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"Curing or Killing the Sick Real Estate Deal: Litigation and Real Estate Strategies"

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Leasing Litigation: Tips and Tactics

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INTRODUCTION

The law of commercial leasing is part real property law and part contract law. As a result it takes a number of twists and turns which often defy common sense and logic. Over the years there has been a steady shift away from some of the more arcane principles as exemplified by the decision of the Supreme Court in *Kelly Douglas v. Highway Properties*[1]. However, because the commercial lease still grants an interest in land, it is unlikely that all of the unique features which arise from this will ever disappear. This presents a unique challenge to both the barrister and the solicitor when advising their clients in landlord tenant matters.

In the first part of this paper, we present an overview of litigation options to consider when dealing with commercial landlord tenant issues. We attempt to touch on a number of topics, and as a result, an in-depth treatment of the topics is not provided.

In the second part of this paper, we review a number of issues which relate to commercial leasing. The selected topics tend to arise at the front end of the commercial lease transaction as, opposed to default remedies. Again we attempt to touch on a number of topics, and are accordingly, unable to provide an in-depth treatment of any one issue.

Finally throughout this paper we have always kept in mind our overall theme, that the law of commercial leasing is a peculiar amalgam of real property law and contract law.

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[1] [1971] S.C.R. 562.

I. LITIGATION OVERVIEW IN LANDLORD TENANT MATTERS

The Originating Process: Application or Statement of Claim

Whenever an issue arises which may lead to litigation, one of the parties, if not both, wants a quick resolution of the issue. Unfortunately we all know that litigation often means a life sentence of discoveries, motions, pretrials, and delays, not to mention expense, with a trial three to five years down the road. As a result, litigators are faced with the challenge of getting a quick, cost effective result. This challenge becomes even greater in the face of one of the most common defense tactics, which is to delay and to obfuscate matters in the hopes that litigation fatigue will set in and the suit will go nowhere.

Notice of Application - rule 14.05

The hearing of an application can be brought on much faster than a trial, often in a matter of months. An application may be brought for a wide variety of relief where it is unlikely that there will be any material facts in dispute. An application proceeds on affidavit evidence and cross examination, no *viva voce* evidence. However, if there are factual issues in dispute that cannot be resolved on the basis of the written record, then the court may order a trial of those issues.

In order to proceed by way of application, either the landlord or the tenant should attempt to cast the issue as an application to interpret a lease (rule 14.05 (d)). To this can be joined a claim for an injunction or a declaration or payment in accordance with the interpretation. For example where there is a dispute over a use clause, the landlord may bring an application to interpret the

clause and an injunction to enforce the tenant's compliance with the clause.

For the tenant, one of the most common applications is for relief from forfeiture. This application may be brought either under the *Courts of Justice Act* ("CJA") section 98, or the *Commercial Tenancies Act* ("CTA") section 20 (1), or to be safe, under both acts.

For the most part, the requirements for relief from forfeiture whether under the CJA or the CTA are the same with one notable difference. Under the CTA it is a requirement that a forfeiture has in fact occurred, i.e., not just a notice of future termination and demand for possession. Under the CJA there is no such requirement. Accordingly relief under the CJA may be available in a wider variety of circumstances than under the CTA. However, keep in mind that it is unsettled whether the *Commercial Tenancies Act* is intended to be a complete code, thereby precluding the applicability of *CJA*, or whether the court may proceed under the *CJA*, despite the provisions of the *Commercial Tenancies Act*.

Statement of Claim

Generally where there is a claim for damages for breach of lease or a claim for non-payment of rent the parties proceed by statement of claim.

In rent collection matters, landlord's counsel will usually issue a statement of claim. This will allow them to obtain default judgment where the claim is not defended.

Default Judgement - rule 19

Where no statement of defense is filed within the time prescribed by the rules the landlord may obtain default judgment signed by the registrar "for a debt or liquidated demand in money, including interest if claimed in the statement of claim" (rule 19.04 (1) (a)). A claim for rent owing under a lease is a liquidated demand for money for which default judgment is available. Default judgment is also available for the rent due over the unexpired term of the lease, although this is not always granted automatically, and the registrar needs to be convinced that it should be granted.

Summary Judgment - rule 20

Where a statement of defense is filed, counsel will assess the quality of the defense, and if it appears that the tenant does not have a defense to the action then a motion for summary judgment under Rule 20 is the next step. The rule provides; "where the court is satisfied that there is no genuine issue for trial .... the court shall grant summary judgment accordingly."

The Court of Appeal has made it clear that when dealing with a motion for summary judgment the court is not to assess credibility or find facts. It is not sufficient for the defendant to merely raise a number of issues. The defendant must present evidence of specific facts to establish that there is a genuine issue for trial. The court must examine that evidence to see if it is reasonably capable of raising a genuine issue for trial. Where the court is satisfied that the evidence does not support the conclusion that there is a genuine issue for trial, then the Court shall grant summary judgment[2].

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[2] *Irving Ungerman Ltd. v. Galanis* (1991) 4 O.R. (3d) 545, [1991] O.J. No. 1478 (C.A.), *Bossé v. Mastercraft Group* [1995] O.J. No. 884 (C.A.), *Aguonie v. Galion solid Waste Material Inc.* (1998) 38 O.R. (3d) 161 (C.A.)

Injunctions

Injunctions are a powerful tool for bringing an issue to a head, and are sought frequently by both landlords and tenants. The claim for an injunction must be made in the originating process (the statement of claim or notice of application), however, in most cases quick action is required and a motion of an interlocutory injunction is brought.

Interlocutory Injunctions

The three point test that a party seeking an interlocutory injunction must meet is well established.

1. First, a preliminary assessment must be made of the merits of the case to ensure that there is a serious issue to be tried.

2. Second, it must be determined whether the applicant would suffer irreparable harm if the application were refused.

3. Finally, an assessment must be made as to which of the parties would suffer greater harm from the granting or refusal of the injunction pending a decision on the merits[3] ie the "balance of convenience" test.

The granting of an interlocutory injunction is an extraordinary remedy, that if granted, gives the moving party a remedy until trial for a right that has yet to be proven. This requires the court

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[3] *Abbott Laboratories Ltd.* v. *Apotex Inc.*, [1998] O.J. No. 2159 (QL)(Gen. Div.), *R.J.R. Macdonald Inc.* v. *Canada (Attorney General)* (1994), 54 C.P.R. (3d),(S.C.C.),

to be particularly vigilant in the exercise of its discretion to grant or withhold such relief until the merits of the case have been determined.

The majority of interlocutory injunction cases come down to the balance of convenience test. In the landlord tenant context, we find that the balance of convenience often favors the tenant because the consequences of granting the interim injunction (or not granting the interim injunction) as the case may be, will often have a far greater impact on a single tenant than on the landlord.

Permanent Injunctions

As a result, the landlord may be better off to bringing an application, or a motion for summary judgment for a permanent injunction, because the granting or withholding of a permanent injunction does not depend on the balance of convenience. However, the party seeking the permanent injunction must prove,

a. on an application that it is entitled to a permanent injunction, or

b. on a motion for summary judgment

that there is no genuine issue for trial with respect to the granting of the permanent injunction. If there are serious factual issues that require a trial then in either case a trial of an issue may be ordered by the judge hearing the application or motion.

Trials

Where the claim is proceeding by way of a statement of claim, the trial will happen in due course, after discoveries, a few motions, a pretrial and a few years. But remember the trial will happen, justice is slow but it is sure. However, you may succeed in obtaining an early trial date

on a application or a motion for judgment where the court orders a trial of an issue.

Trial of an Issue

Application, rule 38.10(1)

At the hearing of an application the judge may order that the whole application or any issue proceed to trial.

Summary Judgment, rule 20.05 (1)

Similarly, on a motion for summary judgment, one of the options open to the court is to order a trial of some or all of the issues.

If you don't succeed on your application or motion for summary judgment for a permanent injunction, or whatever other relief you are after, you may succeed in having a judge order a trial of only the issues that are truly in dispute, and the judge could also order an expedited or early trial date.

A word of caution, there are cost consequences to losing a motion for summary judgment[4] or an application.

Finally the respondents on an application will invariably claim that the case is not appropriate

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[4] rule 20.06 (1) reads as follows: "Where, on a motion for summary judgment, the moving party obtains no relief, the court shall fix the opposite party's costs of the motion on solicitor and client basis and order the moving party to pay them forthwith unless the court is satisfied that the making of the motion, although unsuccessful, was nevertheless reasonable."

for an application, there are factual issues in dispute and your application should be converted into an action[5].

Commercial List

The Commercial List is a special court designed to provide timely resolution of disputes in commercial matters. Cases on the commercial list move quickly, from notice of application to trial in six to eight months and faster if you want. Disputes under the *Commercial Tenancies Act* are not specifically listed as matters which will be dealt with by the Commercial List[6], however, there is a provision for applying to a judge of the Commercial List to have your matter heard by that court. This would certainly be an option for a commercial leasing matter that requires fast action.

Summary Application for Possession

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5 Rule 14.05.

6 The Commercial List practice direction provides as follows:
"Matters Eligible for the Commercial List

1. Matters which may be listed on the Commercial List are applications, motions and actions which in essence involve the following:

(a) *Bankruptcy and Insolvency Act;*
(b) *Bank Act,* relating to realizations and priority disputes;
(c) *Business Corporations Act (Ontario) and Canada Business Corporations Act;*
(d) *Companies' Creditors Arrangements Act;*
(e) *Limited Partnerships Act;*
(f) *Pension Benefits Act;*
(g) *Personal Property Security Act;*
(h) receivership applications and all interlocutory motions to appoint, or give directions to, receivers and receiver/managers;
(i) *Securities Act;*
(j) *Winding-Up Act;* and
(k) such other commercial matters as a judge presiding over the Commercial List may direct to be listed on the Commercial List (*see 771225 Ontario Inc. v. Bramco Holdings Co. Ltd.* [1993] O.J. No. 1772).

In considering whether to make a direction under sub-paragraph 1(k), the judge may take into account the current and expected caseload of matters listed on the Commercial List."

Part III of the *Commercial Tenancies Act* offers a summary procedure for a landlord to obtain possession of its premises. This is a little used remedy as it only allows a claim for possession at the end of the lease, and no claim for damages or rent, except for overholding rent. It is an application, which is commenced by a notice of application. The relief sought is a declaration that the tenancy is terminated and the landlord is entitled to possession of its premises and that a writ of possession issue, directed to the appropriate Sheriff and directing the Sheriff to forthwith take possession of the premises and return them to the landlord. A action for possession is most useful where you want to get rid of a pain-in-the-neck tenant, and nothing more.

Simplified Procedure - rule 76

The simplified procedure is available for claims under $25,000. Under this rule, procedures have been simplified to encourage the quick and economical adjudication of claims where smaller amounts are at stake. Some highlights are:

- no examination for discovery or cross-examination on affidavits filed on motions;
- the parties may agree to a summary trial in which the evidence in chief is introduced by affidavit;
- at a summary trial there are time limits set on examinations and cross-examinations;
- the test for granting summary judgment is lower;
- there are cost consequences to a party who recovers less then $25,000 and did not bring its action under the simplified procedures

Small Claims Court - Provincial Court (Civil Division)

The monetary limit of the Small Claims Court is $6,000, plus interest and costs. A plaintiff cannot unreasonably split its cause of action to bring it within jurisdiction of the Small Claims Court. For example if the tenant is in arrears for 6 months rent at $3,000 per month for a total of $18,000, the landlord cannot bring three actions each for two months rent in order to bring it within the jurisdiction of the court. However, the Supreme Court stated in *Kelly Douglas v. Highway Properties*[7] the landlord may sue for each month's rent as it comes due. The landlord may take advantage of this and bring separate actions for each month's (or two months') rent provided that: (a) the lease has not been terminated, and (b) the landlord issues its claim in the Small Claims Court immediately after the rent has accrued, for the full amount owing on that date. Small Claims Court judges don't like this, but it does work.

Mandatory Mediation

A mandatory mediation pilot project was started in Ottawa on January 1, 1997. It moved to the rest of the province as on January 1, 1999. All case managed cases in Toronto after January 1, 1999, will be subject to a four hour mandatory mediation session. The mediators are selected from a roster of court-connected mediators who are paid $125.00 per hour for a four hour mediation session consisting of one hour for preparation, and three hours for the mediation session. The fee is split by the parties. Mandatory Mediation is now an added cost of litigation, however, if the mediation is instrumental in resolving the dispute then it is certainly good value.

Private Mediation

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7 [1971] S.C.R. 562.

Retired judges and senior practitioners are now offering ADR services. Private mediators are paid by the hour and the rates charged generally reflect their experience and stature in the profession. While retired judges, senior practitioners and experienced mediators tend to charge more then the $125.00 per hour charge for mandatory mediation, again, if they are able to resolve the dispute then it is certainly good value.

With the introduction of Mandatory Mediation we have seen an explosion in the number of mediators and with it some price competition (read undercutting of fees) in order to attract business. It is too early to say what impact this explosion in mediators will have on the litigation process.

From a landlord-tenant perspective, mediation may be most useful where there is an ongoing tenancy and a genuine dispute has developed which needs to resolved without destroying the business relationship between the landlord and tenant. Mediation is probably well advised as opposed to no holds barred litigation.

II. SPECIFIC COMMERCIAL LEASING TIPS AND TACTICS

The Agreement to Lease

In most commercial lease transactions, the agreement to lease is the equivalent of the agreement of purchase and sale, being the document from which everything flows. The agreement to lease ranges from a one page letter agreement to a long complex document larger then some standard commercial leases.

In order to be binding, the agreement to lease must include six essential elements:

- The parties
- Description of the premises to be leased;
- Commencement date of the term;
- Duration of the term;
- Rent, if any;
- All material terms of the contract that are not matters incidental to the relationship of landlord-tenant.[8]

The agreement to lease must also pass the *Statute of Frauds*[9] test being; "unless it be by deed or note in writing signed by the party so assigning, granting, or surrendering the same, or the

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8 *Ossory Canada Inc. v. Wendy's Restaurants of Canada Inc.* [1997] O.J. No. 5168

9 R.S.O. 1990 c.S. 14 s.2

party's agent thereunto lawfully authorized by writing or by act or operation of law as it pertains to an interest in land". In short, it must be in writing, subject to part performance and any other legal doctrines which have developed to deal with the *Statute of Frauds*.

Compelling the Other Party to Sign the Lease

An agreement to lease typically requires the parties to execute a more detailed lease document, usually in the "landlord's standard form", at some point in the future.

So what happens if no lease is signed?

To avoid this problem, many landlords try to enforce a strict "no lease, no key" policy.

Still, there are many tenants in possession on just a short letter agreement or offer to lease. This initial agreement will be binding on both the landlord and the tenant, so long as the agreement contain the six basic requirements for a lease noted above. However, where the agreement to lease also provides that the tenant will sign a lease in the landlord's standard form and the tenant has been provided with that form of lease but has not signed it, in a subsequent dispute, the tenant may be bound by the terms of the landlord's full form lease.[10]

Will a court compel a tenant to sign a lease? At least in Ontario, the answer appears to be yes.[11] However, before threatening a tenant with a "sign or else" ultimatum, landlords should be aware

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10 *Sally Wasserman Interiors & Gifts Inc.* v. *Centre City Capital Ltd.*, [1996] O.J. No. 1295 (Gen. Div.).

11 *Ferleo Tile Inc.* v. *Nubilis Holdings Ltd.*, [1993] O.J. No. 870 (Gen. Div.).

that the Saskatchewan Court of Appeal has ruled that such a threat can amount to an anticipatory breach of the lease by the landlord, whereby the tenant is entitled to elect to sign, or terminate the lease (much to the surprise and chagrin of the landlord in that case who only actually wanted to "scare" the tenant into compliance).[12]

However, where the landlord never provides the tenant with its standard form lease, it is difficult to see how a tenant can be bound by that lease. In this circumstance, the parties' relationship will probably be governed by the original agreement to lease, no matter how sparse.

Specific Performance of a Lease

After an agreement to lease or lease is signed, can either party apply for specific performance of the lease agreement to either:

(a) compel the tenant to take possession, or

(b) compel the landlord to allow the tenant into possession?

Specific performance is a discretionary remedy which will only be granted where the common law remedy of damages would not be an adequate one in the circumstances. In *1110049 Ontario Ltd. v. Exclusive Diamonds Inc.*,[13] the Court of Appeal noted that in cases involving the sale of land it is presumed that real property is unique. However in the *Exclusive Diamonds* case the Court of Appeal did not find that leased premises in a regional shopping mall were sufficiently unique to support an order for specific performance. Instead the court found that damages were

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12 *Homer* v. *Toronto-Dominion Bank* (1990), 83 Sask. R. 300 (C.A.).

13 *1110049 Ontario Ltd. V. Exclusive Diamonds Inc.* (1995) 25 O.R. (3d) 417 (C.A.)

an adequate remedy.

There are cases where residential leases are subject to specific performance,[14] however, granting specific performance of a commercial lease before the tenant goes into possession is rare. This being said there is the decision in *Applewood BMW Inc.* v. *S. Ligouri Investments Inc.*[15] where a tenant was successful in obtaining an order for specific performance.

As for a landlord obtaining specific performance, it is hard to imagine a case where damages would not be an adequate remedy for a landlord. One scenario for specific performance would be where a major anchor tenant refuses to enter into possession thereby jeopardizing the entire development. The landlord could fashion a compelling argument for specific performance, particularly if the entire project depends on the presence of the anchor. On the other hand, the landlord's damages, while potentially large, could be readily quantified.

When a tenant doesn't take possession, the calculation of landlord's damages is straight forward, it is the lost rent. The more interesting question is does the landlord have a duty to mitigate? Could the landlord not simply sit back and take the position that its premises are leased to the tenant and sue for its rents as it came due. Theoretically this is correct, as the landlord would be suing for rent under its lease. However a judge would probably frown on a landlord who makes no effort to re-rent its property. The more prudent course may be to make reasonable efforts to

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[14] See Williams & Rhodes, Canadian Law of Landlord and Tenant, Sixth edition; section2:6:2

[15] [1996] O.J. No. 1579 (Gen. Div.) and related cases.

mitigate[16].

Interesse Termini

The question of a tenant's ability to succeed on a claim for specific performance of a lease before it has possession of the leased premises is further complicated by the old English doctrine of *interesse termini*. "At common law, whether the term is to commence at once or in the future, the lessee has no more than an *interesse termini* [an interest in a term], until he actually takes possession of the demised premises."[17] This doctrine has been abolished for residential tenancies and in some jurisdictions, but it is alive and well in Ontario.

Black's Law Dictionary, sixth edition, defines *interesse termini* as follows: "An interest in a term. That species of interest or property which a lessee for years acquires in the lands demised to him, before he has actually become possessed of those lands; as distinguished from that property or interest vested in him by the demise, and also reduced into possession by an actual entry upon the lands and the assumption of ownership therein, and which is then termed an "estate for years"".

Where the tenant has not entered into possession its remedy is in damages, which are limited to the difference in rent between the demised premises it was denied and any replacement premises

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16 On mitigation, Professor Waddams writes as follows: "The plaintiff is barred from recovering in respect of loss that could have been avoided by acting reasonably. What is reasonable has been called a question of fact depending on the particular circumstances of the case. However, as with remoteness, a finding that the plaintiff ought to have mitigated is not a simple question of fact because it involves a legal conclusion. In case of doubt, the plaintiff will usually receive the benefit, because it does not lie in the mouth of the defendant to be over-critical of good faith attempts by the plaintiff to avoid difficulty caused by the defendant's wrong."The Law of Damages (Looseleaf Edition) S.M. Waddams. Canada Law Book, page 15-7.

17 Williams & Rhodes, Canadian Law of Landlord and Tenant, Sixth edition; page 3-56

it may rent for the same business. The tenant cannot recover prospective loss of profits for the business it would have carried on upon the premises it was denied.[18]

It is interesting to note that in the case of *Applewood BMW Inc.* v. *S. Ligouri Investments Inc.* where specific performance of a lease was granted, the doctrine of *interesse termini* was not raised by either party.

Rectification of a Lease to conform with the Agreement to Lease

What happens when you discover that the lease, which weighs in at over 2 pounds, does not say what you thought it would say at article 13.03 (h) (iii) (C) (1.1) which deals with property taxes.

Mistake and Rectification

To succeed on a claim for rectification, one must convince the court that the parties had an agreement but they did not write it down correctly.

In *HF Clark Limited v. Thermidari Corp. Limited,*[19] Justice Brooks JA, in an often quoted passage, sets out the equitable principle of rectification:

> "When may the court exercise jurisdiction to grant rectification? In order for a party to succeed on a plea of rectification it must satisfy the court that the parties, all of them, were in complete agreement to the terms of their contract but wrote

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18 Williams & Rhodes, Canadian Law of Landlord and Tenant, Sixth edition; page 3-57

19 [1973] 33 DLR 3d 13 (Ont. C.A.)

> them down incorrectly. It is not a question of the court asking to speculate on the parties intention, but rather to make an inquiry to determine whether the written agreement properly records the intention of the parties as clearly revealed in their prior agreement. The court will not write a contract for businessmen or others but rather through the exercise of its jurisdiction to grant rectification in appropriate circumstances, it will reproduce their contract in harmony with the intention clearly manifested by them, and so defeat claims or defence which would otherwise unfairly succeed to the end that business may be fairly and ethically done."

In deciding this question, the court does not look at what the parties today think the provision means or what one of the parties intended it to mean. The court must decide what, if anything, the parties agreed to, at the time the agreement was made. Where the agreement to lease differs from the lease signed by the parties, this would generally be good evidence of what the parties agreed to at the time.

The decision in *Strategeas v. Lloyd Parish Holdings Limited*[20] provides in interesting glimpse into the law of rectification. In this case the tenant purchased a restaurant business in 1981. The purchase agreement provided that the tenant would enter into a lease in the "usual form". The tenant signed a Dye and Durham lease form which was reviewed by his lawyer prior to signing. Dye and Durham's lease form grants the landlord a right to terminate the lease in the event the property is sold. In 1990, nine years after the lease was signed, the landlord found a buyer for

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[20] (1991), 17 R.P.R. (2d) 293 (Ont. Ct. (Gen. Div.))

its property and relying on the termination right in the lease gave notice of termination. The tenant applied to have the lease rectified.

The court found that the termination clause could not be considered a usual covenant. The clause was found to be completely contradictory to the granting of the lease as it gave the landlord the power to destroy the tenant's investment in the restaurant. The court went on to find that given the importance of the clause, the landlord's solicitor had an obligation to point out the clause to the tenant's solicitor and not just assume that the tenant was aware of the clause and had accepted it.

Waiver and Estoppel

The most common example of a waiver in landlord-tenant matters occurs when the landlord accepts rent that comes due after it has learned of a default under the lease entitling it to terminate. The majority of cases find that the acceptance of rent after the landlord becomes aware of a default acts as a waiver of the landlord's right to forfeiture in respect of that default.[21] However, there are cases where the acceptance of rent did not constitute a waiver of the default[22].

When there has been a alleged breach of the lease, other issues surrounding the application and interpretation of the terms of a lease may arise years after the lease is signed. Often, the parties

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21 *R.* v. *Paulson* (1920), 54 D.L.R. 331 (P.C.); *Lippman* v. *Lee Yick* [1953], O.R. 514 (H.C.),

22 *1012765 Ontario Inc.* v. *Regional Shopping Centres Limited*, Ont. Ct. (Gen. Div), June 15, 1993, Rosenberg J.

have been doing things one way for years, and then someone, for some reason decides to read the lease closely and discovers that the parties have not been conducting themselves in accordance with the express terms found in the lease. What then?

It is generally acknowledged that the doctrine of equitable estoppel has its origin in *Hughes* v. *Metropolitan R. Co.* (1877), 2 App. Cas. 439.

> In that case ... the parties entered into negotiations for several months which ultimately failed. Then tenant proceeded to repair but was unable to do so within the original six-month period. The landlord moved to forfeit the lease six months after the first notice. It was the tenant's position that the six month period for repairs ran from the date on which the negotiations broke off. In dismissing the landlord's appeal, Lord Cairns said at p. 448:
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> > ... it is the first principle upon which all Courts of Equity proceed, that if the parties have entered into definite and distinct terms involving certain legal results -- certain legal penalties or legal forfeiture -- afterwards by their own act or with their own consent enter upon a course of negotiation which has the effect of leading one of the parties to suppose that the strict rights arising under the contract will not be enforced, or will be kept in suspense, or held in abeyance, the person who otherwise might have enforced those rights will not be allowed to enforce them where it would have been inequitable having regard to the dealings which have thus taken place between the parties.

The legal elements supporting an estoppel were outlined by Martland J. in the *Canadian Superior Oil* case at p. 939 S.C.R. [quoting from *Greenwood* v. *Martins Bank Ltd.*, [1933] A.C. 51 at 57], and are as follows:

> The essential factors giving rise to an estoppel are I think:
>
> (1) A representation or conduct amounting to a representation intended to induce a course of conduct on the part of the person to whom the representation was made.
>
> (2) An act or omission resulting from the representation, whether actual or by conduct, by the person to whom the representation was made.
>
> (3) Detriment to such person as a consequence of the act or omission.[23]

It is also important to note that questions of estoppel, waiver and amendments to a lease may not matter if the current landlord obtained its title to the property through a mortgagee.

The mortgagee in possession, *Goodyear v. Burnhamthorpe*, Old Law Rediscovered

BUYER BEWARE! TENANTS BE AWARE! : THE "GOODYEAR" CASE[24]

The Ontario Court of Appeal in the case of *Goodyear Canada Inc. v. Burnamthorpe*

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23 As cited in *M.L. Baxter Equipment Ltd. et al.* v. *Geac Canada Ltd. et al.* (1982), 36 O.R. (2d) 150 at 157 and 158-59 (H.C.J.).

24 We thank Kenneth A. Beallor of Daoust Vukovich Baker-Sigal Banka, for allowing us to use this article which he wrote for the Shopping Centre News.

Square Inc.[25], confirmed a well-established but sometimes overlooked principle that tenants and landlords of property that is subject to a pre-existing mortgage (as well as their landlords and their lenders) should be aware of.

Where a lender has a mortgage that pre-dates a lease (or renewal agreement that is not pursuant to an option contained in the lease) and the lender and tenant have not signed an agreement recognizing the lease and requiring the tenant to accept the mortgagee as its landlord if the mortgagee takes possession, and the mortgagee takes possession of the property and does not evict the tenant, the tenant can refuse to accept the mortgagee as its new landlord and treat its lease as terminated, or it can recognize the mortgagee as its new landlord by paying rent to it. If it accepts the mortgagee as its new landlord, it becomes a tenant of the mortgagee under the terms of its previous lease, *except that it is only a tenant from year to year*. When this happens, unless the parties enter into a written agreement to the contrary, both the lender, or a purchaser from the lender, and the tenant, can terminate the lease if either gives at least six months notice effective at the end of the lease year.

Here is a simplified report of what happened in the *Goodyear* case. Goodyear became a tenant of property that was already subject to mortgages.

Non-disturbance agreements from the mortgagees were *not* obtained by Goodyear. The owner of the properties went into default under the mortgages and a mortgagee ultimately took possession of the property and directed Goodyear to continue to pay its rent cheque to the

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[25] OR cite for case

property manager.

Several months later, the mortgages and related security were sold by the lender to a purchaser (Burnamthorpe) which foreclosed on the properties, thus becoming the new owner. Goodyear then took the position that it was just a year to year tenant and gave notice to Burnamthorpe terminating its lease effective at the end of the lease year. Burnamthorpe took the position that Goodyear was bound for the full term of its original lease and that it was not merely a year-to-year tenant.

Burnamthorpe was dismayed to find out that Goodyear was permitted to terminate its tenancy. The Court of Appeal held that when the lender took possession of the property, and Goodyear paid the rent to the lender, a new year-to-year tenancy was created between the lender and Goodyear. Accordingly, when Burnamthorpe purchased the mortgages and related security, Burnamthorpe acquired the lenders' interest which included the year-to-year tenancy and not the original lease that Burnamthorpe thought it had acquired.

What could have been done to preserve the term of the original lease? Firstly, the lender and tenant could have entered into an agreement (a "non-disturbance agreement") in which the tenant agreed that it would recognize the lender, or a purchaser from the lender, as its landlord if the lender takes possession of, or sell, the property. In the same agreement, the lender would agree to permit tenant to remain in the premises for the balance of the term of its lease and any renewal (as long as the tenant did not default). Secondly, as is the case with most lenders, the lender had obtained an assignment of the owners' leases as collateral security for its mortgage. If the lender, had preserved the lease, by giving the tenant a notice before taking possession of

the property, that it was no longer holding the owner's interest in the lease merely as security, and was actually taking over as landlord, the tenant might have been bound for the full term of the lease. (Note the Court of Appeal was of the view that even if the lender had given such notice before taking possession the lender would not have preserved the lease).

As a result of the decision in *Goodyear*, Tenants should be aware that the actions of a lender could open an avenue for the tenant to rid itself of a lease it is looking to get out of. Conversely, tenant's should be cautioned to obtain non-disturbance agreements if they do not want to face early termination in the event the owner runs into financial difficulties.

Furthermore, lenders taking possession of leased properties under their mortgages, and purchasers of leased properties from lenders selling pursuant to their security, should beware: the leases you are assuming, and which may be the basis upon which you are obtaining financing, may in fact be year-to-year tenancies. Careful investigation and professional advice should be sought prior to closing any such transaction.

Distress

No paper on landlord tenant issues would be complete without a word on distress. The first point to remember when considering a distress is that the landlord's right to distrain for arrears of rent arises under the lease. Accordingly once the lease is terminated the landlord's right to distrain is lost. When a tenant is in default for non-payment of rent the land lord must elect to either distrain or terminate the lease, it cannot terminate and then distrain. Nor can the landlord terminate before its distress has been completed and there are still arrears of rent.

From a litigation point of view it is useful to note that Part II of the *Commercial Tenancies Act* provides a summary procedure for resolving disputes which arise on a distress.

When dealing with a distress, from a tenant's perspective one should keep in mind Sections 48 and 50 of the *Commercial Tenancies Act*, Section 48(1) states that where any tenant fraudulently or clandestinely removes goods or chattels from the premises in order to prevent the landlord from distraining them for arrears of rent, the landlord may within thirty (30) days after such removal, follow such goods and distrain upon them. Section 50 states that if a tenant fraudulently removes his goods or if any person wilfully and knowingly aids or assists him in os doing or in concealing them, then such persons are liable to pay to the landlord double the value of such goods.

In *Cowie Industrial Developments v. National Clearance Warehouse Ltd.*[26] the court found the two principals of the tenant company liable for $1,000,000. in damages (ouch) for fraudulently removing the tenant's goods.

THE DISTRAINING LANDLORD: FOR WHOM ARE YOU REALLY COLLECTING?[27]

Across Canada (except in Quebec) landlords can seize and sell (distrain) the goods of a tenant to satisfy rental arrears. Numerous technical and arcane rules must be followed. Otherwise, the landlord may be liable for damages. Even when a distress is done properly, the landlord may find that the proceeds must be handed over to another party, leaving the landlord with little to

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26 [1997] O.J. No. 1855, Court File # 93-CQ-37050CM (Ont. Ct. Gen. Div.)

27 We thank Eric K. Gillespie of Daoust Vukovich Baker-Sigal Banka, for allowing us to use this article which he wrote for the Shopping Centre News.

show for its efforts. There are several reasons.

First, if a bank has taken security under the *Bank Act* and issued the required notice prior to the rental arrears accruing, the bank will have a prior claim to the sale proceeds. Therefore, it is a good idea for a landlord to do a Bank Act search before seizing inventory.

Second, the landlord can only distrain against "chattels" (not fixtures), and the case law dealing with the difference between chattels (items that are not attached to the building) and fixtures (things that are attached to the building) is inconsistent. Also, chattels that are leased, or on consignment cannot be distrained. Goods sold under conditional sales contracts can only be distrained to the exient of the tenant's equity interest in them (which is often very little). The landlord selling off goods might find that the sale proceeds are due to another party. One protection is to do a search under the *Personal Property Security Act* (or similar legislation), but that search does not disclose everything that needs to be known. Leases of equipment, and consignments of goods are not registered and therefore are not detectable on registration searches. Some limited protection might by achieved by consulting with the tenant (who may not be candid), and by asking the bailiff to search for tags or stickers identifying any owner/lessor. Even so, the landlord may still be approached later by someone who claims the sale proceeds for their own.

Third, even where the landlord's right to distrain has priority over a secured creditor, there is a risk that before the distraint sale is completed, the tenant may become bankrupt. This blocks the distress, and puts the secured creditor back on top in any priority dispute. In such a case, the goods must simply be handed over to the trustee in bankruptcy. Even if the distress sale is

completed before the bankruptcy, if the distress occurs within three months of the bankruptcy it will be treated as a fraudulent preference. The proceeds will have to be handed over to the trustee in bankruptcy, and the landlord will get little benefit from the distress.

Fourth, and perhaps most insidious, are the statutory liens that arise and take priority over the landlord's interests. The so-called "super liens" for GST, federal income tax etc. have been around for some time. These create a first charge on any monies realized by the landlord. The real difficulty is that clearance certificates detailing the tenant's account(s) are not issued. Consequently, distraint sales must often be conducted "blindly". The odds are that if a tenant is behind in rent, it is probably in arrears elsewhere. As well, provincial legislation creates liens for unpaid retail sales tax etc. **In a recent change that all landlords in Ontario should be aware of, under the *Retail Sales Act* and certain other statutes, landlords who sell a tenant's goods are now liable to the provincial government not just for the value of the goods seized, but for the entire amount of tax that the tenant owes.** As a result, a landlord MUST obtain a certificate before selling any goods, or be open to potentially staggering liabilities. Fortunately, most provincial agencies will provide clearance certificates promptly.

Where does this leave the landlord? Perhaps the best advice is to conduct the appropriate searches and obtain as many clearances as possible BEFORE distraining; retain a qualified reputable bailiff, and STOP short of selling any goods. In many cases, simply seizing goods is enough to prompt a resolution to the arrears situation. If that does not work, selling the goods, considering what is said above, might cause more problems than it solves.