LEGAL ALERT

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Current Legal Developments Critical to Corporate Management

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If we desire respect for the law, we must first make the law respectable.

~ Louis D. Brandeis (1856 – 1941)

COMMERCIAL PROPERTY AND LEASES

Equitable remedies available in commercial real estate transactions

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The Ontario Court of Appeal has confirmed that equitable remedies such as specific performance and permanent injunctions are available to enforce commercial real estate deals.

Two recent Ontario Court of Appeal decisions clarify the availability of equitable remedies to specifically enforce commercial real estate bargains in both sale transactions and leases, confirming these remedies are alive and well. The Supreme Court of Canada has recently denied leave to appeal in both cases.

Commercial lease

In *1465152 Ontario Ltd. v. Amexon Development Inc.*, a holdout commercial tenant (a law firm) in good standing in a multi-tenant building obtained a permanent injunction against the landlord, tantamount to an award of specific performance, to protect its lease. The landlord wished to demolish and redevelop the property and relocate the tenant into similar premises in a neighbouring building with compensation for the move.

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WHITE COLLAR CRIME

Knowledge of prior dishonesty can affect coverage for later fraud

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Crime insurance coverage can be affected by an employer's prior knowledge of employee dishonesty.

Victims of employee fraud regularly turn to crime insurance coverage or fidelity bonds as the main source of recovery for their losses. But such coverage often terminates with respect to specific employees as soon as the insured employer becomes aware of fraudulent or dishonest acts by that employee.

Essentially, "prior knowledge" clauses provide that once an employer knows an employee is crooked, the employer should bear the risk of that employee causing future losses. If companies want the full protection of their crime coverage, they should never be dismissive of *any* employee

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The lease did not have a demolition clause. After attempting (without success) to negotiate a satisfactory relocation agreement, the landlord served the holdout tenant with a Notice to Vacate in six months. The Notice indicated that after the six-month period, the landlord would turn off all services to the building.

Evergreen *decision*

The Ontario Court of Appeal rejected the landlord's attempt to rely on the British Columbia Court of Appeal's ("BCCA") decision in *Evergreen Building Ltd. v. IBI Leaseholds Ltd.* ("*Evergreen*"). On very similar facts, the BCCA held that a tenant was not necessarily entitled to injunctive relief to protect its leasehold interest.

According to the BCCA, before determining the appropriate remedy, the court needs to consider the equities between the parties, including any factors relating to the "uniqueness" of the leased property, as well as the relative hardship (if any) of holding the landlord to the strict terms of the lease.

The BCCA held that the tenant is not entitled to a permanent injunction simply because the lease is in good standing and the landlord is attempting to repossess the premises when it has no right to do so. The *Evergreen* decision has been strongly criticized by many commentators.

Exclusion clause

The Ontario Court of Appeal also rejected the landlord's reliance on an exclusion clause in the lease limiting the tenant's remedies to damages, recognizing that

> a commercially unreasonable interpretation of [the exclusion clause] would result if the Landlord could act without lawful authority to bring the Lease to an end and re-occupy the premises, and then rely on the disclaimed Lease to prevent the Tenant from restraining the Landlord's unlawful conduct.

The Ontario Court of Appeal held that

> much clearer language would be required in order to restrict the remedies available against the Landlord when it acted arbitrarily and without any basis in the rights conferred on it under the Lease.

The absence of a demolition clause in the lease was an important factor in the interpretation of the exclusion clause in the context of the entire lease.

Injunction

Finally, the Ontario Court of Appeal rejected the landlord's arguments that the tenant was seeking an injunction for an improper purpose — namely, to enhance its bargaining position — and the remedy was disproportionate as it was unreasonable to permit the tenant to continue to occupy premises which amounted to less than three percent of the building rental area when all other tenants had vacated.

The court noted that there had been no finding of improper purpose on the part of the tenant, and the rule favouring injunctions is strongest where there is a direct interference with the plaintiff's property constituting a trespass:

> Such [injunctive] orders may be said to vindicate the plaintiff's right to exploit the property for whatever it is worth to the defendant and prevent the defendant from circumventing the bargaining process.

Design-build transaction

Since the Supreme Court of Canada's decision in *Semelhago v. Paramadevan* almost two decades ago, specific performance isn't automatically available as the default remedy for

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breach of contracts for the sale of land. With reference to vendor claims for specific performance, damages can often address vendors' claims because there is nothing inherently unique about the sale price.

In *Matthew Brady Self Storage Corporation v. InStorage Limited Partnership* ("*Matthew Brady*"), the Ontario Court of Appeal granted a vendor specific performance. The court also clarified that where vendors seek this remedy, the focus should be on the transaction as a whole and whether there is uniqueness (or a special character) to the circumstances *of the transaction*. The subject-matter of the contract should be viewed more broadly.

Specific performance criteria

The court explained that in vendor specific performance claims, the issue does not depend on whether *the land* is unique:

> The special character of the land may remain a factor for consideration but the key factors, looking at the contract broadly, are (i) whether on the facts as a whole, damages will afford the vendor an adequate and complete remedy or whether a money award will be sufficient to purchase substitute performance; (ii) whether the vendor has established some fair, real and substantial justification for the granting of specific performance; and, (iii) whether the equities as between the parties favour the granting of specific performance.

Grant of equitable remedy

The Court of Appeal upheld the decision to grant specific performance for several reasons:

- The defendant was always intended to be the sole owner of the property.
- The agreement was entered into so that the defendant would not have to outlay the necessary capital.
- The plaintiff renovated the subject premises to the defendant's specifications and design criteria.
- But for the defendant's commitment to owning the property, the plaintiff would not have acquired it and done the retrofit.
- The defendant had, admittedly, done a poor job in managing the property — something that would affect its value and impede a ready sale.
- The defendant purposely resiled from the contract, in the face of advice of both Ontario and U.S. counsel.

REFERENCES: *1465152 Ontario Ltd. v. Amexon Development Inc.*, 2015 ONCA 86, 2015 CarswellOnt 1317, 381 D.L.R. (4th) 66, 50 R.P.R. (5th) 167, 330 O.A.C. 344 (Ont. C.A.), leave to appeal refused 2015 CarswellOnt 10072, 2015 CarswellOnt 10073 (S.C.C.), note 1 at para. 16, para 27, quoting Robert J Sharpe, *Injunctions and Specific Performance*, loose-leaf, (Toronto: Canada Law Book, 2014), at para 4.590 (leave to appeal to the Supreme Court of Canada denied July 2, 2015); *Evergreen Building Ltd. v. IBI Leaseholds Ltd.* (2005), 2005 BCCA 583, 2005 CarswellBC 2848 (B.C. C.A.), additional reasons 2006 BCCA 185, 2006 CarswellBC 909, 53 R.P.R. (4th) 68 (B.C. C.A.), leave to appeal allowed 2006 CarswellBC 1600, 2006 CarswellBC 1601 (S.C.C.); *Matthew Brady Self Storage Corp. v. InStorage Limited Partnership*, 2014 ONCA 858, 2014 CarswellOnt 16809 (Ont. C.A.) at paras. 39-41, leave to appeal refused 2015 CarswellOnt 9611, 2015 CarswellOnt 9612 (S.C.C.); *Semelhago v. Paramadevan*, 1996 CarswellOnt 2737, 1996 CarswellOnt 2738, [1996] 2 S.C.R. 415 S.C.C.) at para. 22.

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fraud or dishonesty, no matter how minor.

If the company ignores an employee's minor transgression, then later goes on to claim a loss for a larger fraud caused by that same employee, coverage may be denied.

Seminal authority

In the longstanding seminal authority on the interpretation of prior knowledge clauses, *Grindrod and District Credit Union v. Cumis Insurance Society Inc.* ("*Grindrod*"), both the British Columbia Supreme Court and the British Columbia Court of Appeal interpreted a prior knowledge clause in a credit union's fidelity bond.

The bond provided that it was deemed to be terminated with respect to subsequent losses caused by any employee as soon as the insured became aware of any fraudulent or dishonest act on the part of such employee. The evidence in Grindrod was clear.

The manager of the credit union had falsified entries in the employer's records to cover up large overdraft loans, and had lied to the board of directors about the extent of the overdrafts. The credit union suffered a loss as a result of the manager's fraud.

Prior knowledge clause

The main issue was whether the credit union, upon initially discovering the overdrafts themselves a year

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