation to that tenancy and not just the clause that was breached." (our underscore for emphasis)

In 1995 the Ontario Court of Appeal followed the lead of its Western counterpart, finding that an office tenant was entitled to terminate its lease due to the landlord's failure to recognize the tenant's right of first refusal to lease adjoining space. In the Court's view, the expansion space was an essential term of the bargain and, therefore, the tenant was justified in treating the lease as at an end [*Ad Hoc Management Inc.* v. *Prudential Insurance* (1995) O.J. No. 1419 (QL)].

A case that involved a landlord's breach of an exclusive-use provision also deserves mention. In *Prince Business Inc.* v. *Vancouver Trade Mart Inc.* (1994) B.C.J. No. 2647 (QL), the tenant was granted an exclusive to operate a cafeteria and smoke shop in the building. A school board subsequently moved into the building and installed food and drink vending machines on its floor. Not only did the Court of Appeal hold that the installation and operation of the vending machines breached the exclusive, but it also found that the "shortcomings on the part of the landlord could be said to be sufficient to frustrate the commercial purpose of the tenant's Lease and to constitute a fundamental breach giving rise to rescission and damages."

Recent Decisions

Over the last 18 months or so, three new cases have addressed the issue of fundamental breach in Canada. In *Chisos Investment Co.* v. *Hanlahan* (1999) O.J. No. 1374 (QL), a tenant was able to successfully argue that the landlord's breach entitled the tenant to treat the lease at an end. The landlord induced the tenant to leave its existing location (in Mall A) and move into the landlord's centre (in Mall B). The landlord agreed to pay the tenant's remaining rent on its lease for Mall A. After the tenant was successfully sued by the landlord of Mall A, the tenant looked to its new landlord to cover the award. When the new landlord refused, the tenant treated its lease for Mall B as at an end. In finding for the tenant, the Court held that in return for the tenant's covenant to pay rent for space in Mall B, the landlord undertook the primary obligation to reimburse the tenant for its payment obligations under its lease for Mall A. The landlord's failure to reimburse the Tenant constituted a fundamental breach by the Landlord.

In *Shun Cheong Holdings B.C. Ltd.* v. *Gold Ocean City Supermarket Ltd.* (2000), 31 R.P.R. (3d) 179 (B.C.S.C.), the tenant operated a grocery store that was subjected to frequent leaks of a foul-smelling, greasy liquid, which emanated from the restaurant above the tenant's store. These leaks created a health and safety hazard as well as a negative effect on the attractiveness of the tenant's business. The Court found that the landlord's failure to remedy the leakage problem could reasonably be described as having the effect of preventing the tenant from operating its business such that the "very purpose of the tenancy was undermined in a fundamental way." The Court was of the view that the tenant was justified in terminating its lease. In reaching its decision, the Court noted that each case must turn on its own set of facts (explicitly adopting the principles enunciated in *Wesbild*).

Shortly after Shun Cheong was decided, the Ontario Superior Court of Justice was called upon to consider a similar situation [*Framlance Properties Ltd.* v. *Dahan's Fashion Optical Ltd.*, [2000] O.J. No. 1746 (QL)]. In this case, the tenant vacated the premises, claiming that they were not fit for business due to a constant foul smell and the presence of live mice, dead birds and animal feces. The tenant also claimed (and the evidence disclosed) that the premises were prone to flooding after every rainfall. In finding for the landlord, the Court noted that the lease did not require the landlord to repair the premises nor was there an implied condition that the premises were fit for the use intended by the tenant. On the evidence, it was found that the tenant was able to carry on business and while there may have been some interruption, the property was not rendered inhabitable. Therefore, there had not been a fundamental breach of the lease by the landlord, which could justify the tenant's repudiation. The tenant's remedy was in damages only.

What makes this case interesting is the fact that this Ontario Court seems to have articulated what tenants must establish in order to be successful on a claim based on fundamental breach: "acts of commission by the lessor must be found which are calculated to destroy the lessee's enjoyment of the premises." It remains to be seen if a subsequent or higher court will interpret this principle as meaning that the tenant's right to physically occupy this space must have been deprived.

Conclusion

It is very clear, however, that the acceptance of the fundamental breach remedy in favour of tenants can, and most probably will, lead to an unlimited number of scenarios in which the doctrine will be argued. The difficulty, however, will be in predicting the success of each argument, as undoubtedly each case will turn on its own set of specific facts. Both parties should keep this remedy in mind vis-à-vis their conduct throughout the tenancy relationship.