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## From Sublet To Regret

Every now and again, landlords must face the difficult decision of whether to allow a tenant to transfer its lease. Some leases will provide that the landlord may consider a number of factors when considering the transfer request. Other leases will simply provide that the landlord cannot withhold consent “unreasonably”. What does this mean?

Historically, the law tended to favour landlords. When the landlord unreasonably refused its consent, the tenant’s remedy was limited to asking the court to approve the transaction. The tenant could not terminate or sue for damages. Not surprisingly, some landlords abused this process by delaying a decision or arbitrarily refusing consent. By the time the tenant applied to the courts, it was often too late.

In response to this problem, in the early ‘80’s, the courts began to hold landlords accountable for damages that tenants suffered by reason of an unreasonable delay in responding to the tenant’s request to transfer. For instance, in *Cedar Valley Investments Inc. v. Port Moody (City)*, the court allowed the tenant to bring a lawsuit against the landlord when it unreasonably refused to grant consent to a subletting.

The law developed further in *Lebndorff Canadian Pension Properties Ltd. v. Davis Management Ltd.*, where the court held that a landlord’s unreasonable refusal to consent constituted a fundamental breach of the lease, entitling the tenant to unilaterally terminate its lease.

### Consequences of Delaying Response

A recent decision by the British Columbia Court of Appeal has taken the law a step further. Not only can a landlord’s unreasonable delay or refusal allow the tenant to terminate the lease; now it might also result in a complete discharge of the indemnifier of the lease.

In *Jens Hans Investments Co. Ltd. v. Bridger*, the tenant, Bridger, sought permission to sublet the second floor of its premises. Over a period of nine months, Bridger obtained offers from five potential subtenants and forwarded them to the landlord. The first two offers were rescinded when the landlord failed to respond; the following three offers were left open, but they were also ignored. The tenant finally got the landlord’s attention when it stopped payment on a rent cheque.

The first finding of the court was that the landlord’s persistent failure to reply to the offers amounted to a fundamental breach of the lease, as it was considered an unreasonable withholding of consent. This finding, though severe, was consistent with the ruling in *Lebndorff*.

The second finding, however, was somewhat more startling: not only was the tenant free to break the lease, but the indemnifier was entitled to a full discharge. The court held that the landlord’s inaction constituted a major variation of the risk assumed by the indemnifier such that it was no longer one that the indemnifier had contemplated. For *Jens Hans*, this meant that the landlord was not only prevented from suing the tenant for rent, but was also prevented from suing the indemnifier.

### Acting “Reasonably”

How should a landlord go about exercising its “reasonable” discretion in response to a request for a consent to a transfer?

The case of *Zellers Inc. v. Brad-Jay Investments Ltd.* provides some useful guidance. In *Zellers*, the landlord withheld consent to a sublet to Close-Out King, a large format retail store selling clearance and liquidated merchandise. After receiving the request, the landlord embarked on its own due diligence of the proposed subtenant. It consulted with a variety of professionals in the industry and concluded that the subtenant would not be suitable for the mix of the mall, its business

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would be detrimental to the mall's image and would cannibalize existing sales of other merchants. The tenant retained its own consultants and experts who concluded that the proposed tenant would be a benefit to the mall and increase business.

The court held that the landlord's consent was withheld on a reasonable basis. It was not the function of the court to decide whether the experts were right or wrong. Rather, the court was limited to ensuring that the landlord acted reasonably and in good faith in exercising its discretion when deciding whether or not to consent. In the circumstances, since the landlord had consulted two real estate consultants, two lawyers, and its property manager, the court found the consent to have been reasonably withheld.

### Is One Consent Good For All Time?

It might seem trite to note that in order for consent to be "unreasonably withheld", the tenant must in fact request consent. But confusion arises in situations where a tenant has been granted permission to sublet to the same tenant on one or even two occasions. Would a tenant be justified in assuming the landlord also consents to the third sublet?

This is precisely what transpired in *1497777 Ontario Inc. v. Leon's Furniture Ltd.* On two separate occasions, Leon's had obtained the landlord's consent to a subletting of its premises to a hair salon – one in 1992 and another in 1997. It renewed its lease in 2000 and entered into an additional sublease, but on this occasion failed to obtain the landlord's consent.

The landlord subsequently refused consent, and applied to the court for a termination of the lease on the basis that the tenant failed to obtain consent.

On appeal, the court held that the landlord was entitled to terminate the lease because the tenant had failed to obtain the required consent. In other words, a fresh consent was required for each subsequent sublease. The judge went on, however, to hold that the tenant could make an application for relief from forfeiture. (This application has not yet been heard.)

Upon receiving a request for consent to a transfer, the landlord must respond reasonably and in good faith. First, the landlord may not unreasonably delay its response. In formulating its response, the landlord may generally consider the proposed tenant's reputation, creditworthiness and suitability for the complex. The lease may expand or limit the factors that the landlord may take into account. In assessing the proposed tenant, the landlord may turn to its consultants and advisors before making its decision. Provided that the landlord has exercised its discretion based on the relevant factors and in good faith and not for ulterior motives or a collateral purpose, the courts will not interfere. It is not a question of the landlord being right or wrong – instead, the question is whether the landlord acted reasonably and in good faith.

Where the landlord acts unreasonably or in bad faith, then the courts, as demonstrated by the *Davis Management* and *Jens Hans* cases, have shown a willingness to relieve the innocent party of its obligations under its lease and now, even indemnity agreements.

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