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LOTIATION IN CANADA

By Jacob Cowles, SIOR

While Canadian and American commercial leases share much in common, there are subtle differences that are important to consider when working with clients who have real estate interests in Canada. In this article, we will cover Canada's civil and common law systems and how it impacts Canadian leases.

Canada has a bijural legal system, meaning that two unique systems co-exist. This tradition originates from 17th and 18th century conflicts between France and Great Britain in Canada during colonization. As a result, Quebec is a civil law jurisdiction, while the rest of Canada is governed by common law. Common law is a body of law where rules are based on precedent and custom. Conversely, civil law contains a comprehensive statement of rules, known as the Civil Code of Quebec, that are intended to govern the relationship between parties.

While commercial leasing standards have much in common from province to province, one needs to be mindful that Canada's bijural system means that there are certain differences that must

be kept in mind when doing business in the various provinces.

One of the major differences in commercial leasing in Quebec and in the rest of Canada is in how a lease is defined. The Civil Code of Quebec defines a lease as a "contract undertaken by one party to provide another with the enjoyment of moveable or immoveable property for either a fixed or indeterminate period, in return for consideration." This differs from common law jurisdictions where a lease is considered a contractual agreement by which one party conveys an estate in property to another in exchange for something of value.

In negotiating commercial leases in Canada, among the differences to keep in mind are the following issues:

Good Faith

While good faith is part of the Uniform Commercial Code (UCC) in the United States, it is not required in all states and may be waived in certain commercial contracts. According to the UCC, good faith is defined as "honest in fact and the observance of reasonable commercial standards of fair dealing." In contrast, the duty of good faith—although recognized throughout Canada either through legislation or pursuant to the landmark Supreme Court of Canada decision in *Bhasin v. Hrynew* (2014)—differs depending on whether we are looking at the civil law interpretation of this duty or the common law application.

In Quebec, good faith is explicitly defined by the Civil Code of Quebec as meaning that all parties to a contract "shall conduct themselves in good faith both at the time the obligation arises and at the time [a contract] is performed or extinguished." This generally means that the behavior of those engaged in the contract will not be abusive or deceptive in a way that would compel one party to terminate the contract. This extends not only to the contract itself, but to formation

of the contract and the performance of the contract. Good faith therefore serves as a standard of conduct between the parties throughout their relationship that includes cooperation and loyalty in order to allow all parties to benefit from the contract.

In the rest of Canada, the duty of good faith applies to all contracts and, according to Justice Cromwell of *Bhasin v. Hrynew* (2014), "means simply that parties must not lie or otherwise knowingly mislead each other about matters directly linked to the performance of the contract." Unlike in Quebec, this does not require a duty of loyalty nor does it require that a party put the interests of its contractual partner ahead of its own. As is the case in the United States, the duty of good faith only applies to the performance of the contract itself and not to the pre-contract or negotiation of said contract.

Legal Restrictions Limiting the Term of a Lease

The term of a lease in Quebec may not exceed 100 years and if any lease exceeds such a term, it must be reduced to 100 years. Furthermore, leases in Quebec with a term of more than 40 years—including renewals—are subject to the payment of transfer duties. The "Act respecting duties on transfers of immovables" (the Act)—Quebec's regime for land transfer duties—considers a lease with a term exceeding 40 years as a transfer triggering the imposition of land transfer duties. Similarly, other Canadian provinces have analogous legislation. Another variation on term limits is in Ontario, where the "Planning Act" prohibits the entering into a transaction or contract that grants someone the use of or right to land for a period that is longer than 21 years, including renewal periods, unless the transaction falls within the exemptions provided under the Act—otherwise Planning Act approval is required. The purpose of this limitation is to allow for municipal control over urban development.

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Assignment

Under common law, no consent is required, however standard commercial practice is that the lease overrules the common law in this instance. In most cases the lease will either explicitly prohibit assignments and transfers or will permit it only upon landlord's prior consent. There is nothing under common law to prevent this nor is there anything requiring the landlord to act reasonably.

The Civil Code of Quebec provides that a tenant may assign its lease and that the tenant must give notice to the landlord as well as obtain the landlord's consent. Furthermore, the law provides that the landlord may not refuse its consent without a serious reason. However, these provisions are not of public order. As such, in most commercial leases the landlord's consent must be obtained and a list of circumstances pursuant to which landlord's consent can be refused will be included in the lease.

Although a lease assignment has the effect of terminating the legal relationship between the original tenant and the landlord, the former may still be liable under contract to the landlord, even if it is no longer occupying the space. It is important to note that in Quebec, the law provides that the assignment of a lease releases the tenant of its obligations, however once again this is not of public order. The landlord may contract out of this obligation by stipulating in the lease that the original tenant will remain liable along with the new tenant for the fulfilment of all the obligations under the lease. Understanding the difference between Quebec and the rest of Canada when it comes to assigning the lease is crucial, as it directly defines which party is legally obligated by the conditions of the lease.

Registration of Lease

This is an important element that should be examined in every jurisdiction. The value of registering a lease is to protect the tenant's rights from third parties. In the event a new purchaser acquires the premises—or a hypothecary creditor exercising its rights—the third party will be obligated to respect the lease for the entire term. In Quebec, any lease may be registered at the Land Registry by way of a notice and must only contain the information prescribed in the Civil Code of Quebec. The ability to register a lease is available in other provinces as well, however in certain cases—such as British Columbia—registering a lease requires landlord's consent and the execution by the landlord of a short form of the lease. In addition, in certain circumstances a survey may be required in order to register the lease which makes the process lengthy and costly.

As noted above, there are subtle differences that need to be considered when working with clients who have real estate interests in Canada, though these are just a few of the many things to keep in mind. ▽

MEET THE AUTHOR

Jacob Cowles, SIOR, is managing partner at Landmark Advisory Services in Montreal Quebec. Contact him at jcowles@landmarkcre.ca.