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PANDEMIC RESTRICTIONS ≠ RADICAL ALTERATION

During the pandemic, landlords and tenants questioned whether government restrictions on business relieved tenants of the obligation to pay rent. In our April 6, 2020 News ReLease, we encouraged readers to study the details of any *force majeure* clause, and we suggested that there was not much legal authority in case law to support a claim that leases had been frustrated to the point of allowing tenants to be relieved of their obligations. The recent decision of *Braebury Development Corporation v. Gap (Canada) Inc.* confirms what we posited in April 2020: that if a lease contains a *force majeure* clause, tenants are unlikely to succeed with an attempt to claim that the doctrine of frustration applies.

A Refresher on the Doctrine of Frustration

The doctrine of frustration applies when an event arises (1) that was not foreseeable at the time of formation of contract and (2) for which the parties made no provision in the contract. The threshold test, of whether the event renders performance of the contract "a thing radically different from that which was undertaken by the contract", must be met for a claim of frustration to succeed. When it succeeds, the contract itself (and all obligations under it), simply *ceases* as of the occurrence of the event.

Since the doctrine requires that the supervening event had not been contemplated at the time of contract, inclusion of a risk allocation mechanism (such as a *force majeure* clause), will interfere with the doctrine. A *force majeure* clause is a contractual provision stating that certain contractual obligations are suspended on certain triggering events. (Typically, in a lease, a *force majeure* clause will go on to state that in any event, the obligation to pay rent and other sums will not be suspended.)

The doctrine of frustration has rarely been applied in the case of a leasehold interest. In *National Carriers Ltd v. Panalpina (Northern) Ltd.*, England's House of Lords ruled that a lease was **not** frustrated when the only access road to the premises was destroyed for 20 months of a 10-year term. It held that a temporary interruption did not amount to a frustrating event.

In the Hong Kong decision *Li Ching Wing v. Xuan Yi Xong*, the Court rejected the tenant's claim that the lease was frustrated due to the 10-day SARS isolation order, because the isolation order did not "significantly change the nature of the outstanding contractual rights and obligations" under the lease.

While all of this was outlined in our April 2020 News ReLease, we were still curious as to whether a worldwide pandemic might receive different treatment. After all, it was "unprecedented"!

The Decision in *Braebury*

Gap had operated a store in downtown Kingston since 1994. In response to the Ontario government declaration of a provincial state of emergency, the Tenant closed the store in March, 2020. It did not pay rent for April or May, 2020, and made only partial payments from June until September, 2020, when it vacated the premises and stopped all rent payments.

The Landlord issued a claim for arrears of rent totalling $208,211.85. The Tenant refused to pay, contending that the lease was frustrated by the COVID-19 pandemic and that the Tenant was therefore relieved of its rent obligation. The Landlord argued that the lease's *force*

majeure clause, pursuant to which the Tenant was required to continue to pay rent despite a *force majeure* event, forestalled the application of the doctrine of frustration and that the Tenant was required to pay all rent.

The Ontario Superior Court agreed with the Landlord, holding that the parties had turned their minds to how events beyond their control would be handled, by way of the *force majeure* clause. The Court found that the government's closure order for all non-essential businesses triggered the *force majeure* clause, which stipulated that in any *force majeure* event, the Tenant was still obliged to pay rent.

No "Radical Alteration"

Although the Court in *Braebury* held that the *force majeure* clause served to maintain the rent obligation, it nevertheless reviewed the doctrine of frustration. The Tenant argued that because the government's declaration prevented it from operating its business, the purpose of the lease had been frustrated.

The Court disagreed. It held that in order for the doctrine of frustration to relieve the Tenant of its contractual obligations, the COVID-19 pandemic restrictions must have "radically altered the terms of the lease".

Since the lease did not contain an operating covenant and stated that the Tenant had "no obligation to operate any business nor conduct any business…either initially or any time during the terms of this lease…" the shut down order had **not** radically altered the terms of the lease. This is a twist – when negotiating leases, many tenants fight for the right not to operate and consider it a big point to win. Alas, in this instance, it apparently did not help the Tenant that it had no contractual obligation to operate.

The Court in *Braebury*, consistent with a long line of jurisprudence, rejected the application of the doctrine of frustration in the case of a leasehold interest, because even a burden as novel and extreme as the COVID-19 pandemic did not radically alter the lease terms - which included the *force majeure* provision. It found that the parties had pre-determined who would bear the economic burden of *force majeure* events. It granted judgment to the Landlord for the full arrears owing.

Braebury underscores just how reluctant a court will be to look outside the wording of the lease, and how rarely the doctrine of frustration will be applicable to a leasehold interest.

MARY ANN BADON
416-598-7056
mbadon@dv-law.com

FRANCINE BAKER-SIGAL
416-597-8755
francine@dv-law.com

CANDACE COOPER
416-597-8578
ccooper@dv-law.com

HEATHER CROSS
416-591-3046
hcross@dv-law.com

DENNIS DAOUST
416-597-9339
ddaoust@dv-law.com

ALLISON FEHRMAN
416-304-9070
afehrman@dv-law.com

GASPER GALATI
416-598-7050
ggalati@dv-law.com

PAUL HANCOCK
41-597-6824
phancock@dv-law.com

WOLFGANG KAUFMANN
416-597-3952
wolfgang@dv-law.com

LYNN LARMAN
416-598-7058
llarman@dv-law.com

MELISSA M. MCBAIN
416-598-7038
mmcbain@dv-law.com

PORTIA PANG
416-597-9384
ppang@dv-law.com

JAMIE PAQUIN
416-598-7059
jpaquin@dv-law.com

BRIAN PARKER
416-591-3036
bparker@dv-law.com

DINA PEAT
416-598-7055
dpeat@dv-law.com

MANEET SADHRA
416-479-4357
msadhra@dv-law.com

JACK SARAIVA
416-597-1536
jsaraiva@dv-law.com

CHRISTINE SHAHVERDIAN
416-598-7049
cshahverdian@dv-law.com

LUCIA TEDESCO
416-597-8668
ltedesco@dv-law.com

NATALIE VUKOVICH
416-597-8911
nvukovich@dv-law.com

PHILLIP WALLNER
416-597-0830
pwallner@dv-law.com

DEBORAH WATKINS
416-598-7042
dwatkins@dv-law.com