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Shopping Center Legal Update

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In Depth

When Is a Lease Not a Lease? Seventh Circuit Adopts 'Substance Over' Form Test for True Lease Determination — 2

Burning New Ground in Maryland Subrogation Law: *Rausch* v. *Allstate Insurance Co.* — 5

Employees Who Are Not Disabled: Reasonably Accomodating 'Regarded As' Disabilities — 8

Lingle v. *Chevron U.S.A., Inc.*: How the Supreme Court's Clarification of the 'Substantially Advances' Test Impacts Land Use Litigation — 10

Exclusives—Navigating Safely Through the Minefield — 13

Of Interest

Articles — 16

Cases — 16

- Assumption/Assignment — 16
- Attorney Fees — 16
- Bankruptcy — 16
- Condemnation/Eminent Domain — 17
- Constitutional Law — 17
- Fees — 17
- Franchises — 18
- Landlord & Tenant — 18
- Leases — 18
- Signs/Billboards — 18
- Tort Liability — 18
- Zoning — 18

Legislation — 19

From Canada

In Depth

British Columbia Court of Appeals Confirms No Implied Right of Renewal — 20

Enjoin the Picketers? — 22

Judicial/Legislative Review — 25

When Is a Lease Not a Lease? Seventh Circuit Adopts 'Substance Over' Form Test for True Lease Determination

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As secured financing and leasing transactions involving capital assets become more complicated to account for evolving tax, liquidity, equipment obsolescence and similar considerations, the difference between "true" leases and financing arrangements has become increasingly difficult to ascertain. The similar economic function of these transactions allows for the drafting of "leases" that work as security agreements and secured loans that work as "leases."

The distinction between these property interests is an important one, particularly if the owner/lessee of an asset files for bankruptcy. This is so because different rights and obligations apply under the Bankruptcy Code, depending on the nature of the debtor's interest in the property. Bankruptcy courts are frequently called upon to determine the exact nature of the debtor's legal interest. The Seventh Circuit Court of Appeals recently examined this issue. In *United Airlines, Inc.* v. *HSBC Bank USA, N.A.*, 416 F.3d 609 (7th Cir. 2005), the Court of Appeals ruled that a court must consider the substance of a transaction, rather than its form, in determining whether a transaction is a "true lease" or a disguised secured financing.

Treatment of Leases in Bankruptcy

The Bankruptcy Code itself does not define the term "lease." It broadly defines "security agreement" as an "agreement that creates a security interest" and "security interest" as a "lien created by an agreement." These definitions, however, offer little guidance in distinguishing between financing transactions that involve the retention of a security interest in sold assets, on the one hand, and leasing transactions where the lessor is granted a security interest in leased assets as an added layer of protection, on the other.

Why is the distinction important? The Bankruptcy Code confers certain rights, and imposes various obligations, upon a debtor that is party to leases and other contracts that are "executory" as of the bankruptcy filing date. A Chapter 11 debtor-in-possession ("DIP") or bankruptcy trustee generally has the right to "assume" ("reaffirm") or "reject" (disavow, resulting in breach) such contracts and leases under § 365 of the Bankruptcy Code. Moreover, most assumed contracts can be assigned as a means of creating value for the bankruptcy estate. Pending the decision to assume or reject, however, the DIP or trustee is obligated to remain current on post-petition lease obligations, failing which the leased property must be surrendered to the lessor or the lessor will be allowed to exercise its contractual and legal remedies notwithstanding the strictures of the automatic stay.

Different rules apply if a transaction involves secured financing rather than a lease. In this case, the DIP's or trustee's obligation to make payments to the secured lender during the course of the bankruptcy hinges on the value of the collateral relative to the amount of the lender's claim. If the collateral value exceeds the amount of the debt, the DIP or trustee may be

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required to make periodic interest payments to the secured creditor as a means of "adequate protection." By contrast, if a secured creditor is undersecured because its collateral value is deficient, adequate protection payments are generally not required, and the creditor will hold a secured claim only to the extent of the collateral value and an unsecured claim for the deficiency.

The ultimate fate of the collateral depends on the kind of bankruptcy case (i.e., Chapter 7 or Chapter 11) and the DIP's or trustee's ability to deal with the secured creditor's claims in accordance with the requirements of the Bankruptcy Code. In a Chapter 7, the property would either be abandoned to the secured creditor or sold to the highest bidder, with the secured creditor's liens attaching to the proceeds. By contrast, in Chapter 11, the DIP could confirm a plan of reorganization under which, among other things, the secured obligation is reinstated with the same collateral; the original collateral secures a new obligation whose terms vary from the original secured debt; collateral of equivalent value is substituted for the original collateral; or the collateral is sold, with the secured creditor's liens attaching to the proceeds.

Therefore, in addition to the ultimate issue of ownership of the asset in question, much depends on a transaction's characterization as a lease or a secured financing. How to make that determination, given the absence of any concrete guidance under the Bankruptcy Code, was the subject of the Seventh Circuit's ruling in *United Airlines.*

United Airlines

Prior to filing for Chapter 11 protection in 2002, United Airlines entered into a series of transactions to fund the improvement of its facilities at four airports. One such lease arrangement involved public financing underwritten by the California Statewide Community Development Authority (the "Authority"). United has been the lessee since 1973 of a 128-acre maintenance base at San Francisco International Airport ("SFO"). The lease expires in 2013 unless the parties negotiate an extension. Rent depends on an independent party's estimate of the property's market value.

In 1997, the Authority issued $155 million in bonds to finance improvements to United's SFO facilities (other than the maintenance base). The bonds are without recourse to the Authority and are guaranteed by United. United subleases 20 acres of the 128-acre maintenance base to the Authority for 36 years—the term matches the bond repayment schedule rather than United's lease with SFO. The Authority paid $1 to sublet the premises.

The Authority leases the 20 acres back to United for rent equal to interest on the bonds plus an administrative fee. This lease has a $155 million balloon payment in 2033 to retire the principal. United may postpone final payment until 2038; if it does, the sublease also is extended. United is entitled to prepay, in which case the sublease and leaseback terminate. If United does not pay as agreed, the Authority can evict it from the 20 acres. The leaseback includes a "hell or high water" clause requiring United to pay the rent, even if its lease from the SFO ends before 2033, the property is flooded, or some other physical or legal event deprives United of the use or economic benefit of the maintenance base.

After filing for Chapter 11, United took the position that none of the arrangements at the four airports in question is a "lease" for purposes of § 365 of the Bankruptcy Code. Instead, United sought a declaratory judgment that each transaction involves secured financing and that United should have the right to continue using the airport facilities while paying only a portion of the promised "rent." The bankruptcy court ruled that the arrangement at one of the airports is a true lease, but that the other three transactions (including the SFO arrangement) are not. The district court reversed those rulings in part on appeal, holding that all four transactions involved true leases rather than secured financings. United appealed to the Seventh Circuit.

The Seventh Circuit's Ruling

The Seventh Circuit joined all the other circuit courts of appeal that have considered this issue, ruling that substance rules over form, and that only a "true lease" qualifies as a "lease" under § 365 of the Bankruptcy Code. In reaching this conclusion, the Court of Appeals considered the practical meaning of the Bankruptcy Code, the Uniform Commercial Code (the "UCC") and the historical context of the Bankruptcy Code's enactment, including the statute's legislative history.

According to the Seventh Circuit, it "is unlikely that the [Bankruptcy] Code makes big economic effects turn on the parties' choice of language rather than the substance of their transaction," because to do so would allow the drafters of contracts to obliterate the distinction between the two types of transactions through creative drafting. This is consistent with the UCC, which, unlike the Bankruptcy Code, contains a detailed description of the distinction between a lease and a security interest, emphasizing that "[w]hether a transaction creates a lease or a security interest is determined by the facts of each case."

The Court of Appeals went on to explain that a lease in which "current consumption" (i.e., lease payments at market rates for continued use of an asset) dominates is often called a "true lease," while one in which the asset serves as security for an extension of credit is treated as a security agreement governed by the UCC. Finally, the Court of Appeals observed, the legal community of the 1970s understood that the distinction between leases and security agreements was based on substance rather than form, and looked to the relevant legislative history from the adoption of the Bankruptcy Code, which explains, in relevant part:

> Whether a "lease" is [a] true or bona fide lease or, in the alternative, a financing "lease" or a lease intended as security, depends upon the circumstances of each case. The distinction between a true lease and a financing transaction is based upon the economic substance of the transaction and not, for example, upon the locus of title, the form of the transac-

tion or the fact that the transaction is denominated as a "lease." Thus, the Seventh Circuit concluded that substance, rather than form, should be considered in determining whether a transaction is a "true lease" or a disguised secured financing for purposes of § 365 of the Bankruptcy Code.

The Court of Appeals then examined which law should apply to divine the true nature of any given transaction. Explaining that "nothing in the Bankruptcy Code says which economic features of a transaction have what consequences," the Seventh Circuit concluded that state law is determinative on this issue—in this case, California law. California, the Court of Appeals observed, has adopted a functional approach to the question in both the UCC and the common law governing real property transactions. It went on to discuss California court rulings examining various features of lease and financing transactions.

The Seventh Circuit ultimately determined that the transaction between United and the Authority was not a "true lease" under California law for the following reasons: (i) the "rent" was not measured by the market value of the property; (ii) at the conclusion of the lease, the Authority had no residual interest; (iii) the balloon payment had no counterpart in a true lease, but was a common feature of a secured financing; and (iv) upon prepayment, the lease and sublease terminated immediately, whereas in a true lease, prepayment secures the tenant's right to use the property for the term of the tenancy. Based upon this conclusion, the Court of Appeals reversed the district court's decision and remanded the case for further proceedings.

Analysis

The Seventh Circuit's ruling in *United Airlines* does not represent a departure from the approach employed by most courts, including every circuit court of appeals, to consider the issue, in determining what kind of transactions qualify as "leases" under the Bankruptcy Code. Even so, it illustrates the difficulties associated with sorting out the true nature of complicated lease and financing transactions by examining the substance of a transaction rather than the labels that have been attached to it by the parties. In almost all cases, such an inquiry demands painstaking analysis of a laundry list of factors, under applicable non-bankruptcy law, that have been deemed emblematic of leases, on the one hand, and financing arrangements, on the other. This analysis will only become more difficult as commercial transactions become more complex and exhibit hybrid characteristics that are not readily pigeon-holed in one category or the other.

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Burning New Ground in Maryland Subrogation Law: *Rausch* v. *Allstate Insurance Co.*

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Introduction

In a landlord-tenant relationship, when should a tenant be concerned about its liability if its negligence, or the negligence of its employees, causes great damage to the leased premises or to the remainder of the shopping center? Does existing law offer protection to unwary tenants? An insurer may have the right to sue the tenant if its policy contains a subrogation provision. Subrogation is the substitution of one person for another, giving the substitute the same legal rights as the original party. For example, an insurance company usually has a right of subrogation to sue anyone whom the person it compensated had a right to sue. Where real property is damaged and an insurer invokes a subrogation action, it stands in the shoes of the insured to recover against the third party that caused damage to the insured's property. As a result, without appropriate lease language, a tenant may be liable for the total cost to rebuild a shopping center.

In 2004, the Court of Appeals of Maryland decided *Rausch* v. *Allstate Insurance Company,* 388 Md. 690, 882 A.2d 801 (2005), clarifying Maryland law as it relates to a tenant's liability in a subrogation action. The issue before the court was: "Under what circumstances, if any, [may] the insurer pursue its contractual right of subrogation against a tenant of the insured who negligently damaged the insured premises and thereby caused the loss." *Rausch,* 388 Md. at 694. The court recognized that, in other states, most courts addressing the issue have held in favor of the tenant, finding against the insurance company based upon an express or implied waiver of subrogation or a release by the landlord of its right of recovery against the tenant.

Rausch Facts

The *Rausch* case was actually the consolidation of two cases in which residential tenants—Rausch and Harkin—burned down their respective leased property. Even though residential leases were involved, the same law would apply to commercial leases. In each case, the landlord maintained a fire insurance policy on the leased premises. Each of the tenants signed leases with similar provisions stating, generally: (1) the tenant was required to reimburse the landlord for any damages to the property caused by any act of negligence by the tenant; (2) the tenant would surrender the property in the same condition received; and (3) the tenant was required to maintain adequate personal liability and personal property insurance.

In both cases, insurance covered the landlord's losses. Following the insurance payments, the insurers sued the tenants in reliance upon the subrogation clauses in the fire insurance policies. In both insurance policies, the subrogation clause gave the landlord the right to waive its subrogation rights as to "another person" (Rausch) and a "tenant" (Harkin); but in the leases, the landlords did not expressly waive their rights of recovery or agree to obtain a waiver of the insurer's right of subrogation.

Discussion

The law of subrogation varies widely from state to state. Some states, by virtue of the landlord-tenant relationship, view the tenant as an additional insured and, therefore, not subject to a subrogation claim. Other states allow subrogation claims, with no concern for the landlord-tenant relationship.

The 'Majority' View: *Sutton* v. *Jondahl*

Many holdings state that the Oklahoma case, *Sutton* v. *Jondahl,* 532 P.2d 478 (Okla. Ct. App. 1975), best expresses the majority view on how tenants are regarded with respect to subrogation. In *Rausch,* the court states that *Sutton* is not the majority view and goes on to explain the *Sutton* holding, applicable in Oklahoma, as follows:

> [A]bsent an express agreement in the lease to the contrary, landlord and tenant are co-insureds under a landlord's fire insurance policy, and, as a result, the insurer has no right of subrogation against the tenant to recover amounts paid on the policy by reason of a fire loss, even if caused by the negligence of the tenant. *Id.* at 708.

Basically, by virtue of a landlord-tenant relationship, tenants are implied co-insureds under the landlord's existing fire insurance policies. Jurisdictions following the *Sutton* rule include Connecticut, Delaware, Maine, Massachusetts, Nebraska, Nevada, North Dakota, Utah and Washington. Consequently, these jurisdictions prohibit insurance companies from bringing a subrogation action against an "insured," with tenants being considered insured by virtue of the landlord-tenant relationship.

For two primary reasons, Maryland has refused to adopt the Oklahoma position. First, the *Rausch* opinion states that the Oklahoma court essentially pulled its holding out of thin air, with no legal backing for such a hard-and-fast rule. Second, the

Rausch court states that the Oklahoma court made assumptions about the "realities" of the landlord-tenant relationship, some of which may not be applicable to all circumstances. In essence, the Oklahoma court concluded that the rent charged to the tenant must necessarily reflect the expenses of the landlord, capturing the premium the landlord pays to the insurer. In this regard, the tenant's possessory interest in the premises entitles it to be an implied co-insured.

Divergent Interpretations of *Sutton*

The Court of Appeals of Maryland points out that several courts come to the same conclusion as *Sutton*—that is, that tenants are impliedly co-insured—but through a different logic. In Utah and Maine, the courts view the tenants as impliedly co-insured for economic reasons. Those courts hold that landlords are in a better position to insure the property, making such an arrangement "the most efficient way to allocate insurance costs." Connecticut courts, on the other hand, do not even attempt to justify their holding that tenants are impliedly co-insured. Their courts state that "the *Sutton* result is sound" as a matter of "policy" and "fairness." *DiLullo* v. *Joseph,* 792 A.2d 819 (Conn. 2002).

The 'Minority' View—Courts Adamantly Opposed to *Sutton*

Several jurisdictions have criticized the *Sutton* holding, including Arkansas, Illinois, Iowa, Kentucky, Minnesota, New York, North Carolina and Rhode Island. These jurisdictions have a strict constructionist view of the topic, looking to the terms of the lease in rendering their decisions. These courts hold that an insurer may bring such a claim, unless there is an express or implied agreement precluding a subrogation claim against a tenant.

Although the logic behind the laws of the states varies, the logic of several states is worth mentioning. In Arkansas, a court opined that, absent an agreement otherwise, if the landlord has no insurance he can clearly recover from the tenant and, therefore, the insurer should have the same right. In Iowa, the courts discount *Sutton,* based on the fact that the landlord and the tenant have "separate estates capable of being separately valued and insured." *Rausch* at 711-12. Rhode Island courts, reaching the opposite view of *Sutton,* refuse to rewrite insurance policies to include an insured that is not a party to the contract.

The Real Majority View—Reasonable Expectations of the Parties

After reviewing the national state of subrogation law, the Rausch court concluded that the real majority view is a middle-of-the-road approach. This approach is summed up in *Union Mutual Fire Ins. Co.* v. *Joerg,* 824 A.2d 586 (Vt. 2003), where the court observed:

> The majority of courts, however, have avoided per se rules and taken a more flexible case-by-case approach, holding that a tenant's liability to the landlord's insurer for negligence causing a fire depends on the intent and reasonable expectations of the parties to the lease as ascertained from the lease as a whole [extensive citations omitted]. Of the courts following this approach, most that have denied subrogation have done so because of the existence of specific provisions in the lease, such as a provision obligating the landlord to purchase fire insurance on the premises or a clause excepting fire damage from the tenant's responsibility to maintain or return the property in a good state and condition.

The middle-of-the-road approach looks at the lease and the surrounding circumstances, and reaches an ultimate conclusion based on the reasonable expectations of the landlord and tenant.

In *Rausch,* the Court of Appeals of Maryland adopted the "reasonable expectations" approach as Maryland's law, stating:

> We believe that this middle approach, of looking to the reasonable expectations of the parties to the lease, as determined from the lease itself and any other admissible evidence, is the appropriate one to follow. It avoids the court making assumptions and adopting fictions that are largely conjectural, if not patently illogical, and instead applies basic contract principles and gives proper credence to the equitable underpinning of the whole doctrine of subrogation.

The court rejected any hard or fixed rules for subrogation claims, choosing instead to examine each dispute on a case-by-case basis.

After stating Maryland's acceptance of the "reasonable expectations" approach, the court set forth a general analytical framework for reaching a conclusion as to the reasonable expectations of a landlord and a tenant. The court looked at four general principles on which such decisions should focus:

1. A subrogation claim is not contrary to public policy—normal contract law applies, and the tenant can only be liable to an insurer to the extent of the landlord's liability;
2. If a tenant is released from liability for fire loss in the lease, an insurer stepping into the shoes of the landlord has no right to a subrogation claim against the tenant;
3. A waiver of subrogation is implied where the landlord expressly or impliedly communicates to the tenant that the landlord will maintain fire insurance on the leased premises; and

4. If the leased premises is a unit in a multi-unit building, absent an express agreement to the contrary, a Maryland court will conclude that the landlord has a duty to have adequate fire insurance in place as to the entire building.

Under the fourth principle, the tenant may not be liable for the subrogation claim of the landlord's insurer as to damage to parts of the landlord's building outside of the portion of the building actually occupied by the tenant, but still could be - liable for damage to the leased premises.

Conclusion

What the *Rausch* holding means to Maryland landlords is simple—within the lease, the landlord should be clear as to the right of subrogation. Tenants should also always insist on a clause in the lease mandating that the landlord carry property damage coverage on the entire property. A waiver of subrogation clause without a duty on the landlord's part to carry any insurance may not be of any benefit to the tenant. A well-drafted lease should not require a Maryland court to apply a lengthy reasonable expectations test, but should make the intentions of the parties clear on its face. The lease should simply state that there is (1) a release of claims by the landlord to the extent of insurance, (2) a duty for the landlord to obtain and keep in force property damage insurance, and (3) a requirement that the landlord's policy permit the waiver of subrogation. The result of ambiguity in a lease is the potential for lengthy and costly litigation with the court attempting to interpret the reasonable expectations of the parties.

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Employees Who Are Not Disabled: Reasonably Accommodating 'Regarded As' Disabilities

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Does an employer have to accommodate an employee disability that does not exist? Apparently so in a number of states—including Florida, Alabama and Georgia. In *D'Angelo* v. *ConAgra Foods, Inc.,* the U.S. Court of Appeals for the Eleventh Circuit held in a lengthy opinion that the Americans With Disabilities Act (ADA) requires employers to provide reasonable accommodation to workers who are not actually disabled but only "regarded as" disabled by their employers. The Eleventh Circuit thus joins other federal appellate courts in concluding that such reasonable accommodation is required by law. Since *D'Angelo* imposes additional ADA obligations on employers, it is important to understand its holding and implications.

Facts

Cris D'Angelo was diagnosed with vertigo before she began working at a ConAgra seafood plant in Tampa, Florida. She worked in various factory jobs for almost three years without incident or injury and, during that period, received two promotions. Shortly before her discharge, D'Angelo complained to a non-supervisor line leader that looking at a moving conveyor belt (a task that she had not previously performed) made her light-headed, "off balance" and nauseous. The leader gave her a different job assignment. However, the supervisor subsequently returned D'Angelo to the conveyor belt and demanded medical documentation of her condition. D'Angelo's doctor's note said that she "has a vertigo condition. This affects her when her eyes have to look at moving objects such as belts. She should avoid the situation since it could cause her to fall and sustain injury." ConAgra considered the doctor's opinion and then concluded that, in light of the numerous moving conveyors and mechanical equipment in the factory, D'Angelo posed a safety hazard to herself and others. She was discharged.

D'Angelo filed a charge of disability discrimination and, subsequently, a federal court lawsuit alleging ConAgra had violated the ADA in discharging her rather than reasonably accommodating her vertigo by exempting her from work on the conveyor belt. D'Angelo contended that she not only was actually disabled, but also was "regarded as" disabled by ConAgra because of its erroneous beliefs about her condition. In other words, ConAgra had treated her as disabled even though she was not disabled within the meaning of the ADA. ConAgra moved for summary judgment. The district court granted the motion, finding that D'Angelo was not actually disabled and that the ADA does not require employers to reasonably accommodate workers who merely are "regarded as" but not actually disabled.

D'Angelo appealed the district court's ruling. In a decision announced Aug. 30, 2005, a three-judge panel of the Eleventh Circuit, in a 2–1 decision, affirmed the district court's finding that D'Angelo was not actually disabled (because there was no evidence that her vertigo substantially limited one or more of her major life activities or restricted her ability to perform a broad range of jobs). However, the appeals court majority held that the remaining issues would have to be sent back to the lower court for a jury trial because there were disputed issues of fact as to whether D'Angelo was "regarded as" disabled by ConAgra and whether she was a "qualified individual with a disability" within the meaning of the ADA.

Significantly, the Eleventh Circuit's *D'Angelo* majority also concluded that the district court had erred in holding that the ADA did not require reasonable accommodation for employees only "regarded as" disabled by their employers. It reasoned that because the ADA requires reasonable accommodation for all "disabled" employees, and defines disabled employees to include those merely "regarded as" disabled, employers must reasonably accommodate employees "regarded as" disabled.

The *D'Angelo* majority opinion considered the contrary conclusions of other federal appellate courts, which had held that, in essence, it would be unwise for Congress to have written the ADA to require reasonable accommodation for employees only "regarded as" disabled; the Eleventh Circuit concluded "quite simply, we are without authority to pass judgment on the wisdom of a congressional enactment." It further rejected another argument that had been accepted by several appellate courts—that is, requiring reasonable accommodation for "regarded as" employees sometimes will entitle an employee with a particular impairment to an accommodation while not entitling another with the same impairment to the same accommodation because of the employer's differing perceptions of the two workers. The Eleventh Circuit majority concluded that such disparity could be justified because, in fact, the two individuals were *not* similarly situated—the employee "regarded as" disabled will have suffered some wrongful adverse action that the other employee has not suffered—that is, the employee whose limitations are accurately perceived by the employer gets to work while the employee subject to the discriminatory perception is sent home unpaid. (The strong dissenting opinion in *D'Angelo* did not address the accommodation issue, holding only that the evidence did not substantiate that D'Angelo was either actually or "regarded as" disabled.)

Analysis

The Eleventh Circuit's *D'Angelo* ruling initially seems counterintuitive in the real world: Why or how should an employer accommodate a disability that does not exist? However, the decision makes sense in light of a primary motivation for enactment of the ADA: to ensure that erroneous stereotypes and beliefs about disabilities—and capabilities—do not negatively affect opportunities of otherwise qualified applicants and employees to obtain and retain employment.

The ultimate message from *D'Angelo* seems to be that if employers believe, even inaccurately, that a worker is disabled, they must act consistent with that belief and in accord with the ADA by providing reasonable accommodation. Insistence on an erroneous perception that the worker is disabled, coupled with a failure to discuss accommodation, can constitute, at least in the view of several federal courts, an ADA "failure to reasonably accommodate." As the federal appellate court in Colorado recently noted:

> … an employer who was unable or unwilling to shed his or her stereotypical assumptions based on faulty or prejudiced perception of an employee's abilities must be prepared to accommodate the artificial limitations created by his or her own faulty perceptions. In this sense, the ADA encourages employers to become more enlightened about their employees' capabilities, while protecting employees from employers whose attitudes remain mired in prejudice. *Kelly* v. *Metallic West, Inc.*, 410 F.3d 670 (10th Cir. June 7, 2005).

D'Angelo strongly suggests that employers be very careful in making decisions about employees they suspect to be medically or psychologically impaired. If the employer believes that a worker is disabled and is preparing to act on that suspicion by taking adverse employment action against the employee, the employer first must consider and be ready to provide reasonable accommodation consistent with the suspected disability. For example, if an employer believes that a worker's back injury is too severe to allow him to continue working at a job normally performed while standing, *D'Angelo* requires the employer to consider reasonable accommodation for the worker—for example, whether the job could be performed while seated, whether the job's duties can be restructured to allow it to be performed with a disabling bad back, and so on. It thus appears that *D'Angelo* will result in impaired employees receiving better treatment under the ADA if their employers treat them as disabled even if they are not disabled.

Employers can avoid having to provide reasonable accommodations for employees who are not actually disabled by avoiding erroneous conclusions. If the employer first engages an impaired employee in an interactive process to determine the actual extent of his or her limitations, the employer can accurately assess (using medical professional advice as appropriate) whether the worker is disabled and whether accommodation is factually and legally necessary. Further, even if the employer and the employee never agree about his or her limitations, it may be possible to identify inexpensive reasonable accommodations that will allow the employee to perform the essential functions of the job (and avoid another *D'Angelo* lawsuit).

The *D'Angelo* decision conflicts with other carefully considered opinions of the federal courts. Some courts have been reluctant to require reasonable accommodation to a "regarded as" disabled employee because to do so would provide disincentives for impaired workers to educate employers about their capabilities, discourage employers from clearly assessing employees' talents and provide "regarded as" workers a windfall by perpetuating employers' misperception of their impairments. Further, in the view of other courts denying reasonable accommodation for workers only "regarded as" disabled, such accommodation would compel employers to waste resources unnecessarily—resources that could be better spent assisting persons who are actually disabled and genuinely in need of accommodation. However, until the views of those courts are adopted by the U.S. Supreme Court, many employers will be bound by *D'Angelo.*

Conclusion

It is now common for ADA plaintiffs to allege both actual *and* "regarded as" disabilities; therefore, *D'Angelo* and similar decisions in the federal Third and Tenth Circuits impose additional ADA liability on employers. Although the federal appellate courts for the Fifth, Sixth, Eighth and Ninth Circuits have come to contrary conclusions about the need to accommodate workers only "regarded as" disabled, the U.S. Supreme Court recently refused to resolve those conflicting decisions and, thus, there is no immediate relief in sight for companies having operations in several states. In the interim, employers must carefully assess and accommodate workers who they "regard as" disabled.

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Lingle v. *Chevron U.S.A., Inc.*: How the Supreme Court's Clarification of the 'Substantially Advances' Test Impacts Land Use Litigation

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Shopping center developers lost a bargaining chip—the threat of monetary damages—that was useful when negotiating zoning changes as a result of the U.S. Supreme Court's decision in *Lingle* v. *Chevron U.S.A., Inc.,* 125 S.Ct. 2074 (2005). This article will briefly examine pre-*Lingle* takings law and analyze how *Lingle* changed (or did not change) the equation for developers seeking to change a zoning regulation in the face of opposition from the municipality that has jurisdiction.

Developers' Utilization of the *Agins* Disjunctive Test to Secure Zoning Changes

The Supreme Court stated in *Agins* v. *City of Tiburon,* 447 U.S. 244 (1980), that the "application of a general zoning law to particular property effects a taking if the ordinance does not substantially advance legitimate state interests, see *Nectow* v. *Cambridge,* 277 U.S. 183, 188 (1928), or denies an owner economically viable use of his land, see *Penn Central Transp. Co.* v. *New York City,* 438 U.S. 104, 138, n. 36" (emphasis added). 447 U.S. at 260.

Real estate developers relied on this test and subsequent case law to set the foundation for takings claims in lower courts that did not take into account whether the challenged legislation diminished the economic value or usefulness of their property. In *State ex rel. Shemo* v. *City of Mayfield Heights,* 95 Ohio St.3d 59, 63 (Ohio 2002), for instance, the Ohio Supreme Court stated that the "test is disjunctive, i.e., a compensable taking can occur *either* if the application of the zoning ordinance to the particular property is constitutionally invalid, i.e., it does not substantially advance legitimate state interests, *or* denies the landowner all economically viable use of the land." In other words, if the developer were able to challenge the constitutionality of the zoning restriction successfully, it would have been able to collect monetary damages regardless of whether the restriction affected the property's economic value or usefulness.

This disjunctive test provided real estate developers with a bargaining chip in settling land use cases with governmental authorities. Developers, under the *Agins* disjunctive test, had the ability to use the threat of monetary damages as an incentive to convince local governments to settle zoning disputes. A determined developer could even slant the *Agins* equation further in its favor. It could "sweeten the deal" offered to the municipality with concessions on site plans that would shift the local government's cost-benefit analysis in favor of settling the zoning dispute.

The potential damages avoided through such settlement can be quite substantial. In *Shemo,* for instance, the Ohio Supreme Court held that the property owners were entitled to the diminution in the "value of the use" of their property during the "period of the temporary taking," 95 Ohio St.3d. at 69. Even though the *Shemo* Court later shortened the period of the taking by nearly three years because the property owners had voluntarily dismissed their claim during that time, the potential damages remain substantial.

The Supreme Court's Decision in *Lingle*

A unanimous Supreme Court put an end to the *Agins* disjunctive test in *Lingle*—and the Court did not do this gently. Writing for the unanimous Court, Justice O'Connor acknowledged that "[t]hrough reiteration in a half dozen or so decisions since *Agins,*" the disjunctive test language "has been ensconced in our Fifth Amendment takings jurisprudence." *Lingle,* 125 S.Ct. at 2077–2078. However, she cautioned that the *Agins* disjunctive test was an example of "a would-be doctrinal rule or test" that "finds its way into our case law through simple repetition of a phrase—however fortuitously coined." *Id.* at 2077. It was time, therefore, to clean out this fortuitous *dicta* that had led to much confusion.

Based upon *Agins*' "substantially advances" formula, the lower courts in *Lingle* struck down a Hawaii statute that limited the rent that oil companies may charge to dealers who lease service stations owned by the companies. *Lingle,* 125 S.Ct. at 2078. The record before the Supreme Court contained a stipulation by the parties that "Chevron has earned in the past, and anticipates that it will continue to earn under Act 257, a return on its investment in lessee-dealer stations in Hawaii that satisfies any constitutional standard." *Id.* at 2079. The lower courts, however, applied the *Agins* disjunctive test to conclude that the rent cap effected an uncompensated taking of private property in violation of the Fifth and Fourteenth Amendments to the United States Constitution because it did not substantially advance Hawaii's asserted interest in controlling retail gasoline prices. *Id.* at 2078.

Chevron argued, in *Lingle,* that a "land use regulation that does not 'substantially advance' a legitimate state interest is invalid under the Fifth Amendment ***unless*** just compensation is paid" (emphasis added). Brief for Respondent at 10, *Lingle* v. *Chevron U.S.A., Inc.,* 125 S.Ct. 2075 (2005) (No. 04-163). The petitioners, however, argued to the Court that the "government may not use its power of eminent domain to take property for an improper purpose, regardless of whether compensation is offered or available through the courts." Brief for Petitioners at 20, *Lingle* v. *Chevron U.S.A., Inc.,* 125 S.Ct. 2075 (2005) (No. 04-163).

As such, if "a government regulation is arbitrary or irrational, it cannot become permissible as a result of a government offer to pay compensation, and it would make no sense to impose an obligation on the public to pay just compensation for a regula-

tion that is invalid and must therefore be rescinded." *Id*. The Court ultimately agreed with the petitioners, and held that "no amount of compensation" can authorize an infirm zoning regulation. *Lingle,* 125 S.Ct. at 2084.

The Court explained that there are two ways of challenging the constitutionality of a zoning ordinance:

The first method challenges the zoning ordinance under the Due Process Clause, which is commonly known as the "substantially advances" test. *Lingle,* 125 S.Ct. at 2083. In *Village of Euclid* v. *Ambler Realty Co.,* 272 U.S. 365 (1926), the Court held that a zoning ordinance survives constitutional muster unless it is not "clearly arbitrary and unreasonable, having no substantial relation to the public health, safety, morals, or general welfare." *Id*. at 295. The remedy for such a successful substantially advances challenge is to strike down the infirm zoning regulation—not to award compensation. *Lingle,* 125 S.Ct. at 2084. Since this substantially advances claim exists only under the Due Process Clause and not the Just Compensation Clause, it is "not a valid method of discerning whether property has been 'taken' for purposes of the Fifth Amendment." *Id.*

The second method, however, is to allege a taking of the property and seek compensation under the Fifth Amendment to the United States Constitution. The Fifth Amendment, which is made applicable to the States through the Fourteenth Amendment, provides: "No person shall be … deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation." U.S. Const. Amend. V. The petitioners argued in *Lingle,* and the Court apparently agreed, that the application of the *Agins* disjunctive test "resulted from a mistaken transportation of substantive due process doctrine [the first substantially advances challenge as explained above] into takings law [the second challenge seeking compensation], where it does not belong." Brief of Petitioners at 23, *Lingle* v. *Chevron U.S.A., Inc.,* 125 S.Ct. 2075 (2005) (No. 04-163).

When a party alleges a taking of its property, the Supreme Court had recognized, in *First English Evangelical Lutheran Church of Glendale* v. *County of Los Angeles,* 482 U.S. 304 (1987), that the Just Compensation Clause "does not prohibit the taking of private property, but instead places a condition on the exercise of that power." *Id.* at 314. Thus, "[t]his basic understanding of the Amendment makes clear that it is designed not to limit the governmental interference with property rights *per se,* but rather to *secure compensation* in the event of otherwise proper interference amounting to a taking" (emphasis in original) *Id.* The purpose of compensation when a "taking" has been found (i.e., legitimate governmental regulation that effects a taking), therefore, is to ensure that the property owner should not alone "bear public burdens which, in all fairness and justice, should be borne by the public as a whole." *Lingle,* 125 S.Ct. at 2080 [quoting *Armstrong* v. *United States,* 364 U.S. 40, 49 (1960)].

The Court examined the evolution of regulatory takings jurisprudence in reaching its decision in *Lingle*. In *Lucas* v. *South Carolina Coastal Council,* 505 U.S. 1003 (1992), the Court had observed that "early constitutional theorists did not believe the Takings Clause embraced regulations of property at all." *Id.* at 1028, n. 15. In fact, until the Supreme Court's decision in *Pennsylvania Coal Co.* v. *Mahon,* 260 U.S. 393 (1922), it "was generally thought that the Takings Clause reached only a 'direct appropriation' of property, or the functional equivalent of a 'practical ouster of [the owner's] possession.'" *Lucas,* 505 U.S. at 1014 (citations omitted). The Court, therefore, reaffirmed in *Lingle* that regulatory takings tests aim "to identify regulatory actions that are functionally equivalent to the classic taking in which government directly appropriates private property or ousts the owner from his domain." *Lingle,* 125 S.Ct. at 2082.

The Court explained that there are two types of "categorical" *per se* regulatory takings. The first categorical regulatory taking (a "*Loretto* taking") involves a situation where the government requires an owner to "suffer a permanent physical invasion of her property—however minor." In such a case, it must provide just compensation. *Id*. at 2081 [citing *Loretto* v. *Teleprompter Manhattan CATV Corp.,* 458 U.S. 419 (1982)]. The second categorical regulatory taking occurs where the governmental action, usually an ordinance, completely deprives an owner of "all economically beneficial us[e] of her property." *Lingle,* 125 S.Ct. at 2081 (emphasis in original). This is known as a "*Lucas* taking" based on the U.S. Supreme Court's decision in *Lucas* v. *South Carolina Coastal Council,* 505 U.S. 1003 (1992).

Outside these two narrow categories (and certain land use exactions), the *Lingle* Court resurrected its decision in *Penn Central Transp. Co.* v. *New York City,* 438 U.S. 104 (1978), as the governing law on all remaining regulatory takings challenges. *Lingle*, 125 S.Ct. at 2081. This appears to be the primary impact of the Court's decision. The South Carolina Supreme Court, for instance, noted, in *Byrd* v. *City of Hartsville,* 365 S.C. 650 (2005), that *Lingle* clarifies "Penn Central is the test to be applied when no per se taking is involved." 365 S.C. at 659 n. 9.

Lingle's Practical Effect on Land Use Litigation

Penn Central is a complicated decision that is not easy to apply in practice. It applies a nuanced analysis based on a number of factors, the most important of which is the economic impact of the challenged regulation. *Lingle,* 125 S.Ct. at 2081–2082. The *Penn Central* factors, which are scattered throughout the Court's decision, include

> (1) the economic impact of a regulation on the plaintiff; (2) the extent to which the regulation has interfered with "investment backed expectations"; (3) the character of the governmental action; (4) whether the ordinance prevented a reasonable use of the property; (5) whether the ordinance is reasonably necessary to effect a substantial public purpose; (6) whether the owners of the property received a benefit commensurate with the burden of the regulation; and (7) whether the landowner secured an "average reciprocity of advantage." Stuart Meck and Kenneth Pearlman, *Ohio Planning and Zoning Law* § 10:5 (2005 edition) (compiling *Penn Central* factors from different parts of the Court's opinion).

Yet, *Penn Central's* nuanced approach to *ad hoc* factual inquiries appears to be the formula that has withstood the test of time for regulatory takings claims. In fact, contrary to the perception of many after *Agins,* the *Penn Central* decision never really left the scene. The Ohio Supreme Court's *Shemo* decision, for instance, gained national attention for its emphasis on the *Agins* disjunctive test. Such simplified recognition, however, often overlooked the facts that were before the Court in *Shemo*. Unlike *Lingle,* where the parties had stipulated that Chevron earned a return on its investment that satisfies any constitutional standard, the Ohio Supreme Court applied *Penn Central's* economic impact factors in *Shemo* and found that the property owner had met its burden under *Penn Central*. The Court stated that

> even assuming that the *Penn Cent./Palazzolo* analysis applies, a finding of a compensable taking is still warranted … because [r]estricting relators' land to residential use on property that was held to be unsuitable for residential use had an obvious adverse economic impact on relators, which necessarily interfered with their reasonable investment-backed expectations when they requested that the property be rezoned for retail development." *Shemo,* 2002–Ohio–4905 at ¶ 11.

In other words, had the facts been different respecting the regulation's economic impact, there is at least an argument that *Shemo* may have been decided differently.

In light of *Lingle's* real-world practical effect, it is striking that the public and the legal community's recent attention has been focused on *Kelo* v. *City of New London,* 125 S.Ct. 2655 (2005), instead of *Lingle.* Despite its emotional impact, *Kelo* is a limited decision. Chief Justice Roberts, in fact, outlined *Kelo's* two obvious, but often unmentioned, limitations in his Senate confirmation hearing:

First, then Judge Roberts noted that *Kelo* contained a "caveat" in that it was premised on "an urban redevelopment plan" and "left open" the question of "just taking one parcel and giving it to somebody else, not part of a broader plan." Hearing of the Senate Judiciary Committee Morning Session: Confirmation Hearing for Judge John H. Roberts to be Chief Justice of the United States (Sept. 14, 2005, Federal News Service).

Second, the legislatures, not the courts, are the bodies that exercise the power of eminent domain. If the legislatures choose not to exercise their eminent domain powers, *Kelo* would be a non-issue. The now Chief Justice explained that "the Court was not saying you have to have this power, you have to exercise this power." Instead,

> … what the Court was saying is, there is this power, and then it's up to the legislature to determine whether it wants that to be available, whether it wants it to be available in limited circumstances, or whether it wants to go back to an understanding as reflected in the dissent; that this is not an appropriate public use. Hearing of the Senate Judiciary Committee Morning Session: Confirmation Hearing for Judge John H. Roberts to be Chief Justice of the United States (Sept. 14, 2005, Federal News Service).

In fact, *Kelo* prompted many states to reconsider their eminent domain practices. Regardless of how different states react to *Kelo,* this decision will provide an opportunity for legislatures to study eminent domain and reconsider when it is appropriate to exercise this power. Ohio, for instance, enacted a short-term moratorium on eminent domain for economic development in situations when ownership of the property will eventually be in private hands, and created a Legislative Task Force to Study Eminent Domain and Its Use and Application in the State. [For information on the different states' post-*Kelo* efforts, visit the National Conference of State Legislatures' website at http://www.ncsl.org/programs/natres/post-keloleg.htm, and the Institute for Justice's Castle Coalition's website at http://www.castlecoalition.org/legislation; *see also* John M. Broder, States Curbing Right to Seize Private Homes, *The New York Times* (February 21, 2006).] The hope, indeed, is that in the process of studying eminent domain, state legislatures will also clarify and modernize statutes delineating eminent domain procedures.

As far as regulatory takings jurisprudence is concerned, however, land use and zoning practitioners should focus their attention on how courts react to the *Lingle* decision. While *Penn Central* has been around since 1978 and there have been many Supreme Court regulatory taking cases since then, there is still no firm, coherent approach on how to apply *Penn Central* at the trial level. Trial courts still need guidance from higher courts on how to better apply *Penn Central* with its multifaceted factors. This is still a developing area of the law that promises to bring about many changes with significant practical effects on real estate development.

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Exclusives—Navigating Safely Through the Minefield

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Tenant exclusive rights are a minefield where a failure to "get it right" could unduly hamper the landlord's ability to lease, operate and maximize the potential of its property and expose the landlord to significant liability. This article describes a recent case in which the exclusive restriction was grounds for a landlord's refusal to consent to an assignment. A discussion follows of some of the more important issues that landlords and their counsel should consider when drafting and negotiating exclusives.

Danyaal Enterprises Ltd. v. *Big Bear Food Ltd.* [2004 O.J. No. 3371]

The landlord and tenant (Big Bear Foods) agreed that the tenant's premises were to be used for the purpose of carrying on the business of a "convenience retail store." At the time the lease agreement was entered into, another tenant of the centre had a lease in which the landlord gave that tenant the exclusive right to carry on the business of selling delicatessen sandwiches. A dispute arose when Big Bear Foods began to advertise and sell freshly prepared sandwiches. The landlord sought to restrain Big Bear Foods from selling sandwiches, as it caused the landlord to be in breach of the exclusive right it granted to the pre-existing tenant.

According to the Court, there was nothing in the lease with Big Bear Foods that specifically prohibited it from using the premises for any certain activity. Big Bear Foods was, therefore, entitled to use the premises for the purposes set out in the lease and this use was only limited by the definition of the phrase "convenience retail store." The phrase was clear and unambiguous, and the business of a convenience store included the business of selling fresh sandwiches.

The court concluded that based on the wording in the lease, Big Bear Foods was not prohibited from using the leased premises for the purposes of selling fresh sandwiches. If it was the landlord's intention to place restrictions on the type of business the tenant could engage in to protect the pre-existing tenant's rights, the landlord could have attempted to negotiate some restrictions on the tenant's use of the premises. Since the landlord failed to negotiate any restrictions on Big Bear's use of the premises, the court held that the use of a convenience store to sell fresh sandwiches was permitted under Big Bear's lease.

This case serves as a classic example of what can go wrong when a landlord is not careful in granting exclusives and in drafting subsequent use rights. The dispute in this case could have been avoided, had the landlord considered and addressed the issues described below (in particular, those under the subheadings "Landlord Preliminary Due Diligence" and "Scope of Protected Use").

Landlord Preliminary Due Diligence

Landlords must take great care to avoid granting exclusives that might conflict with other tenants' rights and thereby expose the landlord to claims for damages, injunctive relief or even lease termination. Prior to granting any exclusive, it is imperative that the landlord review all existing exclusives and anchor tenant leases to confirm that the proposed exclusive will not place the landlord in breach of those pre-existing exclusives or any anchor tenant lease restrictions. The landlord should also review all existing permitted uses for its property, and satisfy itself that the use rights of existing tenants do not and could not infringe upon the proposed exclusive.

Leases with unrestricted or very broad permitted uses (such as those permitting "any lawful use") represent a common source of use/exclusive conflict and must be dealt with adequately. (See discussion below regarding "Other Tenants Not Bound by Exclusive.") The landlord should also think about the actual use conducted by its existing tenants, as a tenant's actual use often deviates from its permitted use or encompasses items that are not within the express contemplation of the use clause included in the lease.

Scope of Protected Use

Narrow vs. Broad Protected Uses. The landlord should avoid broad, sweeping exclusives and opt instead for clear, unambiguous and expressly identified items or services or types of businesses that are to be prohibited by an exclusive. Broad exclusives should be narrowed to focus on those businesses or uses that are truly competitive to a tenant seeking the benefit of an exclusive. For example, a generic exclusive prohibiting "family restaurants" could be refined in scope to prohibit "sit-down, full table service, casual dining Italian-themed restaurants having pizza and pasta as their primary menu items." Clearly drafted, narrow exclusives help avoid unintended conflicts with the rights of others and the unnecessary restriction of the landlord's right to lease and operate its property. They also help ensure that the landlord is not left in a position where it is uncertain as to the legal scope of the prohibition which it has granted. For example, the grant of a generic exclusive for a

"music store" may lead to confusion as to whether the landlord may lease the premises to a retailer that sells both books and music compact discs.

If the landlord must agree to a general, broad exclusive, at a minimum, care must be taken to ensure that the tenant is not given the exclusive right to sell one or more of the various products or items offered as part of its business, the intent being to make the exclusive apply to the general type of business but not all individual aspects of the business. By way of example, if the landlord granted an exclusive on "drug stores," the exclusive should expressly permit the landlord to lease premises for such uses as a health food and vitamin nutrition store as well as a beauty and cosmetics store.

Primary vs. Ancillary Use. Ancillary uses conducted by other tenants of a property should not pose too great a competitive threat to a tenant seeking an exclusive. Accordingly, where possible, in order to avoid an unnecessary restriction on the landlord's ability to lease its property, the scope of a tenant's exclusive should be restricted to the primary or principal uses of the other tenants in the landlord's property. For example, in lieu of granting a tenant an exclusive on "the sale of hamburgers," the exclusive should be limited to restrict other tenants from selling hamburgers as a primary or principal menu item. Ancillary uses could be defined as a maximum percentage of gross sales, floor space or shelf display space, or any combination of the foregoing.

Where the landlord cannot limit an exclusive to the primary or principal uses of other tenants, very careful thought must be given to the exact nature of the products and services being protected and, at a minimum, exceptions should be made for those tenants or businesses whose uses are sufficiently diverse such that the protected products and services could be included as part of their business. For example, in granting an exclusive to an ice cream parlor for the sale of ice cream, the landlord should consider negotiating exceptions for restaurants serving ice cream as a dessert item and grocery stores selling ice cream by the tub.

Actual Use Conducted by Tenant. Assume, for example, that a particular tenant in whose favor an exclusive has been granted has itself a broad use clause that enables it to carry on other types of uses, or perhaps the exclusive applies only in relation to one component of a tenant's permitted use. In either case, the landlord should draft the exclusive so that it is enforceable only for so long as that tenant actually carries on the particular use to which the exclusive applies. Without language to this effect, an anomaly could arise where the tenant continues to have the benefit of the exclusive, even though it no longer carries on the business or sells the items protected by the exclusive.

Other Tenants Not Bound by Exclusive

An exclusive right may conflict with the use right of an existing tenant, or an existing tenant may diversify or change its use at sometime in the future and thereupon infringe upon an exclusive granted to another. To avoid problems, existing tenants should be excluded from the scope of any new exclusive granted. This will ensure that conflicts do not arise in connection with prior rights. As a further precaution, the subtenants, successors and assigns of existing tenants should also be excluded, as this will ensure that the exception will continue to apply, should the existing lease be assigned or the premises sublet.

If possible, the landlord should also reserve unto itself the right to replace existing tenants with new tenants having similar uses. In this way, the landlord will be permitted to maintain its merchandising mix, as it may replace competitive uses with similar competitive uses. For example, if the landlord granted an exclusive for a coffee shop while an existing coffee shop was in place at the centre, the landlord would be permitted to replace the first coffee shop with a similar use, thereby ensuring that the centre always maintains two coffee shops.

As anchors and other large tenants typically have very broad or unrestricted uses, these tenants should also be excluded from exclusives granted by the landlord. In this regard, it is typical to exclude department stores, supermarkets and other anchors as well as large stores with a floor area greater than a specified square footage (usually 10,000 to 30,000 square feet).

Duration of Exclusive

As an alternative to granting an exclusive for the entire span of a tenant's lease, the landlord should consider granting an exclusive that is limited in duration. This approach is useful for start-ups or for smaller tenants where the landlord would not otherwise grant an exclusive. The limited exclusive would provide the tenant with some protection while it gets its business up and running and establishes itself. The most common manner in which to limit the duration of an exclusive is to have the exclusive expire after a certain fixed period of time has elapsed. For example, the exclusive could be made to lapse after the first two or three years of the term. Similarly, the exclusive could be made to apply during the initial term but not during any renewal or extension terms. The duration period would obviously be subject to negotiation. The duration of an exclusive could also be limited by tying its applicability to the tenant's gross sales. Using this approach, the tenant's exclusive could be made to come to an end once the tenant's gross sales for a set number of months reach a predetermined dollar amount (which could be calculated on a per square foot or other basis). This type of exclusive helps ensure that the tenant is given enough time to get itself established, but is not given a more generous exclusive than it requires.

Combinations of the two foregoing approaches are also possible. For example, the exclusive could be made to expire on the earlier of the lapse of a certain fixed period of time or when the tenant's gross sales reach a predetermined threshold.

Area Covered

In addition to limiting the applicability of an exclusive to a period consisting of less than the entire duration of a tenant's lease, it is also prudent to consider limiting the area covered by an exclusive so that, unless absolutely necessary, it does not extend to the entire property of the landlord. This is particularly useful in instances where the landlord's property is a mixed-use development or encompasses different categories of leasable premises (such as an enclosed mall, freestanding pad, food court and office). For example, tenants of freestanding, outparcel pads may pose little or no competition to tenants of the associated enclosed mall. In such circumstances, the landlord should consider excluding the outparcels from the scope of the exclusives granted to the enclosed mall tenants. Similarly, the exclusives granted to food court tenants could also be limited so that they only apply to the food court area of the shopping centre.

The landlord may also want to consider excluding future expansions of the shopping centre from the scope of a tenant's exclusive. This will assist the landlord in retaining flexibility with respect to the leasing and merchandising mix of the expansion.

Sometimes a tenant insists that its exclusive is to extend beyond the boundaries of the property where the tenant's premises are found. Typical examples include the extending of an exclusive to adjoining parcels or to properties owned by the landlord within a certain radius of the shopping centre (often several miles). Where such an exclusive cannot be avoided, the exclusive should restrict the landlord from entering into offending leases, but should otherwise permit the landlord to acquire properties or parcels where they contain a pre-existing conflicting use. (In other words, leases that pre-existed the landlord's purchase should be excluded from the scope of the exclusive.) In this way, the landlord will not be barred from purchasing a desired property simply because it would be in breach of an exclusive. The competitive or offending use existed prior to the landlord's acquisition of the property, and the landlord should not be penalized for a lease into which it did not enter.

Miscellaneous Issues

Default. The landlord should not allow a defaulting tenant to restrict the landlord's ability to lease its property or to restrict the goods or services that may be offered by tenants in good standing. Accordingly, if a tenant fails to observe and perform its obligations under its lease, the rights afforded by its exclusive should permanently cease or, at a minimum, should be suspended for the period during which the tenant is in default.

Actually Operating. The landlord should draft the exclusive so that it applies only for so long as that tenant is actively carrying on its business in the premises. Without language to this effect, the tenant will continue to have the benefit of the exclusive, even though it no longer carries on the business or sells the items protected by the exclusive. Failure to so qualify an exclusive could prove detrimental to the merchandising mix of the property if, for example, the landlord could not replace a tenant that provides a valuable or vital service (e.g., clothing alteration, shoe repair or pharmacy). This would be the case if the landlord granted an exclusive for such service to one tenant, but that tenant later elected to cease operating in the premises.

Grandfathering. In cases where the exclusive is not permanently lost if some of the conditions attached to it are not satisfied, a "grandfathering" clause should be included, stipulating that the exclusive will not apply to any and all rights that the landlord granted during any temporary period in which the exclusive was not in effect. This will ensure that the landlord will not be in breach of the exclusive, should the exclusive right become operative at a later date.

Ongoing Prudence

Given the significant liability and other consequences that may flow from the landlord's breach of a tenant's exclusive, landlords should implement a reliable system to track the uses and exclusives within a centre. At a minimum, an up-to-date list of permitted uses and exclusives should be maintained and should be reviewed each time a new lease is entered into or a new use or exclusive is granted. Of course, the landlord's leasing agents should familiarize themselves with this list. As a further line of defense, the landlord should attach a list of all the exclusives it has given in its centre as a schedule to every new lease it enters into and, correspondingly, these leases should include a covenant on the part of the tenant not to breach the exclusives.

The importance of drafting and negotiating exclusives should not be underestimated. Care should be taken to ensure that the issues discussed herein are addressed. The landlord in *Danyaal Enterprises Ltd.* v. *Big Bear Food Ltd.* failed to benefit from a well-drafted exclusive. We can all learn from that mistake.

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Of Interest

Articles

Bill D. Bensinger, "Beneath the Surface of BAPCPA—Modification of Collective Bargaining Agreements: Does a Breach Bar Rejection?" 13 *Am.Bankr.Inst.L. Rev.* 809 (Winter 2005).
Robert N.H. Christmas, "Designation Rights—A New Post-BAPCPA World," 25-FEB *Am.Bankr.Inst.J.* 10 (February 2006).
David I. Cisar & Rebecca H. Simoni, "Secured Letters of Credit and the §502(b)(6) Cap on Lease Rejection Damages," 24-FEB *Am.Bankr.Inst.J.* 10 (February 2005).
Michelle Morgan Harner, Carl E. Black & Eric R. Goodman, "Debtors Beware: The Expanding Universe of Non-Assumable/ Non-Assignable Contracts in Bankruptcy," 13 *Am.Bankr.Inst.J.* 14 (Spring 2005).
Gregory G. Hesse, "Letters of Credit and Leasehold Rejection Damages," 25-MAR *Am.Bankr.Inst.J.* 20 (March 2006).
Pamela Smith Holleman & Magdalena Ellis, "Reexamining the Protections Afforded to Solvent Shopping Center Tenants Under § 365 in Light of *In re Trak Auto Corp.* Part II," 24-FEB *Am.Bankr.Inst.J.* 12 (February 2005).
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Mette H. Kurth & Joel Ohlgren, "Ride-Through Revisited (Again)—The Strategic Use of the Ride-Through Doctrine in the Post-Catapult Era," 24-JUN *Am.Bankr.Inst.J.* 16 (June 2005).
Laura J. Margulies, "Understanding the New Semi-Automatic Stay," 25-MAR *Am.Bankr.Inst.J.* 26 (March 2006).
Bruce H. White & William L. Medford, "Application of Section 502(b)(6)'s Lease Rejections: An Update on Damages Cap to Letters of Credit," 25-MAR *Am.Bankr.Inst.J.* 36 (March 2006).

Cases

Assumption/Assignment

A bankrupt automobile dealership could not assume its executory dealership agreement, under which the debtor was permitted to operate the dealership only in specified locations, and assign it free of the location restriction to a third party that intended to operate the dealership in a different location. *In re Morande Enterprises, Inc.*, 335 B.R. 188 (Bkrtcy.M.D. Fla.2005).

Attorney Fees

Although the parties' original lease provided that an award of attorney fees for the prevailing party was appropriate, the parties' entry into a settlement agreement for a new lease nullified any benefit that might have been received as the prevailing party in a litigation. *Keal* v. *Day,* 164 Ohio App. 3d 21; 2005 Ohio 5551, 840 N.E.2d 1139 (Ct. App. Ohio, 1st App. Dist., Hamilton Co., 2005).

Bankruptcy

The term "option" as used in a commercial lease provided that a lessee would have an option to extend the lease on terms set forth therein for 11 months; the lease provided that it was the lessee's choice whether to extend the lease. If the debtor tenant did not choose to exercise the option, it was not obligated to pay the additional rent claimed by the lessor. *In re Precision Tool Die and Machine Co., Inc.,* 339 B.R. 161 (Bkrtcy.W.D.Ky. 2006).

The bankruptcy court could sanction a sublessor for bad faith in filing a petition, despite the contention that the court lacked personal jurisdiction over him; the debtor-owner could recover reasonable attorney fees as a sanction against the sublessor, notwithstanding the sublessor's claim that the owner had "unclean hands" and the trustee could recover the full amount of his attorney time charges. *In re Rothchild's Jewelers, Inc.*, 337 B.R. 561 (Bkrtcy.E.D.Va. 2004).

Under Ohio law, land installment contracts are executory contracts that must be assumed or rejected in bankruptcy, even if the party holding legal title to the apartment complex may have lost its right to declare a forfeiture for the debtor-seller's failure to make installment payments. *In re Ravenswood Apartments, Ltd.*, 338 B.R. 307 (6th Cir. BAP 2006).

A bankruptcy court may not allow late proofs of claim filed by a Chapter 11 debtor's landlord for lease rejection damages, long after leases had been rejected and the claims bar date has expired. *In re Spiegel, Inc.*, 337 B.R. 816 (Bkrtcy. S.D.N.Y. 2006).

A debtor moved to assume executory contracts with Kmart Corp., and Kmart opposed the motion and cross-moved for relief from the automatic stay to terminate the executory contracts under an *ipso facto* termination clause. The court held that the other party to an executory contract could not enforce an *ipso facto* default clause in order to prevent assumption and performance of a contract by a Chapter 11 debtor-in-possession. *In re Footstar, Inc.*, 337 B.R. 785 (Bkrtcy.S.D.N.Y. 2005).

The bankruptcy court's finding that the debtor had adequate notice of a hearing on the creditor's motion to terminate the automatic stay did not rise to the level of clear error and would not be disturbed on appeal. *In re Harris,* 337 B.R. 921 (8th Cir. BAP 2006).

The phrase "terminated by the expiration of the stated term" as used in the bankruptcy statute provides that the automatic stay does not apply to any act by the debtor's lessor, including expiration under the terms of the lease based on post-default acceleration of the debtor's leasehold obligations and subsequent termination notice issued in accordance with the terms of the lease. *In re Southcoast Exp., Inc.*, 337 B.R. 739 (Bkrtcy.D. Mass. 2006).

The pre-petition conduct of the debtor's principals in knowingly concealing a contract to sell substantially all of the debtor's assets, while continuing to represent that the debtor's payments under the plan would be made out of profits derived in the ordinary course of the debtor's business, was sufficient to prevent confirmation of the debtor's amended plan as not having been proposed in good faith. *In re Proud Mary Marina Corp.*, 338 B.R. 114 (Bkrtcy.M.D.Fla. 2006).

A property owner was not entitled to an administrative expense claim for rent due under an alleged two-year lease agreement because such an agreement was void under the Statute of Frauds. Even if the agreement was enforceable, the property owner would not be entitled to recover rent that allegedly came due post-petition as an administrative expense of the debtor's estate. *In re Camelot Casino Cruises, Inc.*, 330 B.R. 263 (Bkrtcy.M.D. Fla. 2005).

Bankruptcy courts have the authority to abrogate certain lease provisions, including those prohibiting store closing sales on the premises, upon a proper evidentiary showing. In such a case, the landlords are entitled to additional adequate protection beyond regular rental payments. *In re Friedmans, Inc.*, 336 B.R. 880 (Bkrtcy.S.D.Ga. 2005).

A debtor's agreement with a creditor did not convert an ordinary debtor-creditor relationship into a trust or agency relationship so as to take the proceeds from the sale of the creditor's merchandise outside the bankruptcy estate. *In re Ames Department Stores, Inc.*, 144 Fed. Appx. 900 (August 2005).

Where the court holds that a lease is ambiguous about parking spaces available for restaurant patrons, neither the doctrine of merger nor the statute of frauds applies, and neither party was entitled to attorney fees. *In re Ranch House Motor Inn International, Inc.*, 355 B.R. 894 (Bkrtcy.M.D.Fla. 2006).

A lessor's nondisclosure of an agreement with the debtor for a reduction in post-petition rent did not prevent the lessor from asserting an administrative expense claim following rejection of the lease for post-petition, pre-rejection rent based on the rental rate set forth in the original lease. *In re Jillian's Entertainment Holdings, Inc.*, 336 B.R. 298 (Bkrtcy. W.D.Ky. 2006).

A ground lessor may be bound by the terms of a confirmed plan and cannot belatedly object to an alleged lack of prompt cure by the debtor-lessee. *In re Ali Properties, Inc.*, 334 B.R. 455 (Bkrtcy.D. Kan. 2005).

Condemnation/Eminent Domain

Local government may take over remediation when condemning contaminated property. *City of Olmsted Falls, Ohio* v. *United States Environmental Protection Agency*, 435 F. 3d 632 (6th Cir. 2006).

Including the probability of assemblage in establishing compensation does not require proof that the condemnee was likely to assemble the land with other parcels. *City of Norwich* v. *Styx Investors in Norwich, LLC*, 887 A.2d 910 (Conn.Ct.App. 2006).

Where the condemnation issue had previously been litigation in federal court, a property owner may be collaterally estopped from seeking higher compensation based on the value of his property in its prior uncontaminated state in state court. *Albahary* v. *City of Bristol*, 276 Conn. 426; 886 A.2d 802 (Ct. 2005).

A property owner had no cause of action for a *de facto* condemnation for interference with ingress and egress from a service station/mini-mart where a state interchange reconfiguration redirected traffic. *Sienkiewicz* v. *Commonwealth Dept of Transportation*, 883 A.2d 494 (Pa. 2005).

Enactment of the *New Jersey Highlands* Act did not constitute a taking of land that could not be developed due to failure to obtain a permit before a certain date, even though all the documents had been submitted prior to that date. *OFP, LLC* v. *State*, 2005 WL3058158 N.J. Super.Ct. (Nov. 15, 2005).

Absence of findings concerning "rough proportionality" in requiring dedication of land does not indicate that compensation is required. *Hammer* v. *City of Eugene*, 121 P.3d 693 (Ore.Ct.App. 2005).

A taking may occur when a regulatory delay affects less than all economically viable use of the land. *Byrd* v. *City of Hartsville*, 620 S.E.2d 76 (S.C. 2005).

Constitutional Law

The developer of an apartment complex failed to prove retaliation for political campaigning or equal protection violations in a city's rejection of the proposed apartment development. *Campbell* v. *Rainbow City*, 434 F.3d 1306 (11th Cir., Jan. 6, 2006).

Fees

A city's reenactment of a building permit and plan review fee structure modified the duration of the fee, entitling the developer to challenge the resolution under the state's mitigation fee act. *Barratt American, Inc.* v. *City of Rancho Cucamonga*, 124 P.3d 719 (Cal. 2005).

An impact fee calculation may be based on improvements for the entire service area. *City of Olympia* v. *Drebick*, 126 P.3d 802 (Wash. 2006).

Where a party lacks an objectively reasonable basis for a request for removal to federal court, attorney fees may be awarded to the other party. Fees may be reduced at the discretion of the court where the court finds the number of hours spent on the litigation excessive and unnecessary. *Harvard Real Estate-Allston, Inc.* v. *Kmart Corporation,* Kmart Store 9424, 407 F. Supp. 2d 317 (Mass. 2005).

Franchises

The district court granted a preliminary injunction to enjoin a franchisee from using the franchisor's proprietary trademarks and compelling him to cease operating the franchises immediately and honor the post-termination obligations as set forth in the parties' franchise agreements. The credible evidence demonstrated irreparable injury and, although the franchisee would suffer economic damages, they could be remedied in the underlying litigation regarding the franchise agreements. *GNC Franchising, LLC* v. *Sunil Masson and Vitamin Concepts, Inc.,* Civil Action No. 05-1613, United States District Court for the Western District of Pennsylvania, Dec.13, 2005.

Landlord & Tenant

In a series of cases involving a tenant's default and the landlord's confession of judgment, the landlord's claims were barred under *res judicata* where the landlord raised new claims in a second litigation that could have been raised in the first litigation. *Bell* v. *Bernicker,* No. 1904, Common Pleas Court of Philadelphia County, Pennsylvania, Civil Trial Division, Oct. 28, 2005.

Leases

The tenant commenced an action against the landlord, seeking declaratory relief regarding the rights and obligations of each of the parties under the lease because it believed that the landlord had incorrectly calculated the amount owed by the tenant for common area maintenance (CAM). The trial court entered a final order in favor of the landlord, based upon the theories of waiver and estoppel, holding that the tenant was not allowed to object to the landlord's methods for calculating CAM because it had not objected in the past. The appellate court reversed. It held that waiver and estoppel are affirmative defenses that must be pled. Because the landlord had failed to plead waiver and estoppel, those defenses were waived and should not have been the basis of the trial court's decision. *Louie's Oyster, Inc.* v. *Villaggio Di Las Olas, Inc.,* 915 So. 2d 220 (Ct. App. Fla. 4th Dist. 2005).

Although the lease did not specifically require the tenant to do so, a reasonable trier-of-fact could find that the tenant had breached the lease by failing to provide all necessary environmental reports to the state authorities because the lease required the tenant to comply with all applicable environmental laws. The court further considered that in light of the parties' course of conduct, it would be reasonable for the trier-of-fact to conclude that the tenant was responsible for dealing with all state environmental regulatory procedures. *Jaasma* v. *Shell Oil Company,* 412 F.3d 501 (3d Cir. 2005).

Signs/Billboards

A billboard company, which had suffered injury in fact based on one section of a sign ordinance, has standing to challenge the entire ordinance. *Tanner Advertising Group, LLC* v. *Fayette County, Ga.,* 411 F.3d 1272 (11th Cir. 2005) rehearing granted 429 F.3d 1012.

A billboard company cannot invoke the overbreadth doctrine to establish constitutional standing to challenge a sign ordinance. *Advantage Media, LLC* v. *City of Eden Prairie,* 405 F. Supp. 2d 1037 (Minn. 2005).

Tort Liability

A shooting occurred in a parking lot adjacent to a shopping center parking lot and nightclub. Generally, shopping center owners are not liable for the criminal actions of third parties, but a civil liability may arise in limited and specific circumstances where the criminal act was reasonably foreseeable to the owner. The police were called to the parking lot on a number of occasions because of the nightclub and the volume of people that the nightclub attracted. Furthermore, the neighborhood in which the nightclub was located had a shooting almost every weekend, and it was routine for the police to "keep an eye" on the nightclub every weekend. Here, the court concluded that there was a genuine issue of fact as to whether the owner should have reasonably foreseen criminal actions on the property. *Patton* v. *Stevenson Strogen et al.,* 908 So. 2d 1282 (La. Ct. App. 2d Cir. 2005).

Zoning

An environmental impact report, relying on "paper" water entitlements, was inadequate. *California Oak Foundations* v. *City of San Clarita,* 35 Cal.Rptr. 3d 434 (Cal.App.Ct. 2005).

The futility exception to the ripeness requirement did not apply to an owner's claim that the restrictive state land use ballot measure, as applied to the redevelopment of a rock quarry, was a regulatory taking. *County of Alameda* v. *Superior Court,* 34 Cal.Rptr.3d 895 (Cal.Ct.App. 2005).

Legislation

California:
—H.B. No. 1233 requires cities and counties to zone or rezone adequate sites to accommodate its share of regional housing need.
—S.B. No. 1087 requires providers of water and sewer services to establish standards for the provision of services for affordable housing.

Massachusetts:
—S.B. 2237 provides school cost reimbursement to cities and towns with smart growth zoning districts.

Michigan:
—S.B. No. 34 adopts the *Corridor Improvement Authority Act* to revitalize and finance deteriorating older business areas.
—H.B. 4369 enacts the *Commercial Rehabilitation Act*.
—S.B. No. 34 authorizes municipalities to establish corridor improvement.
—H.B. No. 4369 authorizes the commercial rehabilitation tax exemption.

New Jersey:
—A.B. No. 1633 lists Brownfields sites on the Internet.
—S.B. No. 320 amends the "Main Street" redevelopment program.

Pennsylvania:
—S.B. No. 881 limits eminent domain power.

Washington:
—S.B. No. 6574 restricts the power of eminent domain.

From Canada

In Depth

British Columbia Court of Appeal Confirms No Implied Right of Renewal

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In *Sultani v. Blenz, The Canadian Coffee Company Ltd.,* the British Columbia Court of Appeal considered a case in which a franchisee sought relief after discovering that his franchise agreement did not provide a right of renewal.

Mr. Sultani purchased an existing Blenz franchise that had been operated by the former franchisee pursuant to a 10-year franchise agreement. At the time Mr. Sultani purchased the franchise, there were approximately eight years left on the original franchise agreement. Although the franchise agreement did not provide for any right of renewal, Mr. Sultani initially sought an injunction and later proceeded with a claim for damages as a result of certain representations, which, he alleged, led him to believe that the franchise agreement could be renewed following its expiry.

Mr. Sultani appears to have believed that the franchise agreement was renewable, based on a statement in the advertisement of the franchise that the lease of the franchised premises contained an option to renew and a statement from a representative of Blenz. With respect to the statement by the representative of Blenz, the trial court stated:

> I accept the evidence of Ms. Moen on this point. Blenz had just told the plaintiff that it wanted a new franchise and sublease agreement rather than assign the old one. This is consistent with the business practice described by Ms. Moen. The suggestion of the plaintiff does not fit with either the contracts themselves or the business practice of the defendants …. Nikituk [the former franchisee] said that he was aware that there was an "opportunity for a further ten year term which he called a 'renewal.' On this basis, he had informed the broker and the plaintiff. While it was true that there was such an opportunity, it was not contracted and was subject to full negotiation involving the third party landlord as well as Blenz. It appears that this statement by the previous franchisee/vendor took on enhanced life in the mind of the plaintiff which he used to make assumptions and interpretations in his dealings with Blenz. Not once did the plaintiff directly ask about the term of the franchise or any renewal….

Notwithstanding Mr. Sultani's belief, neither the franchise agreement nor the sublease contained rights of renewal. As a result, when at the end of the 10-year franchise term, Blenz decided to take a new direction at the franchised premises, Blenz refused to renew or enter into any continued relationship with Mr. Sultani. In determining that no right of renewal existed, the trial court noted:

> There is no express right of renewal in the franchise agreement or sublease. When there is no right to renew or option to renew on ascertainable terms, no renewal is enforceable by the court …. Both the franchise agreement and sublease were in writing so that any pre-contractual representation not included in the written agreement is inadmissible under the parole evidence rule because it is inconsistent with the written agreement.

After confirming that the court will not imply a right of renewal into a franchise agreement (where no such right is contained in the express terms of a written agreement), the Court of Appeal went on to consider whether it ought to interrupt the trial decision on the basis of certain representations that Mr. Sultani argued contradicted the written language of the franchise agreement. Mr. Sultani based his argument in favour of giving effect to the alleged representations on *Zippy Print Enterprises Ltd.* v. *Pawliuk,* an earlier decision of the Court of Appeal, in which the Court refused to enforce an "entire agreement" clause where the franchisor had made "specific pre-contract representations on points of substance …with the intent to induce the making of the license agreement, unless the intended effect of the exclusion clause was pointed out to the respondents."

The Court of Appeal distinguished the decision in *Zippy Print* before going on to dismiss Mr. Sultani's appeal. In dismissing Mr. Sultani's appeal, the Court referred to "the general rule against giving effect to collateral agreements which contradict a written entire agreement clause," known as the Parole Evidence Rule. In considering the application of the Parole Evidence Rule, the Court of Appeal quoted from an earlier decision of the Court of Appeal with respect to the policy basis for such rule:

> … It is a normal and in my view legitimate expectation in the commercial world that, absent fraud or some other vitiating element, provisions such as [the entire agreement clause] will generally be given effect to, so that prior discussions concerning the contract may not prevail over what has been acknowledged in writing to constitute the parties' "entire agreement …."

The Court of Appeal went on to observe that "to give effect to the argument of the appellant in this case would be to allow an alleged parole representation to effect significant change to the franchise agreement and the sublease."

The *Sultani* v. *Blenz* decision is of importance to franchisors because it confirms that courts will not require a franchisor to renew a franchise agreement unless the franchise agreement specifically provides that the franchisee has a right to renew. The decision is also significant because, although it does not go so far as to overrule the decision in *Zippy Print,* it represents another step in a developing line of cases in British Columbia in which courts have shown a willingness to apply the Parole Evidence Rule to franchise agreements. In doing so, the courts have once again indicated that "absent fraud or some other vitiating element," franchisors ought to be able to enforce the terms of their written agreements.

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Enjoin the Picketers?

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In 2002, the Supreme Court of Canada ruled that picketing is a form of expression protected by the *Canadian Charter of Rights and Freedoms.* In so ruling, the Supreme Court of Canada made it clear that the lawfulness of picketing will be determined by the *conduct* of the picketers, not their location. Prior to this ruling, it was considered illegal *per se* for picketers to exert economic pressure on third parties, such as customers and suppliers, unless those third parties were "allies" of the employer. The distinction between primary picketing and "secondary picketing" (picketing at a location other than the premises of the employer whose employees are on strike) has now been abolished. Secondary picketing is permissible unless it can be shown to be wrongful or unjustified.

For companies that are third parties to labour disputes, it may be surprising that picketing of their premises is considered permissible. However, the laws of intimidation, trespass, nuisance and inducing breach of contract continue to apply to picketers, and picketers may not unduly impede access to or exit from the picketed premises. To minimize the potential for adverse impact upon its business, a company threatened with picketing action should focus on preparing an appropriate contingency plan and on gathering evidence of unlawful conduct. With evidence of unlawful conduct, including threats and undue prevention of access to the company's premises, an injunction may still be available.

This article provides basic information a company should consider in the event that picketing threatens to disrupt its business. It should be noted that each situation is unique, and legal advice should be obtained in the event that a company receives notice its business may be disrupted as a result of picketing.

I. Is Injunctive Relief Available to Restrain Picketing?

Injunctive relief may be available if the picketing involves conduct that is tortious or criminal. A company does not have an automatic right to enjoin picketing activities, even where there is considerable negative economic impact to its business. Therefore, a company's success in obtaining an injunction depends on how successful the company is in gathering evidence of the picketers' criminal or tortious conduct.

II. General Test for an Injunction to Restrain Picketing

To obtain an injunction, the company should be able to show (i) a strong *prima facie* case that the picketers have been participating in unlawful behaviour, (ii) that damages are an inadequate remedy, and (iii) that the balance of convenience favours granting an injunction.

When injunctive relief is being sought from picketing, the first element, that of a *prima facie* case, is generally determinative. As noted above, the distinction between primary and secondary picketing has been effectively abolished. Consequently, proceedings for injunctions with respect to the primary and secondary forms of picketing are held to the same test.

A. The company has a strong prima facie *case that the picketers have been participating in unlawful conduct.*

Since picketing is not itself unlawful, a company must establish a strong *prima facie* case to prove that the picketers have engaged in criminal or tortious conduct in order to seek injunctive relief. When relying on allegations of tortious behaviour, the company must ensure that its allegations are specific and, if proven, would meet the relevant test for the alleged criminal offence or tort.

1. Differentiating Between Lawful and Unlawful Picketing

(a) *Lawful Picketing Activities*—Lawful picketing may include picketing for the purpose of communicating information, obtaining information or peacefully persuading employees to support the picketers' position. It is not unlawful for large numbers of picketers to be involved.

(b) *Unlawful Picketing Activities*—Unlawful picketing usually includes tortious behaviour (e.g., intimidation, inducing breach of contract, defamation, etc.) or criminal behaviour. Specifically, unlawful picketing may include:

- Trespassing on private property (unless the property is one in which the public is normally granted access);
- Conduct that is disorderly (not peaceful);
- The use of force or threats;
- Damage to property;

- Oral or written communication that is slanderous or libelous;
- Unduly hindering access or egress from the premises;
- Any type of picketing that prevents patrons, suppliers or employees from entering the premises; or
- Threatening patrons, suppliers or employees with injury or damage to personal property.

2. Commonly Relied on Torts When Seeking Injunctive Relief From Picketing
As noted above, injunctive relief is generally available only if the conduct of the picketers involves tortious or criminal activity. Canada's Supreme Court has stated that picketing is not permissible if it breaches the criminal law or one of the specific torts such as trespassing, nuisance, intimidation, defamation or misrepresentation. Companies may also receive basic protections through the tort of interference with contractual relations. The more commonly relied on torts are described in some detail below:

Nuisance—Picketing activities that amount to the tort of nuisance are unlawful. Nuisance consists of a substantial and unreasonable interference with an occupier's interest in the beneficial use of his or her land. In order for the tort of private nuisance to be made out, the nuisance must involve private property. For the tort of public nuisance to be made out, there must be some damage beyond the general damage of inconvenience.

Defamation—The use of injunctive relief to restrain defamation is permissible only in the rarest and clearest of cases, where the defamation is so manifestly defamatory that any verdict to the contrary would be considered perverse. There also must be evidence—or grounds upon which to infer—an intention that the defamation would be repeated or published.

Interference With Contractual Relations—The elements of the tort of interference with contractual relations include: (i) the existence of a valid and enforceable contract, (ii) awareness by the defendants of the existence of a contract, (iii) breach of the contract procured by the defendants, (iv) wrongful interference and (v) damages. This tort can only be established in the context of picketing if the interference is caused by an independently actionable wrongful or unlawful act.

3. Examples of Where Courts Have Granted Injunctive Relief
Injunctions have been granted to prevent picketing in the following situations:

- Where the conduct of picketers in denying entry or exit to the picketed premises constituted the tort of nuisance and criminal mischief (the court found that undue delay of persons seeking to enter or exit the premises is unjustified and that picketers do not have an unrestricted right to a blockade of the picketed premises);
- Where picketing involved the use of signs alleging that the picketed group committed criminal offences and were disseminators of communicable diseases (only the unlawful activity was restrained and other picketing activities were permitted);
- Where the picketers impeded access to the courts; and
- Situations where the safety of picketers or others is threatened.

A. The company will suffer irreparable harm that cannot be compensated by damages if an injunction is denied.
In cases where tortious or criminal actions are shown to have occurred, irreparable harm is readily established and compensation by damages is not realistically an available option. Irreparable harm includes harm to the public, as well as harm to the picketers themselves. Excessive economic harm can be irreparable harm, but the Supreme Court of Canada has held that even evidence of considerable economic harm to third parties will not justify restraint on otherwise lawful picketing activities.

B. The balance of convenience favours the granting of the injunction.
Where there is evidence that the picketing conduct is unlawful, the company does not have to meet this part of the test. However, in order to minimize impact and to further balance the convenience, injunctive relief granted may be limited in nature. The court will not interfere with lawful, non-tortious and non-criminal picketing. Rather, it is only the unlawful conduct that is in need of prohibition in order to impact the rights of the picketers as minimally as possible. The wide, injunctive relief requested by a moving party may be denied in favour of an order restraining only the wrongful actions of the picketers.

III. How to Seek Injunctive Relief

A. Steps Relevant to Any Motion for an Injunction to Restrain Picketing

1. Gather First-Hand Accounts of Any Wrongful Conduct
In advance of seeking an injunction, evidence should be gathered from as many first-hand sources as possible. Whether or not injunctive relief will be granted is dependent upon whether the party seeking the relief has put forward sufficient evidence that the picketing is wrongful and unjustified.

2. Make Reasonable Efforts to Obtain Police Assistance

Prior to initiating proceedings to seek injunctive relief, the court must be satisfied that reasonable efforts were made by the moving party to "obtain police assistance, protection and action to prevent or remove any alleged danger of damage to property, injury to persons, obstruction of or interference with lawful entry or exit from the premises in question or breach of the peace have been unsuccessful." Supporting materials, in the form of affidavits confined to statements of fact within the knowledge of the deponent, will be required for such a motion to be made. While it is not absolutely clear that this requirement applies to secondary picketing activities, out of an abundance of caution, the police should be contacted in all circumstances.

B. Picketing Activities With No Connection to a Labour Dispute

Where the picketing activities occur at the premises of a company with no connection to a labour dispute, injunctive relief can be sought through a motion under Section 101 of the *Courts of Justice Act.* Where there is any suggestion that a labour dispute may be underlying the picketing activities, a telephone call to the appropriate labour representatives is required prior to seeking injunctive relief.

C. Picketing Activities Arising in Connection With a Labour Dispute

Where the secondary picketing arises in connection with a labour dispute, a company must consider whether or not the additional requirements found in Section 102 of the *Courts of Justice Act,* R.S.O. 1990, c. C.43, are applicable.

Section 102 applies to picketing "in connection with a labour dispute." The scope of what will be considered to be "in connection with a labour dispute" is not yet settled. At least one Ontario court has suggested that neutral parties should not have to meet the additional requirements in Section 102 when seeking injunctive relief; however, the court held that where there is a close interrelationship with the picketed third-party company and the struck employer, the picketing is "in connection with a labour dispute." It should be noted that the trend in Canadian courts has been to favour the rights of striking employees during labour disputes. Caution dictates that, where circumstances permit, companies subjected to secondary picketing comply with the additional requirements of Section 102.

In addition to meeting the general requirements described above for obtaining injunctive relief, a company seeking to restrain conduct "in connection with a labour dispute" has additional obligations.

1. Shorter Period Permitted for Interim Injunctions Restraining Picketing in Labour Disputes

It should be noted that under Section 102, an interim injunction will only be granted for a maximum of four days.

2. Notice Requirements

(a) The general rule is that at least two days' notice is required before a motion for an injunction. Notice to a union can be effected by personal service on an officer or agent of the union. If the picketing employees are not members of a union, notice can be given by posting the notice in a conspicuous place at the place where the picketing occurs, where it can be read by any persons potentially affected.

(b) To seek an injunction **without notice,** the following must be established through oral evidence of relevant material facts:

(i) It is a proper case for an interim injunction;

(ii) Notice could not be given because the delay would cause irreparable damage or injury, a breach of the peace or an interruption in an essential public service; and

(iii) Reasonable notification (by telephone or otherwise) has been given to an officer of the labour organization.

3. Evidence

Where an injunction is sought in connection with a labour dispute, affidavit evidence submitted by the company must be confined to the personal knowledge or opinion of the deponent, and not based on his or her information and belief. Evidence from security guards, management and police should be provided. In addition, an injunction is more likely to be granted if the company can link a relatively large proportion of the picketers to the unlawful or inappropriate conduct. If the conduct can be viewed as simply bad behaviour on the part of a few individuals, an injunction restraining the picketing is unlikely to be granted.

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Canadian Division Report on Legislative and Judicial Developments

I. GOVERNMENT RELATIONS GENERALLY

A. *Parking Tax*

1. Quebec

ICSC, in collaboration with The Capital Hill Group, has worked with the Quebec Coalition Against the Parking Tax. The City of Montreal continues to push for this taxing power; however, we understand that the Province does not currently favour new or additional municipal taxing powers. With assistance from ICSC consultant, The Capital Hill Group, the Coalition has an action plan targeting the Quebec Government at both the Executive and the Legislative levels as, and when, required.

2. British Columbia

ICSC, led by Ted Williams of Ivanhoe Cambridge and others, and with support from consultants WPC, is continuing in the West Coast fight against the Vancouver parking tax. While the parking tax has been implemented in Vancouver, Ted and his colleagues have been successful in persuading Translink, the beneficiary of the tax, to conclude that the current Vancouver parking tax is an ineffective and inappropriate method of financing the Translink RAV mass transportation line. Translink has adopted a resolution to terminate the tax as soon as alternate and appropriate funding becomes available.

B. *Canada Interest Act*

Fred Carsley of De Grampré Chait is working with ICSC consultant, The Capital Hill Group, to lobby the Federal Government to adopt changes to the *Interest Act* (Canada) to better facilitate longer-term mortgage financing in the Province of Quebec for REITs (real estate investment trusts).

II. PROVINCIAL REPORTS

1. British Columbia

a) Legislative Developments

See above—Parking Tax

b) Case Law

Randy Klarenbach of Richards Buell Sutton, and Blake Hudema of Hudema Consulting Group Ltd., report on the following cases:

- *Lonsdale Quay Market Corp.* v. *Jamshidian (c.o.b. Gam Shoe Repair & Quality Leather)*, North Vancouver Registry No. 0416147
  This case involved an action over seized property. The tenant ran a shoe repair business in the landlord's shopping centre but was in arrears for much of its term. The landlord agreed to abate the rent and arranged to relocate the tenant. The tenant indicated it could not continue, and the landlord advised the tenant to reopen in 24 hours but the same day distrained and seized the tenant's equipment. The judge held that the landlord had no written evidence that the tenant agreed to the relocation or was given sufficient notice; as a result, the landlord was in breach, which rendered the termination and distraint illegal. The tenant was entitled to a refund of security deposit to be offset against the rent owing.

- *Morguard Investments Ltd.* v. *British Columbia* (Assessor of Area No. 12—Coquitlam), Vancouver Registry No. CA032346
  The tax assessor appealed a decision which determined that HBC and Zellers had standing to appeal a tax assessment as tenants in a shopping centre operated by Morguard. As a result of a tax assessment, Morguard increased the amount payable by HBC and Zellers under their leases. The assessor argued that HBC and Zellers were not persons affected within the certain definitions governing tax assessments. The court of appeal reasoned that as tenants who had to pay the taxes assessed to Morguard, HBC and Zellers were persons affected by the assessment decision and were more than interested members of the public.

- *Royal City Shopping Centre Ltd.* v. *Canadian Direct Insurance Inc.*, 145 A.C.W.S. (3d) 511
  Royal City leased premises to CDI with a right to renew, which required written notice of not less then nine months. CDI sent a letter stating it wished to renew "subject to satisfactory negotiation of the lease terms." Royal City took the position that the letter was not sufficient. The court held that the letter did not create a binding renewal. As the letter was ambiguous, the facts needed to be considered. The court noted that CDI was looking for other premises, and

only expressed a willingness to negotiate with Royal City. Royal City had, in fact, commenced negotiations; however, only after negotiations broke off, did CDI seek to enforce the renewal.

2. Alberta

Howie Sniderman of Witten LLP has no **legislative developments** to report for Alberta.

a) Case Law

Murray Tait of T&T Properties reports on the following cases:

- *581834 Alberta Ltd.* v. *Alberta (Gaming and Liquor Commission)*, 2006 ABQB 47 (CanLII), Alberta Court of Queen's Bench, Jan. 16, 2006, Langston, J.
  The subtenant sought damages against its sublandlord for breach of the covenant of quiet enjoyment contained in the sublease agreement. The head tenant leased premises from the landlord for a term of 40 years. Twenty years later, the subtenant subleased those premises from the head landlord at very favourable rent.

  The sublease contained a covenant of quiet enjoyment. At the time of this sublease, there was a mortgage registered on the shopping centre, which contained the subleased premises; however, no non-disturbance agreement had been given by the mortgagee to the head tenant. The mortgage company of the shopping centre foreclosed on the landlord. The mortgage company was granted possession of the subleased premises to the exclusion of the head tenant and the subtenant. In order to remain in the subleased premises, the subtenant negotiated a new lease with the mortgage company at an increased rate.

  The subtenant then commenced an action for damages against the head tenant for breach of the covenant of quiet enjoyment. The court concluded that where interference occurs between a tenant or subtenant, and that interference is by someone superior in title, no relief can be claimed under the covenant of quiet enjoyment. Here, the covenantor was the head tenant; however, the defaulting party was the head landlord. The head landlord is superior in title to the head tenant, and the head landlord does not claim by, through or under the head tenant. The subtenant's sublease was extinguished by the mortgage company's foreclosure. The mortgage company is also superior in title to the subtenant, and the mortgage company obtained title in its own right—not by, through or under the head tenant.

  The court commented that it could not escape the conclusion that it would have been prudent for the subtenant to examine both the title to the shopping centre and the head lease in order to properly engage its exposure to risk. In particular, the court noted that the subtenant failed to ascertain whether a non-disturbance agreement had been given by the mortgage company to the head landlord. As the interference suffered by the subtenant was not caused by the head tenant, or any person claiming by, through or under the head tenant, the head tenant did not breach the covenant of quiet enjoyment.

- *623729 Alta. Ltd.* v. *Alldritt Development Ltd.*, 2006 ABQB 358 (CanLII), Alberta Court of Queen's Bench, May 15, 2006, Moreau, J.
  There was a dispute between the landlord and the tenant of premises in an office building. The tenant argued that it was only required to pay rent (and additional rent) on the actual rentable area, which did not include the building gross-up factor. The lease provided as follows:

  > …certain premises situated on the main floor of the Building containing an area of approximately Four Thousand Four Hundred (4,400) square feet as shown outlined in red on Schedule "A" (in this Lease referred to as "the Demised Premises" or "the demised premises") measured in accordance with the BOMA standard of measurement.

  The rental provision of the lease provided that the basic rent was calculated on the area of the demised premises being 4,400 square feet (sf) and that "the Basic Rent shall be adjusted in the event that the actual area of the Demised Premises shall differ from the aforesaid area."

  The landlord had the premises re-measured and grossed up in accordance with BOMA standards. However, the evidence was clear that this certificate of measurement containing the calculation of the gross up was never forwarded to the tenant. Subsequent to signing the lease, the parties entered into a lease renewal and amending agreement for a period of five years. Pursuant to that agreement, the basic rent was to be determined "based on 4,362.5 square feet as the area of the Demised Premises." That amending agreement also provided that all other terms of the lease would remain in full force and effect.

  The landlord argued that the lease was ambiguous. The landlord could, therefore, use extrinsic evidence, such as the inclusion of the actual grossed-up area in the lease-amending agreement, and the area certificate, to substantiate that the area of the demised premises on which the tenant was obligated to pay rent was to be the grossed-up area. The tenant argued that the lease was not ambiguous and, therefore, there was no need to reference extrinsic evidence. The tenant argued that the rent provision of the lease was specific and provided that the rent was to be based upon the "actual area" of the demised premises. The court concluded as follows:

1. The lease contained no ambiguity. The lease clearly indicated that the demised premises have an area of approximately 4,400 sf "as shown outlined in red on Schedule 'A.'" The area outlined in red on Schedule A to the lease was the actual area of the leased space. The rent covenant provided that the basic rent may be adjusted if the actual area of the premises (the actual area shown outlined in red on Schedule A to the lease) differed from the 4,400 sf. The actual area of the premises was to be measured in accordance with the BOMA standard. The lease made no reference to "rentable area," to "total leasable area" or to "usable area." The lease only dealt with the "actual area," which was the area specifically outlined in red on Schedule A to the lease, as the basis for the calculation of rent.

2. Although the lease-amending agreement reduced the square footage, it did not operate to exclude the opportunity for the tenant to seek rental adjustment based upon the "actual area" of the demised premises, as shown outlined in red on Schedule A.

3. The provisions of the lease with respect to the calculation of the basic rent were not ambiguous, rent was to be paid based upon the actual area of the leased premises, and additional rent calculated accordingly.

   The court granted judgment in favour of the tenant.

3. Saskatchewan

a) Legislative Developments

R. Neil Mackay of MacPherson Leslie & Tyerman LLP reports that *The Miscellaneous Statutes (Directors' and Officers' Indemnification and Insurance) Amendment Act, 2006; The Miscellaneous Statutes (Directors' and Officers' Indemnification and Insurance) Amendment Act, 2006 (No. 2);* and *The Interpretation Amendment Act, 2006,* received Royal Assent on May 19, 2006, and are now in force.

These acts provide for parallel amendments to the indemnification and insurance-related provisions for officers and directors in *The Interpretation Act, 1995; The Business Corporations Act; The Non-Profit Corporations Act, 1995; The Co-Operatives Act, 1996; The New Generation Co-Operatives Act; The Credit Union Act, 1998;* and *The Crown Corporations Act, 1993.*

Among other things, the acts provide that directors and officers have complied with their duty of care if they rely in good faith on financial statements, representations made by an officer, a written report of the auditor or other professional person (e.g., lawyer, engineer, accountant) who is competent to give advice with respect to the matter. The acts also provide new provisions relating to indemnifying and ensuring officers, directors and other persons.

b) Case Law

- *Brennan* v. *Brennan Educational Supply Ltd.* 2006 SKCA 9

The landlord replaced three of seven natural gas furnaces following the tenant's failure to act on an annual inspection that called for the replacement of the furnaces. During the first year of the term, the furnaces developed cracks in their heat exchangers and required replacing. The landlord sought to enforce a covenant in the lease requiring the tenant to pay the cost of maintaining and repairing the plant and equipment supplying climate control to the premises.

The tenant refused to reimburse the expense on the basis that the condition of the furnaces amounted to a structural defect, the repair of which was the responsibility of the landlord. At trial, the landlord's action for judgment was dismissed. Although the lease did not expressly state that it was a "net lease," it bore many of the indicia of such an agreement. Under the lease, the tenant covenanted to pay the cost of "maintaining, operating and repairing" the premises, excluding the cost of "structural and roof repairs" but specifically including the cost of maintaining and repairing "the plant and equipment supplying climate control." The lease included an acknowledgment by the tenant that it had examined the premises, as a condition precedent to entering the agreement, and was satisfied with the physical condition of the premises.

The Court of Appeal noted that the furnaces were in a state of good repair when the lease started and fell into a state of disrepair during the term. The natural and ordinary meaning of the word "repair" is to restore something damaged, worn or faulty to good condition. The furnaces were clearly a component part of the equipment supplying climate control, which the tenant covenanted to maintain and repair. Because the furnaces were but component parts of the heating system, the replacement of the furnaces was included in the tenant's obligation to maintain the climate control system.

The Court of Appeal declined to imply a term of the lease that the landlord was obligated to provide an adequate supply of heat, as such an implied term would contradict the tenant's obligation to bear the cost of maintaining and repairing the climate control system.

The Court of Appeal found the tenant liable for the cost to replace the furnaces.

- *McLaren* v. *Brock (Rural Municipality No.64)* 2006 SKQB 222

  McLaren applied for an order quashing an expropriation by-law enacted by the Rural Municipality of Brock ("Brock"). McLaren owned land that was adjacent to a municipal road on the eastern boundary. There was no road access to the property to the west of the McLaren property. Historically, the owners of the neighbouring property accessed their land by a trail across the south boundary of McLaren's property. However, when a dispute arose between McLaren and the neighbour's spouse regarding an outstanding account, McLaren erected a fence that cut off access to the neighbouring land.

  The Rural Municipality offered to purchase a strip of McLaren's land for the purpose of creating access to the neighbouring lot. McLaren refused to sell, but did suggest alternative solutions including an access easement or access through property owned by other persons. McLaren further stated that he would not negotiate further until the issue of the outstanding account was resolved.

  The Rural Municipality enacted an expropriation by-law to take a portion of McLaren's property in order to provide access to the neighbouring land. The court reviewed the conditions for a valid municipal expropriation: (1) the municipal council must desire the land; (2) it must be for a purpose authorized by the applicable municipal legislation; and (3) it must be shown that the municipality was unable to acquire the land from the owner by agreement. The court concluded that all of these conditions were satisfied and declined to quash the by-law.

- *Jen-Sim Cattle Co Ltd.* v. *Agricultural Credit Corp of Saskatchewan* 2006 SKQB 173

  In 1985, three parties entered a loan agreement with the Bank of Nova Scotia (the "Bank") pursuant to which money was advanced to their company, V. Jensen & Sons Cooperative Stockfarm Limited. The loan was guaranteed by the Government of Saskatchewan and secured by a collateral mortgage against various parcels of land.

  In December 1989, some of the land was transferred to Barry Jensen ("Jensen") subject to the bank's mortgage. After the transfer, the loan went into default, the bank requested payment from the provincial government and the bank's interest was assigned to Agricultural Credit Corporation of Saskatchewan ("ACS"). A transfer of mortgage was registered against the title on June 1, 1993.

  On June 25, 2001, *The Land Titles Act, 2000*, came into effect. That act provided for the computerization of the land titles system in Saskatchewan. The title to the land owned by Jensen was converted to the new computer-based system on Sept. 16, 2002.

  Under the new act, transfers of mortgages are not registered on title. Rather the name of the mortgage holder is changed to that of the transferee. When the title was converted, the Information Services Corporation of Saskatchewan ("ISC") failed to change the name of the registered mortgage holder. Accordingly, after conversion, the title showed the bank as the mortgage holder rather than ACS.

  Jensen subsequently transferred the property to the Rural Municipality of Prince Albert (the "R.M.") in satisfaction of a tax lien, but retained the right to redeem the property if he paid the tax arrears and costs within 30 days of transferring the property to the R.M.

  The R.M. requested and obtained a discharge of the mortgage from the bank. The discharge and Transfer Authorization were registered concurrently so that the R.M. obtained title to the property free and clear of any registered encumbrances. Jensen then arranged for redemption of the property with money from Jen-Sim Cattle Co Ltd. ("Jen-Sim") and the R.M. executed a Transfer Authorization in favour of Jen-Sim. ACS subsequently searched the title to the property and discovered that its mortgage was no longer registered against the title. Prior to the registration of the Transfer Authorization in favour of Jen-Sim, ACS re-registered its mortgage. Jen-Sim applied to have the ACS mortgage discharged from title.

  The court addressed the issue of whether the principle of indefeasibility applied in this case. The court noted that in Saskatchewan, the governing principle has always been one of "immediate indefeasibility." The opportunity for rectification of title is lost once a transfer has been registered. At the moment of transfer, the transferee becomes immediately entitled to the indefeasibility protection of the Torrens system. Therefore, the R.M. obtained title free and clear unless ACS could show its interest was an exception to the principle of immediate indefeasibility. The court concluded that ACS could not establish any express or implied exceptions. As a result, the court directed the registrar of land titles to discharge the mortgage that had been re-registered by ACS.

4. Manitoba

a) Legislative Developments

Glen R. Peters of Fillmore Riley LLP reports that there are two recent City of Winnipeg by-law amendments that may be of interest to members:

1. *Fire Prevention By-law No. 150/2004* ("150/2004")
   By-law No. 30/2006 amends No. 150/2004 by adding the following penalty section:
   60.1 The owner of a building, or his or her agent, who fails to comply with:
   (a) Section 28 of this By-law, by allowing inoperable smoke alarms to exist in residential rental units;
   (b) Subsection 30(1) of this By-law, by failing to install and maintain at least one acceptable smoke alarm in every residential rental unit;
   (c) Subsection 40(1) of this By-law, by failing to ensure that a fire alarm system is operable at all times;
   (d) Sentence 2.4.1.1(1) of the Manitoba Fire Code, by allowing combustible materials to accumulate in and around the building in quantities or locations that constitute an undue fire hazard;
   (e) Article 2.7.1.6 of the Manitoba Fire Code, by failing to ensure that means of egress is maintained in good repair and free of obstructions; or
   (f) An order to remedy a contravention issued pursuant to this By-law; is guilty of an offence and liable upon summary conviction to a fine of not less than $500.00 or to imprisonment for a term of not more than six months, or both.

2. *Business Tax Rates By-law No. 107/2006* ("107/2006")
   By-law No. 107/2006 sets and imposes the 2006 rates of business tax as follows: For the Downtown Class (as defined in the Downtown Winnipeg Zoning By-law No. 100/2004) is set at 7.75%; The Other Premises Class (being everything except the Downtown Class) is set at 9.75%.

b) Case Law Developments

- *Chris Voulgaris v. Heartwood Construction Ltd. et al. 2006 MBQB 52*
  One of the defendants, Merit Properties Ltd. ("Merit"), was the owner and manager of a strip mall (the "Mall"). During the period in question, certain construction work was occurring at the Mall, which resulted in cardboard debris piled at one end of the Mall. Some of the cardboard had slipped into the parking area. It was subsequently found that the defendant slipped and fell on a piece of the cardboard in the parking area and sustained various injuries.

The court found that the issue was whether Merit was liable, in whole or in part, as an occupier of the Mall. It held that Merit was 40% liable (Heartwood, the contractor was 60% liable for creating the dangerous circumstances).

The court stated:

> Merit was an occupier within the meaning of *The Occupiers Liability Act* and the duty of an occupier is to take reasonable care in the circumstances to make the premises safe. That duty does not change but the factors which are relevant to an assessment of what constitutes reasonable care will necessarily be very specific to each fact situation—thus the proviso "such care as in all circumstance of the case is reasonable." See *Waldick* v. *Malcolm.*

The court found that Merit did maintain the surface of the parking lot in good shape, and had systems in place to ensure that snow was removed and that it was properly sanded. However, the court said that Merit did not take appropriate steps to guard against the hazard created by the construction of leaving debris in the parking area. The court stated the following regarding the debris:

> But they were certainly aware that construction activity was going on and they might reasonably have anticipated at least the possibility that this activity would generate garbage or debris. Notwithstanding they apparently took no steps to ascertain what measures the contractors might have in place to contain the debris and did not seek to impose any requirements on the tenant or its contractor in this regard. Nor did they take any active measures themselves to guard against the type of hazard which resulted in the accident in question. On the contrary, their attitude seemed to be—and Mr. Hamburg testified in this vein—that everything was left up to the tenant and the contractor; it was all their responsibility. That might be a reasonable enough attitude to take with respect to the tenant and the contractor but it did not detract from Merit's affirmative duty as an occupier to itself take reasonable steps to keep the premises safe. That was not a duty which could be transferred to others…."

5. Ontario

a) Legislative Developments

Stephen Messinger of Minden Gross Grafstein and Greenstein LLP reports the following:

1. *Bill 42—Eastern Ontario Economic Development Fund Act*

The Bill underwent a First Reading on Dec. 1, 2005. The Second Reading was debated and carried May 4, 2006. The Bill has been referred to the Standing Committee on Finance and Economic Affairs.

The Bill enacts the *Eastern Ontario Economic Development Fund Act, 2005.* The act establishes the Eastern Ontario Economic Development Fund Corporation, which is required to establish and maintain the Development Fund. The Corporation can use money in the Fund to further its objects, which include promoting the economic development of rural areas and smaller urban municipalities in Eastern Ontario—for example—by providing financial assistance to persons or bodies that carry on business in that region or to municipalities that are located in that region. That region is defined to be the area covered by the City of Kawartha Lakes and the counties of Northumberland, Peterborough, Haliburton, Hastings and Renfrew, together with all points in Ontario east of that area, but excluding cities with a population of more than 200,000 inhabitants.

2. *Bill 43—Clean Water Act*

   The Bill underwent a First Reading on Dec. 5, 2005. The Second Reading was debated April 12, and May 3, 15 and 17, 2006, and carried on division May 18, 2006. The Bill has been referred to the Standing Committee on Social Policy.

   The Bill amends the *Building Code Act, 1992,* by permitting the Lieutenant Governor in Council to establish maintenance inspection programs administered by principal authorities to enforce certain standards that are prescribed under the building code in relation to sewage systems. The amendments also allow principal authorities to establish other maintenance inspection programs.

   The *Planning Act* is also amended to permit local municipalities to pass zoning by-laws prohibiting the use of land and the erection or use of buildings on land that contains a sensitive groundwater feature or a sensitive surface water feature, or that is within an area identified as a vulnerable area in a drinking water source protection plan that has taken effect under the *Clean Water Act, 2005.*

3. *Bill 45—Occupational Health and Safety Amendment Act (Harassment)*

   The Bill underwent a First Reading on Dec. 6, 2005.

   The Bill amends the *Occupational Health and Safety Act* to require employers to protect workers from harassment in the workplace, to give workers the right to refuse to work in certain circumstances after harassment has occurred, to require an investigation of allegations of workplace-related harassment and to require employers to take steps to prevent further occurrences of workplace-related harassment.

4. *Bill 53—Stronger City of Toronto for a Stronger Ontario Act*

   The Bill underwent a First Reading on Dec. 14, 2005. The Second Reading was debated Feb. 13 and 27, and April 4 and 10, 2006. On April 10, 2006, the Bill was carried and referred to the Standing Committee on General Government, and was ordered for a Third Reading May 30, 2006. The Third Reading was debated June 6, 2006.

   The Bill enacts the *City of Toronto Act, 2006,* which is set out in Schedule A. The Bill also amends various public acts in respect of municipal matters, and those amendments are set out in Schedule B.

   A new Section 62.1 of the *Liquor Licence Act* authorizes the City of Toronto to pass by-laws extending the hours of sale of liquor by licence holders in all or part of the City. A city by-law prevails over a regulation made under the act. Subsection 6(2) of the act is amended to provide that an applicant for a licence to sell liquor is not entitled to the licence if the applicant is carrying on activities that contravene such a city by-law.

5. *Bill 57—Land Rights and Responsibilities Act*

   The Bill underwent a First Reading on Feb. 15, 2006.

   The Bill amends the *Expropriations Act and the Human Rights Code* to enhance the protection that Ontario law gives to owners of land and persons with respect to their homes.

   Under the *Expropriations Act,* an inquiry officer on an inquiry is required to consider the merits of the objectives of the expropriating authority and to add, as parties to an expropriation inquiry, the owners of all lands affected by the expropriation. The decision of an approving authority is subject to judicial review, reports Deborah Watkins of Daoust Vukovich LLP.

   The amendments to the *Human Rights Code* recognize, subject to specific limitations at law, the right to peaceful enjoyment of one's land, the moral responsibility to maintain it, and the right to freedom from search of one's property and home and from seizure of anything from it. Those rights have long been recognized at common law but are largely missing from the *Canadian Charter of Rights and Freedoms.*

6. *Bill 59—Visual Fire Alarm System Act*

   The Bill underwent a First Reading on Feb. 13, 2006. The Second Reading was debated and carried on division Feb. 16, 2006. The Bill has been referred to the Standing Committee on Legislative Assembly.

The Bill requires that all provincial and municipal public buildings be equipped with a visual fire alarm system so that deaf and hearing impaired people are alerted to fire alarms.

7. *Bill 85—More Time to Appeal Act*

   The Bill underwent a First Reading on March 29, 2006. The Second Reading was debated and carried March 30, 2006. The Third Reading was carried March 30, 2006. The Bill received Royal Assent on March 31, 2006.

   Currently, subsection 40 (2.1) of the *Assessment Act* specifies that the deadline for delivering a complaint to the Assessment Review Board with respect to a taxation year is March 31 following the return of the assessment roll for the taxation year. This Bill amends Section 40 to extend that deadline to June 30, 2006, for complaints with respect to the 2006 taxation year.

8. *Bill 95—Employment Statute Law Amendment Act (Informing Students of their Employment Rights)*

   The Bill underwent a First Reading on May 31, 2006. The Bill amends the *Employment Standards Act, 2000,* and the *Occupational Health and Safety Act* to require employers to give their student employees specified information about both acts by posting a poster in workplaces and providing copies of a booklet.

9. *Bill 98—Increase in Electricity Consumption Reporting Act*

   The Bill underwent a First Reading on April 10, 2006.

   The Bill enacts the *Increase in Electricity Consumption Reporting Act, 2006.* The act requires that every person who causes a building to be constructed report the anticipated annual electricity use, in the case of a new building, or the annual increase, if any, in electricity use in a building that is being extended, materially altered or repaired.

10. *Bill 100—Protection of Minors From Sexually Explicit Goods and Services Act*

    The Bill underwent a First Reading on April 11, 2006. The Bill prohibits a person from knowingly selling, offering to sell, distributing, offering to distribute or displaying sexually explicit goods or services to a minor in any premises or place. The prohibition does not affect communications delivered directly and exclusively to a private residence if the residence is not open to the public. It is an offence to contravene or to fail to comply with the prohibition.

11. *Bill 119—Employment Standards Amendment Act (Wage Security)*

    The Bill underwent a First Reading on Feb. 15, 2006. The Second Reading was debated and carried March 2, 2006. The Bill has been referred to the Standing Committee on Justice Policy.

    The Bill amends the *Employment Standards Act, 2000,* by adding Part XV.1, which establishes the Employee Wage Security Program and provides for the appointment of a Program Administrator. Under the Program, employees will be eligible for compensation for certain types of unpaid wages.

12. *Bill 120—Fire Protection Statute Law Amendment Act*

    The Bill underwent a First Reading on June 1, 2006.

The Bill amends the *Building Code Act, 1992,* and the *Fire Protection and Prevention Act, 1997,* to provide that regulations made under each of those acts, known, respectively, as the Building Code and the Fire Code, ensure that every fire escape is constructed of non-combustible material.

Status of Bills (Ontario) Previously Reported

1. *Bill 21—Energy Conservation Responsibility Act*

   The Bill was carried on division and referred to the Standing Committee on Justice Policy Dec. 13, 2005. The Third Reading was debated on Feb. 20 and 23, 2005, and debated and carried on Feb. 27, 2005. The Bill received Royal Assent on March 28, 2006.

   The Bill contains four schedules: Schedule A enacts the *Energy Conservation Leadership Act,* 2005. Section 2 of the act permits the Lieutenant Governor in Council to, by regulation, require persons who are selling, leasing or otherwise transferring an interest in real property or personal property to provide such information as may be prescribed in the circumstances that are prescribed.

2. *Bill 40—Disclosure of Crimes on Property Act*

   The Second Reading was debated and carried May 11, 2006. The Bill has been referred to the Committee of the Whole House.

The Bill proposes to amend the *Conveyancing and Law of Property Act* and the *Tenant Protection Act, 1997,* to provide that a vendor in an agreement of purchase and sale, and a landlord in a tenancy agreement, must disclose to the purchaser or tenant whether the property that is the subject of the agreement has been used to commit a crime during the time that the vendor or landlord had a legal interest in the property.

3. *Bill 51—Planning and Conservation Land Statute Law Amendment Act*

   The Second Reading was debated April 19, 24 and 26, 2006. The Bill proposes to make numerous amendments to the *Planning Act.* Most of them would modify aspects of the land use planning process, provide additional tools for implementation of provincial policies, and give further support to sustainable development, intensification and Brownfield redevelopment.

   There has been no further legislative activity in respect of the following bills:

   Bill 9—Gender-Based Price Discrimination Prohibition Act

   (i) Bill 20—Frederick Banting Homestead Preservation Act

   (ii) Bill 24—Environmental Protection Amendment Act

   (iii) Bill 31—Liquor Licence Amendment Act

Update on Assessment Board Review and Ontario Municipal Board Hearings
ICSC expects to receive updated information in the near future from the Assessment Review Board with respect to upcoming hearings.

b) Case Law Developments

- *J.S.M. Corp. (Ontario) Ltd.* v. *Brick Furniture Warehouse Ltd.* [2006], O.J. No. 812 (Ontario Superior Court of Justice, March 2, 2006, P.A. Cumming J.)

The landlord commenced an action against the tenant and its subtenant to recover damages incurred as a result of a breach of the lease. The tenant and subtenant were related entities. The subtenant was the operating arm of a large business enterprise. The tenant's sole asset was the lease it had entered into. As the tenant was essentially a shell corporation, practically speaking, the landlord sought recovery of damages from the subtenant, as the subtenant had substantial assets.

The landlord had consented to the sublease by way of a written Consent and Acknowledgement Agreement. At the time of consent, the landlord was presented with a sublease for a fixed term. The Consent and Acknowledgement Agreement included representations to the landlord that the subtenant would pay rent to the tenant and that the tenant would, in turn, pay rent to the landlord pursuant to the head lease. *There was no direct covenant or privity of contact between the landlord and the subtenant as to the payment of rent.*

After the landlord provided its consent, the sublease was unilaterally amended as between the tenant and the subtenant to include a 90-day termination right in favour of the subtenant. The landlord was not aware of the amended sublease and had no knowledge of the early termination clause.

The subtenant subsequently exercised its early termination right under the sublease and vacated the premises. The tenant informed the landlord of this and stated that it would be difficult for the tenant to continue paying rent under the head lease. The landlord terminated the lease when the tenant failed to pay rent.

The landlord was successful in obtaining judgment against the subtenant and the tenant on a joint and several basis. The court ruled that the oppression remedy was available to the landlord against *both* the subtenant and the tenant. In this regard, the court held that the addition of the termination provision was a fundamental change to the sublease and, as such, the landlord's consent was required. The landlord did not consent to the change, so it was the original sublease and not the amended sublease that bound the landlord. In the court's view, it was oppressive and unlawful for both the tenant and the subtenant to first create reasonable expectations and reliance on the part of the landlord that the subtenant would meet the rental obligations for the premises through the sublease, but then, seek to defeat those expectations through the exercise of a termination right in the sublease, which the landlord was not aware of. The court also noted that the subtenant's conduct was oppressive, given that the subtenant had undertaken with the tenant to pay rent under the sublease and held out to the landlord that it would meet such obligation as an inducement for the landlord to enter into the Consent and Acknowledgement Agreement.

The landlord also sought to recover damages from individual directors of the tenant and subtenant by arguing that the directors intentionally interfered with the economic relations between the landlord, tenant and subtenant, and that the directors induced the breach of contracts. However, this claim was dismissed, as the court held that there were no grounds on which to find liability as against the individuals.

- *Nicholby's Franchise Development Inc.* v. *1263448 Ontario Ltd.* [2005], O.J. No. 4396 (Ontario Superior Court of Justice, Oct. 14, 2005, P.T. Matlow J.)

  The landlord sought to relocate the tenant in order to accommodate a new, large grocery store. The lease stipulated that the landlord could relocate the tenant so long as the landlord's right to relocate was not exercised "for the purpose of depriving the tenant of the use and enjoyment of the premises or in order to relet the premises to another party."

  The tenant sought to have the landlord's relocation notice set aside on the basis that it violated the terms of the lease and the covenant for quiet enjoyment. According to the tenant, the landlord was attempting to re-let the premises to another party, which was strictly prohibited by the lease. The landlord argued that it was not relocating the tenant in order to lease the premises to another party but, rather, that it was "remerchandising" the centre and relocating several tenants in the process. The landlord also took the position that it was not leasing to someone else, as the premises would be demolished and would no longer exist (that is, the premises would be demolished and the floor area would form part of the much larger grocery store). In the alternative, the landlord sought the court's approval of a scheme whereby the tenant's premises would remain vacant and would be excluded from the area leased to the grocery store (notwithstanding that the premises would be completely surrounded by the grocery store premises).

  The court ruled that the landlord's proposed relocation was in contravention of the lease. In the court's view, it was clear that the landlord was relocating the tenant to lease the premises to another party. It did not matter that the landlord was purporting to "remerchandise" the centre, nor did it matter that other tenants were also being relocated in the process. The court was also of the view that the destruction of the walls and ceilings was insufficient for the landlord to claim that it was not leasing the premises to a third party, as the premises would no longer exist once they were incorporated into the larger grocery store. The court also rejected the landlord's alternative proposal whereby the tenant's premises would remain vacant and not leased to the grocery store. The court viewed this as being a sham. The notice of relocation was set aside, and the tenant was permitted to remain in possession of the premises.

- *Great Atlantic & Pacific Co. of Canada* v. *Topostar (Aurora) Inc.* [2006], O.J. No. 945 (Ontario Superior Court of Justice, March 10, 2006, D.R. Cameron J.)

  This case involved the interpretation of an expansion clause in a lease. In particular, the court was called upon to determine if the expansion clause was enforceable as against the landlord. The expansion provision in question stated that the tenant could expand so long as the landlord approved the tenant's plans. The provision also stipulated that rent for the expansion space was "to be negotiated by the landlord and tenant acting reasonably."

  In August 2004, the tenant indicated it was interested in negotiating under the expansion clause. Until that time, the evidence indicated that the parties treated the expansion right as if it was fully enforceable. Negotiations ensued, and the main issue between the parties was the fixed annual rent to be paid on the expansion space. There was a fundamental disagreement about the amount of the rent. The lease provided for different permitted uses of the premises; and, as different uses can attract different rents, the landlord and the tenant were unable to agree on which use should determine the rent. Negotiations broke down, and the landlord subsequently took the position that it would no longer discuss the expansion with the tenant, as the expansion provision was unenforceable.

  The court examined the language in the lease to uncover the intention of the parties. In the court's view, the words in the lease provided no objective standard (such as "market" rent) and there was no provision for arbitration or any other method to obtain an agreement if the negotiations failed. Accordingly, the court ruled that the expansion provision was merely an agreement to agree and, as such, the expansion clause was unenforceable.

6. **Quebec**
   Fred Carsley of De Grampré Chait has nothing to report for Quebec.

7. **New Brunswick**
   Serena Newman of Barry Spalding LLP has nothing to report for New Brunswick.

8. **Nova Scotia**
   James Rossiter of Wickwire Holm reports that the **legislative development** of Sunday shopping continues to be a contentious issue.
   a) **Case Law Developments**
   Nothing to report.

9. **Prince Edward Island**
   a) **Legislative Developments**
   Donald K. MacKenzie of Foster Hennessey MacKenzie reports the following: By Order No. LA06-06 of the Island Regulatory and Appeals Commission, dated May 31, 2006, a decision by the Town of Stratford to re-zone two parcels

of property for development purposes was overturned. The land in question had been re-zoned for the purposes of the development of an Atlantic Superstore by the APM Group. The Island Regulatory and Appeals Commission allowed the appeal and quashed the decision of the Town, thereby prohibiting the development of the new grocery store.

b) Case Law Developments

Nothing to report.

10. Newfoundland and Labrador

a) Legislative Developments

Robert Andrews of White Ottenheimer & Baker reports the following:

1. Municipal Remedies

- City of Corner Brook Act
- City of Mount Pearl Act
- City of St. John's Act
- Municipalities Act
- St. John's Assessment Act

Amendments under these acts give municipalities the authority to disconnect service of a water system, sewage system or water and sewage system where a tax, fee, levy, assessment, fine or other charge imposed by the council is in arrears. Previously, only non-payment of taxes would have allowed a municipality to disconnect these services.

2. Changes to *Building Accessibility Act*

This act has been amended to provide that a person who makes changes to a building that existed prior to Dec. 24, 1981, to improve its availability and accessibility to persons with disabilities, must make those changes in conformity with the standards set by the act. Further, drawings and specifications must be registered with the director appointed under the act before a permit for construction of the building will be given.

Certain changes have also been made to the appeal process under the act. In addition, there has been an increase in the fines that may be levied against an individual and a corporation for violations of the act. The fines for an individual range between $500 and $5,000, and for a corporation between $1,000 and $25,000. There is also a per diem fine of between $200 and $2,000 per day for continued non-compliance.

These amendments increase the level of responsibility that a builder owes when undertaking to make its buildings accessible to people with disabilities and makes the fines for failure to comply much more substantial.

3. *Occupational Health and Safety Act*

Changes to this act have extended the limitation period during which offences under the act or regulations may be prosecuted to two years from the date upon which the offence is alleged to have been committed; or from the date upon which an assistant deputy minister or an officer of the Occupational Health and Safety Division becomes aware of the alleged offence, whichever is later.

4. *Assessment Act/St. John's Assessment Act*

Amendments to the *Assessment Act* and *St. John's Assessment Act* create a new category of property called a "special purpose property"—that is, one that has a design or layout or is that is constructed of special materials or in a manner that restricts its use. Assessments for special purpose properties will be based on the reproduction cost of the property, which is the cost to construct a reasonably identical replacement of the property less physical depreciation only.

The impact of this amendment, and its apparent ambiguity, has yet to be determined. However, it is widely perceived as a reaction to the 2005 decision of the Newfoundland and Labrador Court of Appeal decision dealing with a brewery valuation for tax purposes in St. John's.

5. *Human Rights Code*

The Human Rights Code in Newfoundland has been amended substantially. It has been amended to prevent discrimination on the basis of marital status, family status and age in the provision of services, facilities and goods. Further, it is prohibited to discriminate against a person based on family status, age and source of income with respect to the occupancy of commercial or dwelling units. Marital status and family status have also been added to the prohibited grounds for discrimination in employment. Previously it was not prohibited to discriminate based on age in employment for persons who were less than age 19 and over 65. However, amendments to the act now make it a discriminatory practice to discriminate against people for employment purposes on the basis that they have reached the age of 65.

b) Case Law

In *Petty Harbour—Maddox Cove (Town)* v. *Peerless Fish Co.*, the Trial Division of the Newfoundland and Labrador Supreme Court dealt with issues of discrimination in the application of business tax and notice of tax increases. The town had not levied business tax against another company in the town, operating the same business as the defendant on the basis that it had a legal opinion that that business was not subject to business tax. The court determined that the town had an option with respect to charging the tax to the other company and that its decision to not tax the other company while continuing to tax the defendant was a discriminatory practice. As a result, the Court awarded a small amount of damages to the defendant.

Of further issue was an increase in water tax that was applicable only to the defendant and the similar company. The other company had a board member who also sat on Town Council and was, therefore, aware of the water tax increase. The town attempted to provide notice to all taxpayers by putting a notification in the mailboxes at the post office. The defendant never received this notice.

Despite the fact that a curative position existed in the *Municipalities Act,* which states that payment of a tax or a service surcharge is not affected by the failure of a municipality to comply with the notice requirements of the act, the Court determined that, in this case, where only two taxpayers were subject to the tax—one of which had actual notice of the matter due to its representation on the Municipal Council—the town should have taken the steps of providing actual notice to the defendant. As a result of this failure, the defendant was not liable for the additional water tax.

Blended Business Occupancy Tax

At present, municipalities in this province continue to levy a property tax against business or commercial property, which forms a priority lien against the subject property, and also a business occupancy tax for a similar amount against the business operated upon the property. This latter tax is the responsibility of the tenant and, as such, does not constitute a lien against the landlord's property.

Many other provinces have had similar systems, but have blended the tax in the hands of the landlord over the past number of years. The issue has again been raised in Newfoundland and Labrador, primarily by the city of St. John's, and this may be the time the actual change occurs. The impact, of course, is that taxes uncollectible from the tenant become a landlord problem, and not the municipality that then enjoys a complete priority lien against the real estate.

With this is mind, landlords should be expressing their concerns about the impact of blending to the provincial and municipal governments. They also must be reviewing their leases and financial documents to assess their individual situations and their preparedness for the potential legislative change.

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