

REASONABLE LIMITS ON THE DUTY TO MITIGATE

A recent decision from the Saskatchewan Court of Queen's Bench provides landlords with some guidance and clarity on the duty to mitigate damages following a breach of lease. In *M. Thompson Holdings Ltd. v. Haztech Fire and Safety Services*, 2016 SKQB 294, the court upheld the rule that landlords are responsible for making reasonable efforts to mitigate their damages. However, the court also emphasized that there must be reasonable limits placed on the mitigation efforts. It was determined that, in discharging its duty to mitigate, a landlord is not required to go above and beyond what a reasonable but conservative person would do in like circumstances.

The Facts

In February, 2013, the tenant signed a lease (the "**Lease**") with the landlord for commercial premises of about 10,000 square feet in Regina, Saskatchewan (the "**Premises**"). The Lease was for a term of over ten years, from June 1, 2013 to November 30, 2023 (the "**Term**").

On September 20, 2013, less than four months into the Term, the tenant informed the landlord that it intended to abandon the Premises, thereby breaching the Lease. In response, the landlord sent the tenant a formal notice of default, which the tenant failed to cure. On October 2, 2013, the landlord formally terminated the Lease and retook possession of the Premises.

The landlord commenced an action against the tenant seeking damages for breach of the Lease. The tenant did not dispute breaching the Lease, but it challenged the landlord's calculation of damages, alleging that the landlord did not take all reasonable steps to mitigate its loss. The landlord brought a motion for summary judgment on its claim.

The Mitigation Efforts

The day after the Lease was terminated; the landlord immediately began efforts to secure a new tenant for the Premises in order to mitigate its damages. The landlord took the following steps as part of its mitigation efforts:

- (a) the landlord instructed a very experienced and reputable leasing brokerage to re-list the Premises for lease immediately;

- (b) the brokerage prepared an updated listing brochure for the Premises and distributed it to all of its agents in the province, as well as all commercial brokers in the Regina area;
- (c) the availability of the Premises was advertised on the broker's national property listing website; and
- (d) "for lease" signs were placed in the windows of the property and the parking lot.

The landlord was able to secure a replacement tenant for about 50% of the Premises for a new ten-year term beginning on December 1, 2015. Early in 2016, the landlord leased an additional 18% of the Premises for a five-year term beginning on March 15, 2016 to June 30, 2021. The landlord was unable to secure any other new leases and about one-third of the Premises remained vacant.

The Landlord's Damages

Having secured replacements tenants for the Premises, the landlord divided its damages into three time frames:

- (a) amounts owing from the beginning of the Term to the date of the tenant's breach in the amount of \$6,666.17 (the "**Past Damages**");
- (b) unpaid basic and additional rent from the date of termination of the Lease to November 30, 2015, the date on which the first replacement tenant began to occupy the Premises in the amount of \$416, 991.62 (the "**Present Damages**"); and
- (c) future basic and additional rent owing from December 1, 2015 until the end of the Term in the amount of \$879,695.87 (the "**Future Damages**"). These damages were speculative and were based on the available space, by using 2015 base average amounts for municipal property tax, additional insurance costs, separately-metered utilities and operating costs. The landlord submitted that, as a result of its mitigation efforts, it was able to reduce its total loss of \$1,979,088.12 by over \$986,000. The landlord also applied a discount rate of 3% to its damages after mitigation to arrive at damages of \$879,695.87. The 3% discount represented the interest rate prescribed by

the Queen's Bench Rules as the applicable interest rate used in determining the capitalized value of an award with respect to future pecuniary damages.

The tenant did not dispute the landlord's use of the three breach periods. However, it challenged the amounts being claimed by the landlord.

The Tenant's Position

The tenant took the position that, despite its efforts, the landlord failed to take all reasonable measures to mitigate its loss. Specifically, the tenant claimed that the landlord's efforts fell short because the landlord refused to consider offers to sell the property and declined to lease the Premises to a restaurant chain which showed interest in the Premises. The tenant also argued that the landlord had an obligation to produce evidence substantiating its decision to lease, not sell, the Premises.

In support of its position, the tenant submitted evidence from a commercial realtor in Regina. The realtor deposed that a commercial property of similar size would be "a desirable property for leasing purposes in that it can be leased for a wide degree of purposes including but not limited to retail space, office space, food establishment and light duty warehouse".

In response, the landlord argued that, regardless of any offers to purchase the property, it had no interest in selling it. In regard to the offer to lease from the restaurant chain, the landlord submitted that the offer was declined because it would be difficult to break up the Premises to the size that they requested.

In regard to the Future Damages, the tenant argued that these damages were too speculative and could lead to double recovery in the event that the Premises were fully leased before the end of the Term. In support of its position, the tenant referred to the Ontario Superior Court of Justice decision in *Morguard Corp. v. 2063881 Ontario Inc.*, 2013 ONSC 7213 ("**Morguard**") to argue that the landlord was required to provide expert opinion evidence of the "present value of the unpaid future rent for the unexpired period of the lease less the actual rental value of the premises for that period plus reasonably foreseeable consequential losses".

The Court in *Morguard* found that the proper measure of damages for a terminated lease is the arrears of rent plus the present value of the loss of the future rent, which is the present value of

the unpaid rent for the unexpired period of the lease, less the actual rental value of the premises for that period. Damages could also include reasonably foreseeable consequential losses. *Morguard* confirmed that when there is no replacement tenant by the time of the default judgment, the landlord will have to provide evidence demonstrating the “actual rental value” of the premises and the amount of time it would take a landlord acting reasonably to find a new tenant.

The tenant relied on *Morguard* to argue that the landlord did not provide evidence of the market rental value of the Premises after it was vacated. The tenant also argued that the landlord failed to demonstrate how long it would take a landlord acting reasonably to find a tenant to pay the market rental value of the Premises.

The tenant also relied on the Ontario Court of Appeal decision of *Canadian Medical Laboratories Ltd. v. Stabile* (1997), 98 O.A.C. 3 (Ont. C.A.) (“*Stabile*”) to argue that the 3% discount applied by the landlord for the Future Damages was not the appropriate rate. In *Stabile*, the Court of Appeal rejected the use of the discount rate provided in the Ontario *Rules of Civil Procedure*.

The Decision

The court held that the landlord had sufficiently discharged its duty to mitigate and awarded the landlord the Past Damages and the Present Damages. In regard to the tenant’s position, the court held that the tenant did not adduce sufficient evidence to show that the landlord did not appropriately pursue the opportunity for the restaurant chain to lease the Premises. The court also disagreed that the landlord was obligated to lead evidence substantiating its decision to lease the Premises instead of selling it.

In arriving at its decision, the court cited the Alberta Court of Appeal in *Tangye v Calminton Investments Ltd.* (“*Tangye*”). The court in *Tangye* held that two rules apply to the duty to mitigate. First, the onus is on the debtor (here, the tenant) to prove failure to mitigate. Second, it must be determined whether a reasonable but conservative person in the landlord’s shoes, knowing the facts then known, might have made the same choice. It was emphasized that the test to show reasonable efforts to mitigate is “relatively lax”.

As such, the court held that the tenant did not discharge its onus pursuant to the *Tangye* decision. The court stated that: “[the tenant’s] onus to prove a failure to mitigate includes leading evidence that a reasonable person would not have made the same decision. It did not do so. Instead, [the tenant] argued that the fact the leased premises are not fully re-leased three years later is evidence of a failure to mitigate. With respect, the evidence before me does not allow me to reach that conclusion”.

In regard to the tenant’s position on the landlord’s refusal to sell the Premises or lease it to the restaurant chain, the court held:

- (a) the tenant’s evidence did not address the issue of whether the landlord should have pursued the opportunity to rent to the restaurant chain and there was no other evidence to support the conclusion that the landlord did not appropriately pursue the opportunity;
- (b) the landlord did not have an obligation to produce evidence to support its decision to lease, not sell, the Premises. The tenant’s onus to prove a failure to mitigate includes leading evidence that a reasonable person would not have made the same decision and the tenant did not lead any such evidence;
- (c) the landlord produced considerable evidence of its efforts to re-lease the Premises and it had a right to hold onto the Premises and continue its efforts to lease out the available space. As stated by the court in *Tangye*, if "a reasonable but conservative person in his shoes, knowing only the facts then known, might have made the same choice", there is no failure to mitigate; and
- (d) the tenant did not discharge its onus to show that the landlord made an unreasonable decision in refusing to sell the Premises. The tenant’s only evidence confirmed that "property is a desirable property for leasing purposes", which affirmed the landlord’s position. As such, there was no evidence before the court to allow it to conclude that a reasonable person would have made a different decision about selling the Premises.

The landlord was therefore granted judgment for the Past Damages and the Present Damages. However, in regard to the Future Damages, the court held that there was a triable issue in the calculation of damages involving the landlord’s continuing duty to mitigate, and the requirement

for evidence on the appropriate discount rate. Accordingly, the court did not grant summary judgment for the Future Damages, but ordered that the landlord was permitted to return to Court annually for an assessment of the Future Damages.