

Commercial Leasing Bulletin:

LESSONS LEARNED: The Ontario Court of Appeal Dishes Out Important Lessons for Landlords and Tenants

September 15, 2021

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Subway Restaurants of Canada Ltd. v. BMO Life Assurance Co.

On May 26, 2021, the Ontario Court of Appeal released its decision in [Subway Franchise Restaurants of Canada Ltd. v. BMO Life Assurance Co.](#), affirming the decision of the Superior Court. In this case, the tenant's mistake in recording the correct start and end date of the lease term led the tenant to improperly exercise its renewal option. Despite the tenant having made several attempts over the duration of the term to confirm the correct dates, the court held that the tenant was responsible for its failure to properly abide by the lease.

The case before the Court of Appeal hinged on the landlord's duty of good faith in the performance of the lease contract in circumstances of tenant misapprehension. This decision provides insight into the duty of good faith owed by parties to a lease, and also serves as a reminder to tenants of the importance of codifying key dates not explicitly set out in the lease and carefully reviewing an estoppel certificate before signing.

The Facts

On April 25, 2008, Subway Franchise Restaurants of Canada Ltd. (the "Tenant"), on behalf of one of its franchisees, entered into a lease with AIG Life Insurance Company of Canada (the "Original Landlord") for an initial term of 10 years with two five year renewal options.

As is the case with many leases requiring tenant build-outs, the lease as written did not have a specific start or end date but instead was subject to a fixturing period. The option to renew clause stated that the tenant must exercise its first option to renew by written notice made not less than nine months and not more than 12 months prior to the expiry of the initial term.

The Tenant began occupying the premises and commenced its work without any written notice from either party confirming the start of the fixturing period or the commencement date of the term. Instead, the Tenant determined, erroneously, that the initial term had begun (and therefore would expire) three months earlier than was determined by the Original Landlord.

Less than a year into the initial lease term, the Original Landlord was acquired by, and amalgamated with, BMO Life Assurance Co. (the “Landlord”). At this time the Tenant signed an estoppel certificate provided by the Landlord, which included the commencement and expiry dates as determined by the Original Landlord. The Tenant signed the estoppel without realizing that it differed from their interpretation of the term of the lease.

On several occasions in the years leading up to the expiry of the initial term, the Tenant wrote letters to the Landlord asking, amongst other things, to confirm the expiry date of the term. The Landlord confirmed receipt and review of such letters; however, they never responded. Eventually, the Tenant formally exercised its renewal in what it believed to be the window of time for such notice pursuant to the lease. Unfortunately, it was more than 12 months from the expiry of the term as stated in the estoppel certificate, so the Tenant failed to properly exercise its renewal.

The Trial and Appeal

At trial, the Tenant sought relief from forfeiture on the grounds that the Landlord ignored their requests to confirm the correct expiry date of the term and seemingly allowed the Tenant to improperly exercise their renewal option, meaning that the Landlord had failed to act in good faith in the performance of the lease contract. The Superior Court sided with the Landlord, stating: “the onus is on the tenant seeking relief from forfeiture to, at the very least, make a diligent effort to comply with the Lease’s terms.” As the Tenant had signed the estoppel certificate, the court determined that they would have uncovered the true expiry date of the term had they made a diligent effort to comply with the lease. On the issue of good faith, the Superior Court found “the duty of good faith is designed to ensure that the contract terms are performed in the spirit and substance of each party’s rights and obligations...It is not, however, designed to transform or modify those rights and obligations.”

In considering the Landlord’s duty of good faith, the Superior Court followed a decision that was subsequently overturned by the Supreme Court of Canada, providing the Tenant with grounds for appeal. The Court of Appeal unanimously dismissed the appeal and provided further insight on the evolution of the duty of good faith in contract following the Supreme Court’s recent decision in C.M. Callow Inc. v. Zollinger. The Court of Appeal found that for a contracting party to breach their duty of good faith, they must actively deceive the injured party. The decision reads, “In the absence of the defendant’s false representations, the failure to disclose a material fact, without more, would not be contrary to the standard [of acting in good faith].”

Key Takeaways

This case highlights the significance of properly tracking deadlines pursuant to a lease, especially given how common it is for new leases to commence based on the expiry of a fixturing period rather than a clearly defined date. Neither court doubted that the Tenant genuinely believed that it was properly exercising its option to renew; however, they still failed to exercise their renewal pursuant to the lease. Where a lease is being negotiated with a start date subject to a fixturing



period, tenants should ensure that the lease accounts for a notice to be prepared and signed by all parties on or before the commencement date clearly setting out the ultimate start and end dates. Furthermore, this decision demonstrates that renewal and extension options need to be exercised in strict accordance with the terms of the lease. Providing notice too early rather than too late, can be just as costly to the tenant regardless of whether the landlord is prejudiced by such early receipt.

This decision also demonstrates that estoppel certificates matter! In the trial decision, Morgan J states “The [Tenant] signed an Estoppel Certificate representing to the [Landlord] when the term of the Lease ends; the very point of the Certificate is that the signing party is estopped from asserting anything to the contrary.” In this case, the estoppel certificate was the only document where both parties confirmed the start and end date, which caused the courts to determine that the Landlord’s recorded dates were correct. Additionally, the failure to consult the estoppel certificate was evidence that the Tenant failed to act diligently to ensure it properly exercised its renewal notice.

It is essential for tenants to properly review the estoppel certificate before signing it, and not to sign anything if there is information that appears to be incorrect. In certain circumstances, courts have given difference to substantive terms contained in estoppel certificates contrary to the provisions of a lease. Signing an estoppel certificate demonstrates that you are both aware and in agreement with all of the information contained therein.

For landlords and tenants, the Court of Appeal’s decision sets a shockingly high bar for the breach of the landlord’s duty to perform the lease in good faith. The Landlord in this case was found not to have breached the duty of good faith despite their failure to respond to several requests to confirm the correct expiration date. A landlord that does not deceive its tenant, or in some way actively contribute to a tenant’s failure to properly interpret the terms of a lease, does not have a responsibility to correct such failure.

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](#).



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