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"REELING THEM IN: WHAT TO DO WHEN THERE IS A DEFAULT"

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"Casting The Net Commercial Lease"
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REELING THEM IN:

WHAT TO DO WHEN THERE'S A DEFAULT[1]

INTRODUCTION

When there is a default there are three areas which should be considered:

- what does the lease say about the default in question?
- are there any provisions in the *Commercial Tenancies Act* (the "Act") which apply to the default in question? and
- has the landlord waived its right to act on the default?

In this paper we will review the default remedies typically available to a landlord in a comprehensive and sophisticated commercial lease. We will review the enforcement of those provisions and consider the advantages and disadvantages of any one particular course of action.

For the most part the remedies stipulated in the lease document will govern. However there are exceptions, caveats and cautions which must be kept in mind. By way of introduction here are three examples and many more will be discussed in this paper:

- section 19(2) of the Act provides that the landlord must give reasonable notice of a non-monetary breach and an opportunity to cure prior to exercising its right of re-entry. While the lease can override many of the provisions of the Act, it is generally

[1] I would like to acknowledge the significant contributions made to this paper by each of Deborah Watkins, Ken Beallor and Eric Gillespie. Without their help I would still be writing this paper.

accepted that this is one section the parties cannot contract out of.

- where the lease is silent, for instance, on the giving of notice to the tenant of a rental default, section 18(1) of the Act governs. This section provides that the landlord may re-enter, without notice, if the rent has been in arrears for 15 days;
- the equitable principle of waiver may limit the landlord's right to terminate the lease or otherwise exercise its remedies under the lease, notwithstanding a non-waiver provision in the lease.

I. DEFAULT: PRELIMINARY CONSIDERATIONS

1. The Lease

The standard form of lease used by sophisticated commercial landlords will typically include a full and comprehensive "Default" section. A sample default section is attached as Schedule "A". When there is a default, the lease document must be fully and carefully reviewed in order to determine if, in fact, a default has taken place, and what rights the parties then have.

The most common default is a failure by the tenant to pay rent. However, both the tenant and the landlord will likely have a much wider variety of obligations under the lease. Some of these, such as covenants to repair, may have specific default provisions or remedies attached to them. Commercial leases will also contain a general provision which states that any failure to perform any term or condition, or to abide by any covenant in the lease, is an event of default.

2. Nature of the Default: Monetary or Non-Monetary Breach?

When any type of default by a tenant occurs, one of the key questions to ask is: is this a monetary or a non-monetary default? To answer this question, one must consider the definition of 'rent' in the lease. Rent is generally defined in commercial leases to include minimum rent, additional rent and all other sums payable by the tenant to the landlord under the lease. Certain charges which the landlord may wish to collect from the tenant (such as capital tax, large corporations tax, management and administration fees which are generally found under the definition of "Operating Costs" or "Net Lease") must be specifically addressed in the lease to be recoverable by the landlord.[2] The benefit to the landlord of an expansive definition of rent in the lease is:

(a) a wider range of remedies are available to recover those arrears, such as the landlord's right of distress;

(b) a default in the payment of rent generally has shorter and less onerous notice requirements than those governing non-monetary defaults (ie. no need to comply with the strict notice provisions in Section 19(2) of the Act; and

(c) in the event the tenant is placed into bankruptcy, the landlord has the right to accelerate rent for a three month period and will rank as a preferred creditor for the accelerated rent. Accordingly, the wider the definition of rent is the larger the tenant's preferred claim would be.

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[2] *Dylex Ltd.* v. *Premium Properties Ltd.*, [1996] O.J. No.2165 (Gen. Div.); *Han* v. *9938 Investments Ltd.* (1995), 45 R.P.R. (2d) 100 (B.C.C.A.); *KPMG Peat Marwick Thorne and Johnson & Higgins Ltd.* v. *SPE Operations Ltd.*, unreported, No. 4675/94, April 6, 1995.

Another important question is; "Does the lease provide for accelerated rent upon any default by the tenant under the lease?" If the lease does provide for acceleration of rent on default (usually 3 months) then even a non-monetary default by the tenant would give rise to a rental default which would then allow the landlord to pursue remedies available on non-payment of rent (ie. distress) and to avail itself of the less onerous notice requirements.

In addition, is there, or is there likely to be a dispute with the tenant as to whether there is a default in the payment of rent (in particular, look for any tenant's rights of set-off in the lease)? If the tenant is subsequently found by a court not to have been in default of its obligation to pay rent, then the landlord may be liable for damages wrongfully terminating the lease or wrongfully distraining against the tenant's property.

3. Who is Occupying the Premises?

The landlord must also consider who is occupying the premises. If it is someone other than the original tenant named in the lease, then a wide variety of other considerations may apply. Some of these include:

(a) Subtenants:

(i) If the landlord is considering terminating the lease as a result of the default, section 21 of the Act permits a subtenant to apply to the court for relief from forfeiture. However, many sublease agreements specifically provide that the subtenant waives its rights under section 21 of the Act. The rights of the subtenant on such an application will depend on many factors including

whether the landlord has consented to the sublease.

(ii) If the landlord is considering distraining against the tenant's goods as a result of the default, section 32(2) of the Act allows a subtenant occupying the premises *with the consent of the landlord*, to provide a statutory declaration that the head tenant has no interest in its goods and to pay any rent owing under its sublease directly to the landlord, upon which the landlord will have no right to distrain against those goods upon the premises belonging to the subtenant.

(b) Receiver:

(i) if there is a receiver at the premises and the receiver is court appointed, the receiver is an officer of the court and acts in its own capacity and not as the agent of the tenant. Most receiving orders provide for a stay of all proceedings against the debtor. Accordingly, the landlord would have to make an application to the court to enforce its rights under the lease (ie. to distrain for rental arrears or to terminate the lease);

(ii) if the receiver is privately appointed, such as by a creditor under a general security agreement, the receiver is then the agent of the creditor, and the landlord retains all of its rights under the lease including its right to distrain. The landlord may even have the right to terminate the lease where the appointment of a receiver is an event of default under the lease.

4. Notice Requirements

The lease should be reviewed to determine who must be given notice in the event of default and how is notice going to be given, i.e. concurrent with notice to tenant, who else must be notified of the default and the landlord's intentions?

(a) The Tenant - check notice provisions in the lease, and carefully check property management files for any notices of change of address;

(b) Guarantor/Indemnitor - if there are any guarantors or indemnitors of the lease, notice should be provided to them concurrent with the notice to the tenant. Failing to notify the guarantor or the indemnitor could render the guarantee or indemnity unenforceable;

(c) Mortgagee or other lender: in some cases (especially large ground leases) where the tenant mortgages its leasehold interest to finance the development of the property, the landlord will almost certainly have entered into an agreement with the lender agreeing, amongst other things, to provide the lender with notice of any defaults under the lease and the right to cure such defaults.

(d) Franchisor: leases entered into by tenants who are parties to a franchise agreement may contain provisions requiring the landlord to give the franchisor notice of any default and an opportunity to cure the default or assume the lease. Alternatively, there may be a separate agreement between the landlord and the franchisor which requires that notices of default be provided to the franchisor.

5. The Overall Objective: Preserving or Terminating the Lease?

There are a number of overall considerations that go into the decision of how the landlord should proceed when a default under the lease occurs. These include:

(a) you may not distrain once you terminate the lease;

(b) landlord's duty to mitigate arises once the lease is terminated;

(c) if terminating the lease, written notice of your intention to claim damages for the loss of the benefit of the lease to the end of the term must be provided to the tenant either concurrent with the notice of termination or shortly thereafter[3]. Commencing an action for damages shortly after terminating the lease has been held to be sufficient notice to the tenant of the landlord's intent to claim damages for loss of the benefit of the lease to the end of its term[4]. Failure to provide the tenant with such notice may result in the landlord losing its right to claim for future damages.

II. TERMINATING THE LEASE: FORFEITURE

Except in cases of non-payment of rent, courts generally do not look favourably on forfeitures. In some instances, however, forfeiture can be a useful tool for landlords, provided that certain

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[3] *Highway Properties Ltd.* v. *Kelly, Douglas & Co.* (1971), 17 D.L.R. (3d) 710, [1971] S.C.R. 562 (S.C.C.)

[4] *North Bay T.V. & Audio Ltd.* v. *Nova Electronic Ltd.* (1983) 4 D.L.R. (4th) 88, aff'd 12 D.L.R. (4th) 767 (C.A.)

procedural matters are followed.

1. The forfeiture procedure - General

The landlord's forfeiture rights for non-payment of rent are set out in s. 18 (1) of the Act, and for non-monetary breaches we must look to section s. 19(2). Section 18 (1) specifically allows the parties to agree to terms other than those in the section. Section 19(2) does not specifically allow the parties to contract out of that section, although Estey CJHC (as he then was) suggested , in *obiter*, in *Mount Citadel Ltd. v. Ibar Developments Ltd.*[5] that it was possible to contract out of this section. The decision has not been generally accepted as correct.

2. Monetary Breaches: Non-payment of rent

Under s. 18 (1) of the Act, the landlord has the right to re-enter the premises if rent is outstanding for more than 15 days. In practice, landlords are reluctant to wait such a long period of time and will generally allow no more than five days delay before declaring default. In fact, the lease may provide that the landlord has the right to re-enter immediately if rent is not paid on the date it is due. The Act does not require the landlord to give a notice to the tenant of its default in paying rent although most leases provide for notice to the tenant. This does not apply to non-payment of security deposits only; in those cases the more arduous procedure described for breaches other than non-payment of rent has to be followed.[6]

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[5] (1976), 14 O.R. (2d) 318 (H.C.)

[6] *Nationwide Parking Inc. v. Daulat Investments Inc.* (unreported, Ont. H.C., June 15, 1990, Doc. No. Toronto RE 1278/90).

The tenant has the right under s. 20 (1) of the Act to apply to the court for relief from the forfeiture. Parties to a commercial lease cannot contract out of s. 20 (1): section 20 (6) stipulates that it applies despite any stipulation to the contrary.

3. Non-monetary Breaches

Under s. 19 (2) of the Act, the landlord must provide the tenant with notice of the alleged breach, setting out a reasonable time to correct the breach if possible and in any case requiring monetary compensation for the landlord's losses stemming from the breach. It is only after this period expires and the tenant fails to comply with this notice that the landlord has a right to forfeit the lease and re-enter the premises or seek a writ of possession.

The notice must clearly and correctly describe the breach[7] and request that the breach be remedied if it is possible to remedy it. The notice should set out any claims to compensation; however, if the landlord is not seeking compensation, then the failure to include a compensation claim in the notice will not invalidate it.[8] Not making a claim for compensation does not necessarily prevent the landlord from seeking damages at a later date. Even if the breach cannot be remedied, the notice must be issued before forfeiture can take place.[9] It must be clear from the notice that the tenancy is

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[7] an incorrect description may render the notice invalid: *Holman v. Knox* (1912), 25 O.L.R. 588 at 604, per Sutherland J. (Ont. Div. Ct.)

[8] *Chick'n Treats Inc. v. Woodside Square Ltd.* (1990), 38 O.A.C. 138 (C.A.)

[9] *780046 Ontario Ltd. v. Columbus Medical Arts Building Inc.* (1994), 118 D.L.R. (4th) 609 (Ont. C.A.)

in jeopardy: a notice that contemplates the continuation of the landlord-tenant relationship is not valid.[10]

Section 19 (2) states that the landlord must give reasonable time to correct the breach if it can be corrected, and/or make compensation if compensation is sought. The lease may set out what the parties accept as reasonable time for a notice under s. 19 (2).

4. Forfeiture and Re-entry

Once the notice period expires and the breach has not been remedied then the landlord may forfeit the lease and re-enter. The forfeiture must be an act which is not compatible with a continued landlord-tenant relationship.[11] A mere notice is not sufficient.[12] The commencement of an action or application for possession under Part III of the Act has been held to be an act of forfeiture.[13] Changing the locks is the usual and most reliable way to effect forfeiture.[14]

5. Writ of Possession

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[10]*Re Simpson and Young & Biggin Ltd.* [1972] 1 O.R. 103 (C.A.)

[11]*Winbaum v. Ginou* [1947] O.R. 242 (H.C.)

[12]*Re Simpson and Young & Biggin Ltd., supra*

[13]*Grimwood v. Moss* (1872), L.R. 7 C.P. 360

[14]though in one unusual case where the premises served as an airport, changing the locks was found insufficient because planes could still land and take off: *Falkowski v. Wilson* (1965) 49 D.L.R. (2d) 490 (Ont. H.C.)

The landlord may apply to the court under Part III for a writ of possession. This is a summary procedure which is usually relatively speedy. If unopposed, it might take no more than a few days; and even if opposed, it is not too optimistic to expect a decision in a few months. The writ is a good alternative if physical re-entry is not possible, if it is likely to be unopposed or if the re-entry is not urgent.

6. Distress

Distress will not effect termination of the lease; in fact, if the lease has been terminated distress is no longer available since distress is an incident of the landlord-tenant relationship and termination ends that relationship.

7. Waiver

In any default situation, the landlord must be careful not to do anything that could be interpreted as a waiver or an indication of intention contrary to forfeiture. Waiver is discussed in more detail below; however two points are worth making:

(a) Accepting rent from the tenant which came due after the default came to the landlord's attention is generally seen as a waiver of the forfeiture. This is so even where the lease specifically includes a "non waiver" provision which states that the acceptance of the rent is without prejudice to and is not a waiver of a forfeiture.[15] Rent arrears, however, may be accepted by landlord on account for periods prior to

[15] *Mbozos v. Hios* (1982), 36 O.R. (2d) 627 (H.C.), *Royal Inns Canada v. Bolus-Revelas-Bolus* (1982), 37 O.R. (2d) 339 (Ont. C.A.)

the notice.

(b) If the breach complained of is the abandonment of the premises, the landlord should not accept the keys to or possession of the premises from the tenant. Such acceptance may be held to be an acceptance to the tenant's abandonment.[16]

8. Mitigation

In case of a breach, the landlord has the right to sue for the rent for the balance of the lease term. If the landlord has terminated the lease, it must mitigate its losses. A written notice of the intention to sue, setting out the damages claimed, must be provided to the tenant at the time the lease is terminated. In addition to present value of expected future rent, damages may also be claimed for other losses, including costs of re-renting the premise. The landlord may also claim damages for such things as an unauthorized renovation[17]. The measure of the damages for the breach will usually be the injury to the value of reversion - i.e. the projected loss to the value of the property[18].

The area of mitigation of damages by the landlord has recently been complicated by the decision of Sutherland J. in *Unisys Canada Inc. v. York Three Associates Inc.*[19] In that case the court found, quite correctly, that the landlord could not recover damages which it could reasonably have avoided.

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[16] *Gulutzan v. McColl-Frontenac Oil Co.* (1960), 35 W.W.R. 337 (Sask. C.A.)

[17] *Finnegan's Ltd. v. Azores Wharf Ltd.* (1981), 99 A.P.R. 448 (Nfld. T.D.)

[18] *Gooderham & Worts v. C.B.C.*, [1947] 1 W.W.R. 1, (P.C.)

[19] [1999] O.J. No. 4859, Ontario Superior Court of Justice, December 17, 1999.

The problem is, the court seems to suggest that in mitigation of its damages the landlord should have renegotiated its lease with its tenant and accepted a lesser rent. This is a questionable application of the mitigation. The case is currently under appeal and we are hopeful that the court of appeal will limit the impact of this decision.

III. RELIEF FROM FORFEITURE

1. Relief from Forfeiture: The Tenant's Right to Challenge

The tenant has the right under s. 20(1) of the Act and s. 98 of the Ontario *Courts of Justice Act* (the "CJA"") to apply to the Ontario Superior Court of Justice for relief from the forfeiture. Parties to a commercial contract cannot contract out of s. 20 (1): section 20 (6) states that it applies despite any stipulation to the contrary.

If the forfeiture is for a breach other than the non-payment of rent, even the slightest of procedural mistakes by the landlord may prove fatal. If the requirements as to notice and period for compliance are not complied with, the courts may use that as the basis for granting a reprieve from forfeiture to the tenant on a relief from forfeiture application In *780046 Ontario Inc. v. Columbus Medical Arts Building*,[20] Laskin J.A. explained the reasons for this rule as follows:

> "Notice is a protection of the tenant. Its purpose is to warn the tenant that its leasehold interest is at risk and to give the tenant an opportunity to preserve that interest by remedying

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[20] *Supra* at p. 616 D.L.R.

> the breaches complained of and, where necessary, by compensating the landlord. Because courts have not looked favourably upon the remedies of re-entry, forfeiture, and termination they have insisted that landlords strictly comply with the notice requirement in s. 19(2) of the Act."

Forfeitures are also set aside if they were illegal for reasons other than inappropriate notice, such as the lease not giving the landlord the right to forfeit the lease for the breach alleged or that the tenant was not given sufficient time to remedy the breach or give financial compensation.[21] The tenant may also argue that the landlord waived its right to forfeit.[22] The outcome of such arguments will depend on the facts in each case.

Even if the landlord complied with all procedural and substantive requirements, a court may still grant relief from forfeiture. The courts are particularly concerned to ensure that landlords do not use the forfeiture provisions to get out of their long-term bargains with the tenant merely because that bargain is no longer advantageous to them. Thus forfeiture will be set aside for breaches that are merely technical and cause no losses to the landlord.[23] However, relief from forfeiture will almost never be granted unless the tenant is willing, ready and able to fully compensate the landlord for its

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[21] *Re Industrial Propane Inc. and Cooper* (1984), 48 O.R. (2d) 321.

[22] *Mbozos v. Hios (supra)*.

[23] *Re Hurontario Management Services Ltd. and Menechella Brothers Ltd.* (1983), 41 O.R. (2d) 348 (C.A.); *York Condominium Corp. No. 26 v. Becker Milk Co.* (1982), 37 O.R. (2d) 679 (Co. Ct.)

losses.[24]

If the tenant made significant improvements to the premises so that the landlord reaps a windfall, or if the financial hardship to the landlord is much smaller than what the hardship to the tenant would be if the lease was forfeited, relief is also often forthcoming.[25]

The tenant's actions will also be examined: ie. tenants that breach the lease flagrantly and repeatedly,[26] or for a long time after they were warned are less likely to obtain relief.[27] Tenants also must come to court with clean hands, for example in *461 King St. W. v. 418 Wellington Parking*[28] where the tenant refused other tenants access to the parking lot thereby threatening the landlord's business, relief from forfeiture was refused.

Conversely, tenants that breached the lease inadvertently, or who seriously attempted to correct the breach are more likely to get a reprieve.[29]

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[24]*Re Rexdale Investments*, [1967] 1 O.R. 251 (C.A.)

[25]*Re Koumoudouros and Marathon Realty Co.* (1978), 21 O.R. (2d) 97 (Div. Ct.)

[26]*Jeans West Unisex Ltd. v. Hung* (1975), 9 O.R. (2d) 390 (H.C.)

[27]*Re Jawanda and Walji et al* (1975), 10 O.R. (2d) 527, at 531 (Div. Ct.)

[28](1994), 40 R.P.R. (2d) 220 (Ont. Gen. Div.)

[29]*Conwest Exploration Co. Ltd. et. al. v. Letain*, [1964] S.C.R. 20.

IV. DISTRESS

The landlord may levy distress against the tenant's goods on the premise for arrears of rent during the currency of the lease. The following is a general outline of the remedy of distress, together with some basic practical considerations.

1. What Is "Distress"?

Distress is a combination of a statutory and common law self-help remedy whereby the landlord is entitled to seize and sell the goods of the tenant upon the leased premises (chattels not fixtures) to satisfy any existing rental arrears.

2. When Can It Be Exercised?

The remedy of distress is only available when there is a landlord and tenant relationship and a default in the payment of "rent" as that term may be defined in the lease. It can only be exercised after there has been default in the payment of rent and may only be exercised between sunrise and sunset , and never on a Sunday(??).

3. How Is Distress Exercised?

The landlord or its agent, usually a bailiff, may enter the premises during daylight hours to distrain. The landlord or its agent may not use force to enter the premises to effect the distress. Note that it has been held that using a pass key to enter the premises when locked without the consent of the tenant for the purposes of distraining is a forcible entry and renders the distress illegal. Be aware that

if using a bailiff to effect the distress, the bailiff is the agent of the landlord and the landlord will be responsible for the actions of the bailiff during the distress.

4. What Goods May Be Seized?

The landlord may seize those goods upon the premises belonging to the tenant and any other party liable to pay rent[30]. However there are numerous exceptions,[31] including:

(a) The landlord can only distrain against chattels of the tenant and not fixtures. Trade fixtures are fixtures not chattels and are not subject to distress despite the fact that the lease allows the tenant to remove them at any time during, or on expiration of the term.[32] Given the myriad of case law on the distinctions between fixtures and chattels, there remains constant uncertainty over what is a fixture and what is a chattel, especially when dealing with equipment. The general rule is that if it is affixed to the property it is a fixture. However the case law has distinguished on many occasion between levels of affixation to the property and found what some would have considered fixtures to be chattels.

(b) The goods must be owned by the tenant. Goods on consignment are not owned by the tenant consequently they are not subject to distress. Similarly, with goods placed

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[30]Section 31(2) of the *Commercial Tenancies Act*.

[31]See also Section 2 of the *Execution Act*, R.S.O. 1990, c. E.24.

[32]*859587 Ontario Ltd. (c.o.b. Atlantic International Equipment Sales)* v. *Starmark Property Management Ltd.* (1998), 81 A.C.W.S. (3d) 539; [1988] OJ No. 3022; appeal from (1997), 34 OR (3d) 43.

on the premises for conditional sales, the right of the landlord to distrain is limited to the tenant's interest in the goods subject to the conditional sales agreement.[33]

(c) The landlord must determine if there are goods subject to any security interests. The current status of the law is that if the landlord commences its distraint prior to any seizure by a secured party under its security, the landlord will have priority over the secured creditor.[34] Essentially it is a race to the swiftest. However, the Ontario Court of Appeal has held that a landlord's distress completed within 3 months of a tenant's bankruptcy, amounts to a "fraudulent preference" and that the proceeds of the distress belong to the trustee in bankruptcy leaving the landlord with its preferred claim under the *Bankruptcy and Insolvency Act*[35]. Due to the numerous cases concerning priorities before the courts though, it is open for the courts to reverse the current state of the law or to provide for additional exceptions to the rule, thus leaving a further level of uncertainty as to priority when rendering a distress.

5. To Distrain or Not to Distrain?

(a) Pros:

(i) does not terminate the lease;

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[33] *J.R. Autobrokers Ltd.* v. *Hillcreast Auto Lease Ltd.*, [1968] 2 O.R. 532 (H.C.)

[34] *Commercial Credit Corp. Ltd.* v. *Harry D. Shields Ltd.* (1980), 29 O.R. (2d) 106, affd 32 O.R. (2d) 703 (C.A.)

[35] *Canadian Imperial Bank of Commerce* v. *Canotek Development Corporation* (1997), 35 O.R. (3d) 247 (C.A.)

(ii) costs of distress chargeable to tenant;

(iii) fast and gets tenant's quick attention;

(b) Cons:

(i) Uncertainty over whether goods are chattels or fixtures;

(ii) Detailed and onerous procedures which if not strictly followed could lead to the landlord being liable for trespass and/or even termination of the lease, which would then preclude the landlord from claiming damages for the loss of the benefit of the lease to the end of its term. Example: changing the locks and denying tenant access to the property while distraining could result in the termination of the lease, which then results in the landlord losing its right to distrain (as the right only exists so long as there is a landlord and tenant relationship) as well as losing its right to sue the tenant for damages for loss of benefit of the lease to the end of its term.

(iii) Uncertainty as to the title of the goods being seized.

(iv) Further complicated by trust claims by, the Ontario Ministry of Finance for Retail Sales Tax and other provincial taxes, and superior lien claims by the Canada Customs and Revenue Agency for unpaid G.S.T. and Employee remittances. These claims have priority over the landlord's right to distrain and attach to and follow the goods.

(v) Can be defeated if tenant becomes bankrupt before the distress is complete (ie. before the goods are sold and proceeds distributed to satisfy the arrears) or if the tenant becomes bankrupt within 3 months of the completion of the

distress.

6. Some Practical Considerations

(a) Has the Landlord contracted out of the right to distrain in the Lease? It is common especially in ground leases where the tenant is making a substantial investment in the development of the property for the tenant to insist that the landlord waive its rights to distrain against the goods of the tenant.

(b) Is there, or is there likely to be a dispute with the tenant as to whether there is a default in the payment of "rent" (look for tenant's rights of set-off in the lease)? If the tenant is subsequently found by a court not to have been in default of its obligation to pay rent, the landlord may be liable for damages for trespass and conversion if it completed its distraint.

(c) Value of the goods, ie. the goods may have a greater value on the premises (eg. restaurant equipment) than if sold under a distress;

(d) The financial position of the tenant. Is the tenant on verge of bankruptcy? If tenant becomes bankrupt before the landlord completes its distraint (ie. sale of goods seized and the receipt and application of the proceeds of the sale to arrears of rent) then the landlord's claim for distress will be defeated and the goods or proceeds from the sale of the chattels will vest in the trustee.

(e) If the tenant has substantial assets and values the premises, the landlord may prefer to sue the tenant for arrears of rent and reduce the potential risk of having the lease terminated or being found liable to the tenant for damages in the event of an illegal

distress.

(f) Distraining may interfere with the tenant's business being conducted from the premises and further impair the tenant's ability to pay arrears of rent or future rent.

(g) For retail tenants in particular, where there are arrears of rent it is likely that there are also arrears of PST, GST and employee remittances, all of which have superior claims to the landlord's distress.

V. SELF-HELP REMEDIES

The remedies of forfeiture and distress discussed above are "self help" remedies used by landlords without the need for judicial approval or intervention. While forfeiture and distress are the two most common self help remedies, some additional remedies that do not depend on court proceedings are also often included in a lease.

1. The Right to Cure Tenant Defaults

Most commercial leases contain provisions allowing the landlord to cure the defaults of the tenant without effecting a termination of the lease. These provisions usually further provide that any costs incurred by the landlord in curing such defaults are the responsibility of the tenant and may be recovered by the landlord as additional rent under the lease. For example, where the tenant, after proper notice from the landlord, has failed to carry out the necessary repairs required of it under the lease, the landlord may elect to enter the premises and make the necessary repairs. The costs of the

repairs would be chargeable to the tenant as additional rent under the lease, and if not paid the tenant would then be in default of its rental obligations under the lease. This provides the landlord with a wider scope of remedies and simpler notice requirements if it then elects to terminate the lease.

2. The Right to Re-Let on the Tenant's Behalf

Most commercial leases also provide that upon default, the landlord may re-enter the premises without terminating the lease and re-let the premises on behalf of the tenant. Despite having this right, it is rarely used as a court may find that the lease was terminated on the re-letting because the new lease was on terms and conditions inconsistent with, or that altered the original tenant's obligations under the original lease (such as extending beyond the term of the original lease). The result would be the landlord's loss of its right to claim damages for loss of the benefit of the lease for its term.

Coupled with the Landlord's right to re-enter and re-let is often the landlord's right "to make such alterations to the premises as are necessary in order for tenant to re-let the premises, the costs of which are then chargeable to the tenant." This is not a blanket right for the landlord to effect any alterations it wishes, as the courts will impose some reasonableness on the landlord and look to see if the alterations could have been reasonably foreseen or contemplated by the tenant as necessary for the landlord to re-let the premises.

3. The Right to Appoint a Receiver

Occasionally, commercial leases will provide that on an event of default, such as non-payment of

rent, the landlord will have the right to appoint a receiver . This is rarely done due to the exposure of the landlord to liability for the acts of the receiver and the fact that landlords are not in the business of running tenants' businesses.

4. The Right to Act as Attorney of the Tenant

On the sale or re-financing of leased property, the landlord will generally require estoppel certificates from its tenants as a condition of the closing of the transaction. Most leases provide that the tenant must deliver to the landlord estoppel certificates within a certain number of days from the date requested by the landlord. To ensure that they are delivered in time and do not delay the landlord's closing of its transaction, many leases provide that if the tenant fails to execute and deliver the estoppel certificate to the landlord as required under the lease, the landlord may execute the estoppel certificate as attorney for the tenant.

5. The Landlord as a Secured Creditor

It is common these days for landlords to take a security interest in the property of the tenant to secure the tenants obligations under the lease. The benefit of taking a security interest in the property of the tenant is that if properly drafted and registered in accordance with the provisions of the *Personal Property Securities Act*, upon bankruptcy of the tenant, the landlord will be a secured creditor for the full amount of the tenant's debt under the lease as opposed to being a preferred creditor for 3 months accelerated rent and an unsecured creditor for the balance of the debt the tenant as provided for under the *Bankruptcy and Insolvency Act*.

VI. WAIVER OF FORFEITURE

Courts have consistently held that a landlord's right of forfeiture will be waived where there is an "unequivocal act" of the landlord confirming the existence of the lease, after the landlord has knowledge of or is deemed to have knowledge of a tenant's breach. The most common "unequivocal act" constituting waiver is acceptance of rent by the landlord **after** the tenant has breached a covenant of the lease[36]

For example, in the case of *Lippman v. Lee Yick* [37] the tenant breached the lease by subleasing the premises to a third party without the landlord's consent. The landlord, with knowledge of the arrangement made between the tenant and the third party, accepted rent from the tenant. The court held that the landlord waived its right of forfeiture when it accepted the rent.

In fact, even where acceptance by the landlord of rent has been due to clerical error, if acceptance of rent occurs after the landlord has become aware of the breach, the landlord's acceptance will still constitute waiver of forfeiture as a matter of law. In *Central Estates (Belgravia) v. Woolgar (No.2)*[38] the landlord circulated a memorandum to its employees informing them of the landlord's decision to forfeit the tenant's lease and instructing the employees not to demand or accept rent

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[36] *Royal Inns of Canada Ltd. v. Bolus-Revelas-Bolus Ltd.* (1982), 37 O.R. (2d) 339 (C.A.); leave to appeal to S.C.C. refused (1983), 38 O.R. (2d) 703n

[37] [1953] O.R. 514 (H.C.)

[38] [1972] 1 W.L.R. 1048, [1972] 3 All E.R. 610 (C.A.)

from the tenant. A clerk did not receive the memorandum and demanded rent from the tenant. The court held that the landlord had waived its right to forfeit the lease.

If a landlord accepts money after the default which represents rent due and owing **before** the default occurred, this will *not* constitute waiver of the landlord's right to terminate the lease for the default.

The right to forfeit (and therefore the right to re-enter) for breach of covenant to pay rent is incapable of revival after the landlord has waived the right[39].

1. Intention of the Parties: Irrelevant

Where there has been an unequivocal act done by the landlord recognizing the existence of the lease (for example, the acceptance of fresh rent) after having knowledge of the ground of forfeiture, the intentions of the parties are irrelevant; it is immaterial that the landlord did not intend its action to waive forfeiture and that the tenant knew at the time of paying the rent that the landlord intended to forfeit the lease. *(Belgravia)*

2. Attitude of Courts

"The courts **do not** look with favour upon forfeitures, and will take advantage of even trifling

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[39] *Malva Enterprises Inc. v. Rosgate Holdings* (1993), 14 O.R. (3d) 481 (C.A.)

reasons to avoid upholding them."[40]

3. Impact of a Non-Waiver Clause in a Lease

There is judicial authority to support the proposition that a non-waiver clause contained in a lease will be ineffective in a situation where a landlord has waived a breach of the lease by accepting rent from the tenant after the tenant's default. (*Royal Inns*)

Further, there is authority for the proposition that the landlord will be held to have waived the right to forfeiture upon the acceptance of rent even where the lease contains a provision that states that any waiver will be ineffective unless it is in writing. In *R. v. Paulson*[41] the landlord was held to have waived forfeiture despite the fact that a letter sent by the landlord to the tenant expressly stated that the rent was only being accepted conditionally.

However, there is recent caselaw which stands for the countervailing proposition. That is, where there is a clear non-waiver provision in a lease, acceptance of rent by the landlord after notice of default **may not** represent a waiver by the landlord of the right to terminate the lease and re-enter the premises. In *1012765 Ontario Inc. v. Regional Shopping Centres Limited* [42], the lease contained a provision which expressly stated that any acceptance of rent on the part of the landlord

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[40] *Big Valley Collieries Ltd. v. MacKinnon* (1915), 9 W.W.R. 4, 23 D.L.R. 62 (Alta. T.D.)

[41] (1920), 54 D.L.R. 331 (P.C.)

[42] Ont. Ct. (Gen. Div.), June 15, 1993 (unreported).

would not operate as a waiver. Citing this non-waiver provision, Rosenberg J. concluded that the landlord could re-enter the premises, despite the fact that the landlord knowingly accepted rent from the assignee/subtenant.

Unfortunately, the *1012765* judgement has not been considered by any subsequent court; therefore, it is impossible to provide a definitive answer with respect to the issue of effectiveness of a non-waiver clause. Counsel for the tenant, in *1012765*, advised that the non-waiver provision was not as expressly worded in *Paulson* as in *1012765*. Accordingly, considerable care must be taken in drafting a non-waiver provision in order to maximize the probability that such a provision would be held to be effective by a court if it were challenged.

SCHEDULE "A"

ARTICLE XIV

DEFAULT

Section 14.01 - Right to Re-enter

(a) An "Event of Default" occurs whenever:

(i) any Rent or Sales Taxes are not paid when due and payable and the non-payment continues for five (5) days after written notice to the Tenant;

(ii) any covenant or condition of this Lease to be observed or performed by the Tenant is breached (other than a breach specified below in Section 14.01(a)(iii)) and (A) the breach is not remedied within ten (10) days after written notice to the Tenant specifying particulars of the breach, or (B) if ten (10) days is not a reasonable time to remedy the breach, the Tenant has not commenced diligently to remedy the breach within such ten (10) day period or is not proceeding diligently to remedy the breach thereafter within a reasonable time; or

(iii) any of the following events occurs:

(1) a report, statement or certificate delivered by the Tenant pursuant to this Lease is false or misleading except for a misstatement that is the result of an inadvertent or unintentional error;

(2) the Tenant, or a Person carrying on business in a part of the Leased Premises, or an Indemnifier becomes bankrupt or insolvent or takes the benefit of any statute for bankrupt or insolvent debtors or makes any proposal, assignment or arrangement with its creditors;

(3) a receiver or a receiver and manager is appointed for all or a part of the property of the Tenant, or of another Person carrying on business in the Leased Premises, or of an Indemnifier;

(4) steps are taken or proceedings are instituted for the dissolution, winding up or other termination of the Tenant's or the Indemnifier's existence or the liquidation of their respective assets;

(5) the Tenant or the Indemnifier makes or attempts to make a bulk sale of any of its assets regardless of where they are situated (except for a bulk sale made to a Transferee when the Transfer is permitted under this Lease or has been consented to by the Landlord);

(6) property is sold, disposed of or removed from the Leased Premises so that there does not remain sufficient property on the Leased Premises available for distraint, free and

clear of any lien, charge or other encumbrance ranking ahead of the Landlord's right of distress, to satisfy the Rent due or accruing for at least twelve (12) months;

(7) the Leased Premises are vacant or unoccupied for five (5) consecutive days, or the Tenant abandons or attempts to abandon the Leased Premises;

(8) the Tenant effects or attempts to effect a Transfer that is not permitted by this Lease; or

(9) this Lease or any of the Tenant's assets on the Leased Premises are taken or seized under a writ of execution, an assignment, pledge, charge, debenture, or other security instrument.

(b) Upon the occurrence of an Event of Default, (i) the full amount of the current month's and the next three (3) months' instalments of Rent (calculated according to Section 14.01(c)), and Sales Taxes will become due and payable, and (ii) the Landlord may re-enter and re-possess the Leased Premises and on such a re-entry, this Lease and all of the Tenant's rights hereunder will terminate without liability on the part of the Landlord for loss or damage, and without prejudice to the Landlord's rights to recover arrears of Rent or Sales Taxes or damages for any previous breach by the Tenant of any covenant or condition of this Lease. On such a termination, (1) the Tenant will promptly (and in any case within ten (10) days after written notice requiring it to do so) remove all of its property from the Leased Premises, or (2) the Landlord may at any time remove all or part of the property from the Leased Premises and store it in a public warehouse or elsewhere at the cost of the Tenant. The Landlord will not be responsible for loss or damage to any of the

Tenant's property regardless of how the loss or damage is caused, and regardless of negligence. If the Tenant fails to remove its property as required by clause (1) above, or if it fails to pay the Landlord's costs of removal and storage within ten (10) days after written notice specifying those costs, the Tenant will be considered to have abandoned its property and the Landlord will be entitled to retain it or to sell or dispose of the Tenant's property for the Landlord's own benefit. Notwithstanding any such termination, the Landlord shall be entitled to recover damages from the Tenant including, but not limited to, (A) damages for loss of Rent and Sales Taxes suffered by reason of this Lease having been prematurely terminated; (B) the cost or recovering the Leased Premises; and (C) solicitor's fees on a solicitor and his client's basis.

(c) If the Landlord terminates this Lease for an Event of Default after the expiration of two (2) or more twelve (12) month Lease Years, the annual Rent for the purpose of calculating the Landlord's damages will be considered to be equal to the aggregate of (i) the annual Minimum Rent specified in this Lease; (ii) the average Percentage Rent that was payable for the two (2) preceding twelve (12) month Lease Years; and (iii) Additional Rent for the preceding twelve (12) month Lease Year. If the termination takes place before the expiration of two (2) twelve (12) month Lease Years, the annual Rent for the purpose of calculating the Landlord's damages will be considered to be equal to the aggregate of (1) the annual Minimum Rent specified in this Lease; (2) twelve (12) times the average monthly amount of Percentage Rent paid or payable based on Gross Revenue for each full month of the Term preceding the termination; and (3) twelve (12) times the average monthly amount of Additional Rent for each full month of the Term preceding the termination. If the whole of the Leased Premises is not open to the public for business on any day (a "Closed Day") that is a business day Gross Revenue for the Closed Day will be deemed to be equal to the average daily Gross Revenue for the last

week preceding the Closed Day throughout which the Leased Premises were open to the public for business.

Section 14.02 - Rejection of Tenant's Repudiation

If an Event of Default occurs the Landlord may, instead of terminating this Lease, insist on the performance of the covenants and conditions of this Lease and in that case may do both or either of the following: (a) levy distress for arrears of Rent; and (b) take legal proceedings against the Tenant for both or either of (i) payment of Rent and Sales Taxes as they become due; and (ii) performance of the covenants and conditions of this Lease; all without prejudice, however, to the Landlord's right to terminate this Lease at any time should the Event of Default continue unremedied.

Section 14.03 - Expenses

If legal proceedings are brought for recovery of possession of the Leased Premises, for the recovery of Rent, or because of an Event of Default by the Tenant, the Tenant will pay to the Landlord its expenses, including its solicitors' fees (on a solicitor and his client's basis).

Section 14.04 - Waiver of Exemption from Distress

Notwithstanding the Landlord and Tenant Act (Ontario) or any other applicable Act or legislation, none of the inventory, furniture, equipment or other property that is, or was at any time, owned by the Tenant is exempt from levy by distress for Rent.

Section 14.05 - Landlord May Cure the Tenant's Default

If the Tenant defaults in the payment of money that it is required under this Lease to pay to a third party, the Landlord may, after giving five (5) days notice in writing to the Tenant, pay all or part of the amount payable. If the Tenant commits a breach of a covenant or condition of this Lease (except for a default in the payment of Rent) the Landlord may, after giving reasonable notice (it being agreed that forty-eight (48) hours is a reasonable notice of default of Section 6.07), or, without notice in the case of an emergency, perform or cause to be performed all or part of what the Tenant failed to perform and may enter upon the Leased Premises and do those things that the Landlord considers necessary for that purpose. The Tenant will pay to the Landlord on demand, the Landlord's expenses incurred under this Section 14.05 plus an amount equal to fifteen percent (15%) of those expenses for the Landlord's overhead. The Landlord will have no liability to the Tenant for loss or damages resulting from its action or entry upon the Leased Premises.

Section 14.06 - Application of Money

The Landlord may apply money received from or due to the Tenant against money due and payable under this Lease.

Section 14.07 - Remedies Generally

The remedies under this Lease are cumulative. No remedy is exclusive or dependent upon any other remedy. Any one or more remedies may be exercised generally or in combination. The specifying or use of a remedy under this Lease does not limit rights to use other remedies available at law generally. Subject to Section 11.01(b)(iii), any breach by the Landlord under this Lease can be adequately compensated in damages and the Tenant agrees that its only

remedy to enforce its rights under this Lease is an action for damages.