

PROPERTY — LEASING UPDATE

JANUARY 2015



Beware: Insurance, Indemnity, and Terms Not As They Appear

Mac Allen » [full bio](#)

Landlords and tenants should always be thinking about the relationship between an obligation to insure and a lease's indemnity clause so that the risk, should the "Premises" be damaged, is allocated as the parties intended.

Generally, where insurance is obtained for the benefit of one party, the obligation to insure operates as a waiver of liability in favour of the other party. However, in one recent case *Deslaurier Custom Cabinets Inc. v 1728106 Ontario Inc.*, 2014 ONSC 5148 ("**Deslaurier**"), the Ontario Superior Court of Justice held that a tenant's covenant to insure may be limited by express provisions in the lease.

In *Deslaurier*, 1728106 Ontario Inc. (the "**Landlord**") entered into a lease with Deslaurier Custom Cabinets Inc. (the "**Tenant**") to carry on the business of manufacturing and sale of custom cabinets in Units 4, 5, 11, 12, 13, 14, and 16 of the Building, containing a rentable area of 95,090 square feet (the "**Premises**"). As a condition of the lease, the Landlord was required to have John Faught Steel Inc ("**JFS**"), perform structural repairs to the Premises. During this repair work, a fire occurred resulting in the total loss of the building.

The Tenant sought recovery of damages to its property, and its business interruption losses. The Tenant was paid approximately \$10,861,885.65 by its insurer and sought to recover its remaining alleged losses from the defendants, the Landlord and JFS, in the amount of \$4,138,114.35. The Landlord brought a summary judgment motion and the Tenant brought a cross-motion to determine who assumed the risk of damage resulting from the fire. JFS did not participate in the summary judgment proceeding.

The issue was the interpretation of the lease, and the relationship between the Tenant's obligation to insure clause 8.1.1, the Landlord's indemnification clause 8.2.1, and the effect of clause 9.3, the relevant parts of which are set out below:

- 8.1.1 The Tenant must also obtain the following insurance for the Premises:
 - ii. insurance against all risks of loss or damage to the Tenant's property; ...
- 8.2.1 ... the Landlord further covenants to indemnify the Tenant with respect to any encumbrances on or damage to the Premises occasioned by or arising from the act, default, negligence of the Landlord, its officers, agents, employees, contractors, customers, invitees or licensees; ...

WeirFoulds LLP

66 Wellington Street West
Suite 4100, PO Box 35
Toronto-Dominion Centre
Toronto, Ontario, Canada
M5K 1B7
Office 416.365.1110
Facsimile 416.365.1876
www.weirfoulds.com

Follow us on:  

9.3 Apart from the provisions of Section 9(1) **and as otherwise specifically provided for in this Lease**, ... nor shall the Tenant be entitled to claim against the Landlord for any damages, general or special, caused by fire, water, sprinkler systems, partial or temporary failure or stoppage of services or utilities which the Landlord is obligated to provide according to this Lease, from any cause whatsoever. *[Emphasis added]*

Before determining whether the Landlord's liability was changed by section 8.2.1 Justice Métivier, writing for the Court, first had to decide what the parties meant by the term "Premises". On its face, "Premises" referred to nothing more than the rentable area leased by the Tenant. Other terms of the lease referred to Premises in the following contexts: "...the Tenant shall: keep in good condition the "Premises" including all alterations and additions made thereto (save and except for wear and tear)..." and "[i]f the Tenant... desires to make any alterations or additions to the Premises, including but not limited to... attaching equipment, and installing furnishings... the Tenant may do so at its own expense...". Justice Métivier acknowledged that the reference in the lease to "Premises" seemed to indicate that the term was to be restricted to the rentable space and excluded the Tenant's property.

Nevertheless, Justice Métivier held that if "Premises" meant nothing more than the rentable area, then the Landlord would be indemnifying the Tenant for something in respect of which the Tenant had no interest. It does not appear from the decision that the Court considered whether the Tenant's leasehold interest, or the market value of the leasehold interest, was an interest the Tenant had and which was amenable to indemnification by the Landlord. Instead, Justice Métivier held that limiting the "Premises" to the rentable area would, in effect, render the second portion of s. 8.2.1 meaningless. The Court decided to reject an interpretation which in its opinion would render one of the lease's terms ineffective. In our view, the decision in *Deslaurier*, is an indication that the courts are willing to expand a term's meaning beyond the written words in the lease or its customary usage, and pursue an interpretation that produces a "fair result" or a "sensible commercial result".

Having expanded the interpretation of "Premises" to include the Tenant's property, the Court then shifted focus to decide whether the Tenant's obligation to insure was in any way limited by the other provisions in the lease. The Court relied on the introductory wording in section 9.3 and extrinsic evidence regarding leases for other units in the same building that only contained one-way indemnification clauses to find that the parties must have specifically intended to give the Tenant some contractual right not granted to the other tenants in the building. The Court held that the Tenant's covenant to insure was limited by the express provisions in the lease that required the Landlord to indemnify the Tenant for its (or its agent's) acts or negligence. Therefore, the Landlord was held liable for the losses claimed by the Tenant.

In conclusion, landlords and tenants should pay particular attention to the insurance and indemnification clauses of their leases that allocate the risk of loss between the parties in the event of damage and destruction. When a premises is damaged as a result of the acts or negligence of others, your insurance and indemnity clauses are crucial to making your business whole again. However, as demonstrated in *Deslauriers*, landlords and tenants must be aware that the slightest ambiguity in either clause may provide the court with an opportunity to hold one party or another to be responsible for so much more than that for which they bargained.

PROPERTY

Since the First World War, we have acted on the largest and most significant property and infrastructure developments in Canada. These projects have ranged from shopping centres to public transportation projects, from waterfront re-development to hydro transmission corridors, from land fill sites to office towers, from highways to industrial projects, and virtually everything in between. We are regarded as having the premier Property practice in Ontario – in one of the most dynamic economies on the continent and home to North America's fifth largest city – Toronto.

ABOUT THIS NEWSLETTER

For over 150 years, the lawyers of WeirFoulds have been proud to serve our clients in their most difficult and complex matters. We are the firm of choice for discerning clients within our core areas of practice: (1) Litigation; (2) Corporate; (3) Property; and (4) Government Law. Within these core areas, as well as key sub-specialties, we address highly sophisticated legal challenges. We have acted in some of Canada's most significant mandates and have represented clients in many landmark cases. Reflecting the firm's focus, our lawyers are consistently recognized as leaders in their chosen areas of practice and in the profession at large. To learn more about our firm, visit www.weirfoulds.com.

Information contained in this publication is strictly of a general nature and readers should not act on the information without seeking specific advice on the particular matters which are of concern to them. WeirFoulds LLP will be pleased to provide additional information on request and to discuss any specific matters.

If you are interested in receiving this publication or any other WeirFoulds publication by e-mail, or if you would like to unsubscribe from this newsletter, please let us know by sending a message to publications@weirfoulds.com.

© WeirFoulds LLP 2015