

DOCTRINE OF SPENT BREACH CAN OVERRIDE LEASE RENEWAL TERMS

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In a recent Ontario case, a Tenant's breach of a commercial lease did not prevent it from exercising an option to renew despite an express lease term to the contrary.

Tenant Fails to Pay Rent and Landlord Disputes Lease Renewal

In *H.A.S. Novelties Limited v. 1508269 Ontario Limited*,^[1] a Landlord and Tenant entered into a partial rent deferral agreement at the outset of the Covid-19 pandemic. A few weeks later, the federal government introduced the Canada Emergency Commercial Rent Assistance (“**CECRA**”) program, which would have required the Tenant to pay only one quarter of the rent during the time it applied. The Tenant asked the Landlord to apply for CECRA. The Landlord initially agreed but later suggested that it may not apply after all.

During the period of uncertainty about the CECRA application, the Tenant failed to pay the full amount of rent owing under the rent deferral agreement. It paid a lower amount on the understanding that the Landlord would apply for the CECRA program. After the Landlord made demands for payment, the Tenant paid all outstanding arrears (except for rent owing for one month).

The Tenant later advised that it intended to exercise its option to renew the lease. However, the Landlord claimed the Tenant had lost its renewal option by failing to pay full rent. The Landlord relied on the following lease term:

Provided the Tenant is **not at any time** in default of any covenants within the lease, the Tenant shall be entitled to renew this lease for 1 additional term(s) of 60 months (each) on written notice to the Landlord given not less than 6 months [12 months in the case of unit 3] prior to the expiry of the current term at a rental rate to be negotiated. [bold added]

In response, the Tenant claimed that its failure to pay was not a breach of the lease because the Landlord had promised to apply for CECRA and was therefore estopped from requiring full payment. In any event, the Tenant claimed that the breach was “spent” because the Tenant had brought the arrears into good standing. It claimed that a “spent” breach could not deprive the Tenant of its option to renew the lease.

No Obligation to Apply for CECRA

The court held that the Landlord never promised to apply for CECRA. Although there was no need for written or even express oral statements to make a binding promise, the Landlord had only “given the impression” that it would apply for CECRA. There was no promise or assurance intended to affect the legal relationship between the Landlord and Tenant. Accordingly, the Landlord was entitled to rely on the Tenant’s breach of the lease by failing to pay rent.

“Spent Breach” Does Not Prevent Tenant from Exercising Renewal Option

Despite its breach, the Tenant was still entitled to renew the lease. The court held that the doctrine of “spent breach” provides that a Tenant will not lose a renewal right so long as the Tenant cures its breach by the time the option to renew is exercised.

The court’s decision is of interest for several reasons:

1. The “spent breach” doctrine applied despite express language in the lease that the Tenant must not be in breach “at any time” in order to exercise its renewal option. On first glance, this language would seem to end the Tenant’s renewal right upon the occurrence of any breach, even if the Tenant later cured its breach.
2. One rationale for applying the doctrine of “spent breach” in past cases has been that “absolute and precise compliance” by a tenant is not possible. Based on this rationale, it is arguable that the doctrine should only relieve from minor breaches. In this case, the doctrine applied despite rent due in October 2020 being in arrears until as late as April 30, 2021. This suggests that the doctrine will relieve from non-trivial breaches.
3. In applying the doctrine of “spent breach”, the court may consider the surrounding circumstances and the degree of effort expended by the Tenant in attempting to cure its breaches. The court appears to have taken the circumstances of the Covid-19 pandemic into account in finding that we are “in extraordinary times that call for extraordinary measures”. The court also noted that the Tenant tried “its level best” to pay the rent.

With many Tenants facing financial difficulties during the Covid-19 pandemic, we may soon receive additional clarity from the courts about the doctrine of “spent breach”. Aside from that specific issue here, this case may also serve as an example of how the Covid-19 pandemic should be expected to impact the application of legal principles generally in respect of commercial lease matters.

Negotiating Leases Going Forward

Landlords engaged in negotiating leases going forward may want to attempt to exclude or limit the

application of the doctrine of “spent breach”. It may be effective to specifically provide that the doctrine of “spent breach” shall not apply, but that may be difficult to achieve in a negotiation. Alternatively, some further precision in drafting the preconditions to the exercise of a renewal or extension right could be pursued such as requiring that the tenant not have been in chronic or persistent default and defining such a default as, for example, three or more defaults at any time or two or more defaults in any twelve-month period.

[1] [ps2id id='1' target='']2021 ONSC 642.

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A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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