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To assign or sublease, now that is the question

There is much confusion surrounding the concepts of subleasing and lease assignment. The frequent use of the term "transfer" in commercial leases blurs the nuances which distinguish the two concepts by interpreting them substantially in the same way, whereas they are in fact two distinct mechanisms, each with their own legal consequences. It is therefore important to distinguish them clearly. It should be noted that, according to a decision rendered in 2002 by the Quebec Court of Appeal, faced with the vagueness of a lease as to the actual intent of the parties to either sublease or assign, the contract concluded that the parties' intent was to sublease¹.

Furthermore, it is important to understand that the *Civil Code of Québec* (the "CcQ") applies in a suppletive manner in the context of commercial leasing. In other words, the provisions of a commercial lease supersede the default leasing provisions found in the CcQ, with the exception of the provisions of public policy². Commercial leases, therefore, often render inoperative the provisions of the CcQ, since they are only of a public nature in respect to residential leasing³. In addition, items that are not provided for in the lease will be governed by the provisions of the CcQ.

Consent of the landlord

Before making an assignment or sublease, the tenant must notify the landlord and obtain his consent, express

or implied, subject to the conditions of the lease⁴. There is tacit consent where there is no objection or reaction from a landlord with knowledge of the process⁵.

A landlord may not refuse consent without serious cause⁶. The public nature of this rule is unclear⁷, but the courts seem reluctant to allow a purely arbitrary refusal⁸. Moreover, the assignment of a lease without the landlord's consent does not necessarily result in it being void if the landlord has no serious reason to oppose it⁹.

It is common for leases to list grounds that will be considered serious, and as such, the landlord who invokes one of these grounds for refusal need not justify its reasonableness¹⁰. However, it seems that clearly unreasonable grounds for refusal could be challenged before the courts even if the lease purports to establish a presumption that refusal on such a basis is valid¹¹.

Many leases provide the right for the landlord to terminate the lease when the tenant informs him of his intention to sublease the premises or to assign the lease. It should be noted that the legality of this practice has not yet been established by the Quebec courts. A tenant should attempt to have such a right removed from the lease, or at least to ensure that certain exclusions apply, particularly in the case of the sale of a business or a corporate reorganization. A landlord may not, however, improperly avail himself of his right to terminate with the simple goal of circumventing the obligation to provide serious grounds for refusal¹².

According to the case-law, reasons considered to be "serious" include:

- Modification of the use or destination of the premises
- A use that contravenes exclusivities granted by the landlord to the other tenants in the building
- The solvency and financial capacity of the subtenant or assignee, including his credit rating or payment practices¹³
- The tenant's refusal to provide all requested information about the proposed subtenant¹⁴

According to the jurisprudence, reasons considered not to be “serious” include:

- Reasons linked to rent increases and profit sharing related to the proposed transaction¹⁵
- The fact that the subtenant pays the tenant a higher rent than the tenant is required to pay to the landlord¹⁶
- Discriminatory grounds¹⁷

If the landlord's refusal to consent to a sublease or assignment is not based on serious grounds, the landlord is considered to be in breach of his obligation to provide for the peaceful enjoyment of the premises¹⁸ and does not suffice as grounds for the landlord to prevent the tenant from subleasing the premises or assigning the lease. The tenant may, if necessary, obtain a court order to compel the landlord to comply with this obligation¹⁹. On the other hand, where the transfer is made without the landlord's consent and where the landlord could have objected for a serious reason, the subleasing and assignment could be voided by a court²⁰.

Sublease

The CcQ provides the tenant's right to sublease the premises described in his lease²¹. Subleasing involves the coexistence of two separate leases: a primary lease and a sublease. Given the principle that one cannot grant more rights than one owns, the “sub-landlord” must exercise caution when arranging a sublease, such as its duration, renewal options and use of the premises²². The sub-landlord has the dual role of landlord and tenant: to the subtenant, he assumes the responsibilities of a landlord and, with respect to the landlord, he assumes the responsibilities of a tenant. Subject to the conditions of the primary lease, it is namely possible to sublet all or part of the premises for a lower or higher rent. Note that clauses prohibiting partial subleasing of the premises or payment of a higher rent are, however, commonly found in commercial leases. During the course of a sublease, the primary lease continues to be in effect and the relationship between the tenant and the landlord continues. Thus, the tenant remains liable to the landlord for damages caused by the subtenant²³. It is therefore in the tenant's best interest to ensure that the subtenant respects the primary lease, since the subtenant's default would be attributable to him.

According to the principle of the relative effect of contracts, the contract is effective only between the contracting parties²⁴. Since the landlord is a third party to the sublease contract, there is, in principle, no legal relationship between the landlord and the subtenant. Nevertheless, the CcQ provides for exceptions to this principle by creating certain legal relationships between the landlord and the subtenant²⁵. For example, the CcQ provides for direct recourse between the landlord and the subtenant²⁶. A landlord may apply for the termination of

the sublease if the subtenant fails to meet a required obligation, for example, if the subtenant fails to pay the rent or adversely and seriously affects the peaceful enjoyment of other tenants. The subtenant, for his part, may employ the tenant's rights and recourses to compel the landlord to fulfill his obligations if the latter fails to fulfill those to which he is bound. The subtenant can also take advantage of an extra contractual remedy for damages if, for example, the obligation has become impossible to fulfill²⁷.

Moreover, it is possible to contractually waive the principle of the relative effect of contracts. The landlord may require that the subtenant contractually undertake to fulfill all the obligations provided for in the primary lease contract and pay the rent directly to him²⁸.

The sublease, a precarious contract

The sublease is subject to the existence of the principal lease, which remains outside the control of the subtenant, especially if he makes the payments to the tenant. In addition, the subtenant has no right to continue to occupy the premises if the principal lease is terminated.

To avoid such a situation, a subtenant should ensure that he obtains an undertaking from the landlord that the landlord shall maintain the existing sublease in the event the principal lease is terminated due to the tenant's breach of his obligations, or request the right to remedy the tenant's failures in the case of such breach to avoid the termination of the primary lease. In addition, subject to the terms of the sublease, the subtenant losing use of the premises by the fault of the tenant would have a contractual remedy available for seeking damages against the tenant.

The subleasing mechanism is useful when a tenant wants to maintain some control over the premises, particularly in terms of franchising. Note that a sublease cannot be validly published²⁹.

Lease assignment

The lease assignment does not create a new lease: the rights and obligations of the assignor are simply passed on to the assignee. Therefore, the destination and use of the premises remain the same³⁰.

The CcQ provides that the assignment releases the former tenant from his obligations. For this reason, there is no longer any link between the landlord and the tenant-assignor, this link having been transferred and now existing exclusively between the landlord and the assignee³¹. This rule, however, is not of public order and landlords often contract out of this rule by requiring that the tenant-assignor remain jointly and severally liable with the assignee for the performance of the obligations provided in the lease³². The release of the assignee is often the subject of negotiations, notably with regards to his continued liability during renewal periods of the lease.

Where the tenant-assignor is not discharged from his obligations, the landlord may choose to apply to either the assignor or the assignee if the assignee fails to fulfill his obligations. In the event that the tenant is liable to pay due to the default of the assignee, the tenant would have recourse against the assignee. This does not alter the exclusive relationship between the landlord and the assignee and, unlike subletting, the tenant-assignor does not have a dual role. Thus, the assignee's remedies can only be directed against the landlord. The lease may also include a clause requiring the tenant-assignor to take back the premises in the event of default by the assignee³³.

Conclusion

Subleasing and assignment are two distinct legal mechanisms. It is essential to understand the legal consequences of each to properly draft a commercial lease. It is also important to know the suppletive provisions of the CcQ which apply, in order to ensure that the lease is drafted in accordance with the parties' intentions. We would be pleased to assist you in drafting an effective commercial lease corresponding to your needs.

1. *Société immobilière I.M.O. enr. v. Scabrini Imprimeurs inc.*, 1999 CanLII 11197 (QC CS), REJB 1999-13671, par. 57-59, confirmed on appeal: 2002 CanLII 63741 (QC CA).
2. *Leblond v. Dionne*, 2006 QCCA 341, par. 27.
3. Article 1893 CcQ.
4. Article 1870 CcQ.
5. *Centre électrique mauricien inc. v. 9101-9380 Québec inc.*, AZ-50317788, par. 23; Denis Paquin, "Cession et sous-location – Outils importants dans un bail commercial", in *Le bail commercial*, La Collection Blais, vol. 9, 2011, p. 45-46.
6. Article 1871 CcQ.
7. *91133 Canada Ltée v. Groupe Thibault Van Houtte & Associés Ltée*, 2003 CanLII 46804 (QC CA), par. 93. Please note that this decision refers to the opinion of Professor Pierre-Gabriel JOBIN, in *Traité de droit civil, le louage*, 2nd ed., Cowansville, Éditions Yvon Blais, 1996, p. 70-71. The Professor believes that this rule should be imperative, even in the context of nonresidential leasing.
8. *Ferme Guy Bonin enr. v. Malouin*, 2000 CanLII 6582 (QC CA), par. 29.
9. *Lévesque v. Tourbières Premier Ltée*, AZ-97021095, granted on appeal: *Lévesque v. Premier Horticulture Ltée*, AZ-99011717.
10. *Immeubles Bleury-Dorchester inc. v. Banque Nationale du Canada*, 1997 CanLII 9086 (QC CS).
11. Denis Paquin, *supra* note 6, p. 56-57.
12. *91133 Canada Ltée*, *supra* note 7, par. 93.
13. *Ibid.*, p. 62; Brigitte Caplette, *Le louage commercial*, Répertoire de droit, Chambre des notaires, 3rd ed., 2016, par. 263.
14. *Goordazi v. 9268-2798 Québec inc.*, 2016 QCCS 3926.
15. Denis Paquin, *supra* note 5, p. 66 and Pierre-Gabriel Jobin, *Le louage*, 2nd ed., 1996, p. 69.
16. Pierre-Gabriel Jobin, *supra* note 16, p. 69.
17. *Ibid.*, p. 68; *Charter of Human Rights and Freedom*, C.Q.L.R. c. C-12, articles 10, 12-13.
18. *9015-2489 Québec inc. v. Baldo Lumia inc.*, 2001 CanLII 39037 (QC CS), par. 106.
19. Pierre-Gabriel Jobin, *supra* note 16, p. 73.
20. Brigitte Caplette, *supra* note 13, par. 266, citing article 1416 CcQ.
21. Article 1870 CcQ.
22. Brigitte Caplette, *supra* note 13, p. 79; Article 1856 CcQ.
23. *Bazinet v. Arbour*, AZ-97061056, [1997] J.L. 142 (RDL).
24. Article 1440 CcQ.
25. Articles 1874, 1875 and 1876 CcQ.
26. Articles 1875 and 1876 CcQ. Please note that these articles are not of public order in the context of commercial leasing.
27. *2855-0523 Québec inc. v. Ivanhoe Cambridge inc.*, 2011 QCCS 6624, par. 54-66.
28. Brigitte Caplette, *supra* note 13, p. 80. Please note that direct payment does not alone create a legal relationship between the landlord and the subtenant. (*Dere v. Soltron Realty Inc.*, 2005 CanLII 19442 (QC CS), par. 60.)
29. *Compagnie des chemins de fer nationaux du Canada v. Télé-cinéma Taurus inc.*, 2006 QCCS 845, par. 141-151.
30. Brigitte Caplette, *supra* note 13, par. 245.
31. Article 1873 CcQ.
32. Denis Paquin, *supra* note 5, p. 39.
33. *Ibid.*, p. 73.

The content of this newsletter is intended to provide general commentary only and should not be relied upon as legal advice

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