GUARANTEES AND INDEMNITIES IN COMMERCIAL LEASES: WHAT TO WATCH FOR

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Guarantees and indemnities are ancillary agreements often included in commercial leasing transactions. These agreements are meant to further secure a tenant's obligations under the lease and enhance the landlord's recourse for tenant defaults under the lease. Despite their shared purpose, indemnities and guarantees differ in their practical effects.

This bulletin explores the key differences between guarantees and indemnities, and offers practical considerations for landlords and tenants contemplating these agreements as part of their commercial lease agreements.

Key Differences

The main differences between indemnities and guarantees are the contractual relationships they create between the indemnifier or guarantor and the landlord, and the triggers for the landlord's recovery against the guarantor or indemnifier.

Under an indemnity, the indemnifier is primarily liable for the landlord's losses incurred as a result of the tenant's default of its obligations under the lease. This means a landlord may pursue recovery from an indemnifier without first pursuing the defaulting tenant. In addition, an indemnity provision will survive the unenforceability of a lease. This means that the indemnifier remains liable for indemnified losses even if the lease cannot be enforced against the tenant for any reason such as the disclaimer of the lease in the context of a tenant bankruptcy.

In contrast, under a guarantee the guarantor is secondarily liable to meet the tenant's obligations under the lease. In other words, the landlord must first pursue recovery against the tenant before seeking recourse against a guarantor. A guarantor's liability falls away if the underlying lease is rendered unenforceable or changed without the guarantor's consent, the landlord fundamentally breached the lease or the lease creating the guarantor's obligations has not been signed yet.

As such, it is important for all parties to seek legal advice when negotiating and entering into indemnity or

guarantee agreements to ensure that their rights and obligations are clearly defined and properly protected.

Interpreting Guarantees and Indemnities

Contracting parties should be aware that simply calling a document a "guarantee" or an "indemnity" does not necessarily mean that the document is what it purports to be. A court will look to various indicia, and the context of the document itself, to determine whether the parties actually agreed to a guarantee or an indemnity. In any event, guarantees and indemnities are contracts, and therefore must contain the requisite components of any contract such as offer, acceptance and consideration.

Practical Tips

While not an exhaustive list, the following points should be kept in mind when negotiating guarantees and indemnities:

- From a tenant's perspective, it is advisable to exclude a guarantee or indemnity from a lease and instead attempt to satisfy the landlord in some other way regarding the tenant's ability to meet its covenants. If the landlord insists on the inclusion of a guarantee or indemnity, these provisions can be limited by time (e.g. the first two years of the lease's term); decline over time; or be limited by amount (e.g. the indemnifier's liability capped at $50,000.00).
- The scope of a guarantee should be carefully reviewed to see what the guarantor/indemnifier is actually agreeing to be responsible for; is it merely monetary amounts like rent, or does the obligation involve a wider scope, such as all of the obligations of the tenant under the lease.
- Guarantees and indemnities should clearly indicate that they are in consideration of the lease agreement. The best outcome from the landlord's perspective is to have the indemnifier/guarantor sign the lease as well, and have the guarantor/indemnifier acknowledge they have read and understood the contents of the lease.
- The landlord and the tenant may consider including a provision dealing with the tenant's change of control or transfer of the lease, and whether such an event releases the guarantor/indemnifier; the landlord will prefer that the obligation remain, while the tenant or guarantor/indemnifier would prefer that it fall away.
- Where there are multiple guarantors or indemnifiers, the landlord should consider adding a joint and several liability clause to ensure that the landlord can fully recover its losses from any of the guarantors/indemnifiers.

Provincial Considerations

In Alberta, the *Guarantees Acknowledgment Act* (the "**GAA**")[1] prescribes a formal procedure that must be

followed for a personal guarantee/indemnity to be effective, besides the general requirement that a guarantee/indemnity must be in writing to satisfy the *Statute of Frauds*[2] and other common law requirements. The GAA does not apply to guarantees or indemnities given by corporations, among other categories.

The GAA process involves appearing before a lawyer, with the lawyer explaining the nature of a guarantee/indemnity to the guarantor/indemnifier, and the lawyer satisfying itself that the guarantor/indemnifier is aware of and understands the contents of the guarantee/indemnity.[3] The lawyer then signs a standard form certificate to that effect and the guarantor/indemnifier signs confirming they are the person named in the certificate. A guarantor/indemnifier may comply with these requirements either in person or via two-way video conferencing with a lawyer.[4] Given the potential defence that the guarantor/indemnifier did not actually sign the GAA certificate (or guarantee) it is asserted to have signed, a landlord should request an originally-signed guarantee/indemnity and GAA certificate to hold for their records.

A guarantee or indemnity in British Columbia does not need to be in writing, since the *Law and Equity Act* allows for implied acceptance if "the alleged guarantor or indemnitor has done an act indicating that a guarantee or indemnity consistent with that alleged has been made".[5] For example, signing a credit application to pay a related party's outstanding invoices in exchange for the related party continuing to receive goods and services from the counterparty whose invoices were unpaid (for work performed for the related party).[6]

Given that Manitoba repealed the *Statute of Frauds* in 1988,[7] a Manitoba guarantee or indemnity could arguably be made verbally, although a written agreement provides far greater certainty on the terms agreed to between the parties.

While each province (other than Manitoba) has adopted the *Statute of Frauds* in some form, given the varying wording and the potential for differing interpretations of the *Statute*, landlords and tenants are wise to ensure their guarantees reflect relevant provincial considerations.

Conclusion

For a more detailed review of questions and concerns pertaining to guarantees and indemnities, please reach out to one of the members of McMillan's Commercial Leasing Team.

[1] RSA 2000, c G-11 [GAA].
[2] 29 Car c 3 (1677) (Other than the common law provinces discussed below).
[3] GAA, *supra* note 1, ss 3–4.
[4] Per the *Guarantees Acknowledgment Forms Regulation*, Alta Reg 66/2003, s 1.1, the video-conferencing

option currently expires August 15, 2024.
[5] *Law and Equity Act*, RSBC 1996, c 253, s 59(6). This Act replaces the *Statute of Frauds* in British Columbia.
[6] *Ace Instruments Ltd v Tobinsnet Oil & Gas Ltd*, 2022 BCSC 421 at para 7.
[7] *An Act to Repeal The Statute of Frauds*, CCSM c F158.

by Mervyn Allen, Ximena Pinilla and Jacob Stucken

A Cautionary Note