

# Commercial Leasing Bulletin:

## Lessons for Landlords: Avoiding the Doctrine of Spent Breach

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By: Benji Wiseman - Minden Gross LLP Commercial Leasing Group

In most commercial leases, a tenant's option to extend or renew the lease is generally subject to the tenant's satisfaction of a common set of conditions. At a minimum, landlords typically want to keep tenants with a history of default from having the right to extend the lease. A recent case provides a valuable lesson for landlords that think this can be achieved by a catch-all condition stating the tenant's rights are conditional on there not having been a tenant default at any time during the term of the lease.

### The H.A.S. decision

The *H.A.S. Novelties Limited v. 1508269 Ontario Limited* ("H.A.S.") decision shows that courts are willing to apply the doctrine of spent breach to allow tenants with a history of defaulting to extend a lease. This in spite of language providing that their extension rights are conditional upon the tenant not having defaulted at any time during the term.

As a result of the pandemic, the tenant was in significant rental arrears over several months during the final year of the initial lease term, including the time it was due to deliver notice to the landlord exercising its extension option. The tenant provided such notice, and the landlord refused on the basis that the lease provided that the option was conditional on the tenant not having been in default **at any time** during the lease. Before the term ended, the tenant satisfied all rental arrears, and then sought a declaration from the court that it was entitled to the extension. The court sided with the tenant, applying the doctrine of spent breach.

### The doctrine of spent breach

The doctrine of spent breach, as applied by the court, provides that "an historical breach of a lease covenant, once remedied, will not entitle a landlord to refuse an otherwise valid option to renew the lease." In other words, because the tenant had cured their default before the term expired, the tenant was entitled to exercise its extension option. The rationale behind the doctrine of spent breach is that it is almost impossible for a tenant to complete a lease term without any breach whatsoever. Therefore, the court argues, it is unfair to apply an essentially impossible condition on the tenant. This appears to be a relatively surprising decision, given the nature of the tenant's breach. While it may not be fair to nullify an extension option in light of any minor breach that is

subsequently cured, in this case, the breach was significant. As a result, the application of the doctrine of spent breach in *H.A.S.* suggests that it may be applied to any default cured prior to the expiry of the term.

## Avoiding the doctrine of spent breach

In the wake of *H.A.S.*, landlords should consider updating their extension option language to ensure that the tenant's rights are actually limited by any historical default. One way to avoid the application of the doctrine of spent breach would be to include language explicitly opting-out of it. Alternatively, landlords can potentially avoid the doctrine of spent breach by making the tenant's extension option conditional on the tenant not having a history of repeated or persistent default, with explicit reference to a number of defaults over the course of the term or over a specific period of the term (e.g., in any year of the lease). The *H.A.S.* decision differs from the one explored in *Cardillo Entertainment Corp. v. PCM Sheridan Inc.*, where the tenant's extension rights were conditional on the tenant not having "material or chronic (three times or more) default." The doctrine of spent breach did not apply in that case as it did not impose the impossible standard of expecting perfect compliance.

## Conclusion

The *H.A.S.* decision suggests that the doctrine of spent breach will permit tenants to extend their lease regardless of the nature of the breach in question. However, this could easily be avoided by drafting a more precise condition that sets a more attainable standard for the tenant.

We will continue to provide updates on commercial leasing topics of interest. If you have any questions or would like to obtain legal advice on any leasing issues or litigation, please contact any lawyer in our Commercial Leasing Group.

## Commercial Leasing Group

### **Stephen Posen**

Chair, Commercial Leasing Group  
e: sposen@mindengross.com  
p: (416) 369-4103

### **Ian Cantor**

Partner, Litigation Group  
e: icantor@mindengross.com  
p: (416) 369-4314

### **Christina Kobi**

Partner, Commercial Leasing Group  
e: ckobi@mindengross.com  
p: (416) 369-4154

### **Catherine Francis**

Partner, Litigation Group  
e: cfrancis@mindengross.com  
p: (416) 369-4137

### **Michael Horowitz**

Partner, Commercial Leasing Group  
e: mhorowitz@mindengross.com  
p: (416) 369-4121

### **Boris Zayachkowski**

Partner, Commercial Leasing Group  
e: bzayachkowski@mindengross.com  
p: (416) 369-4117

**Benjamin Radcliffe**

Partner, Commercial Leasing Group  
e: bradcliffe@mindengross.com  
p: (416) 369-4112

**Steven Birken**

Associate, Commercial Leasing Group  
e: sbirken@mindengross.com  
p: (416) 369-4129

**Alyssa Girardi**

Associate, Commercial Leasing Group  
e: agirardi@mindengross.com  
p: (416) 369-4104

**Melodie Eng**

Partner, Commercial Leasing Group  
e: meng@mindengross.com  
p: (416) 369-4161

**Leonidas Mylonopoulos**

Associate, Commercial Leasing Group  
e: lmylonopoulos@mindengross.com  
p: (416) 369-4324

**Benji Wiseman**

Associate, Commercial Leasing Group  
e: bwiseman@mindengross.com  
p: (416) 369-4114

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