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Withholding Rent: Gutsy or Risky?

In the face of economic downturn, uncertainty and pandemic lockdown, tenants value liquidity. Many view their rent obligations as daunting. When cash is scarce, the health of the tenant's business takes on immediacy.

Withholding rent is not a decision made lightly. Deliberate non-payment of rent frees up capital that may facilitate short-term survival. Or, it may provide landlords with an opportunity to pounce.

The question is: can non-payment pay off? Does it signal bold manoeuvring or cavalier disregard for contractual obligations?

Withholding rent yields certain inevitable steps: first, the landlord issues a notice demanding payment. What happens when the tenant still refuses to pay? The landlord must decide on the next step. In most Canadian provinces, the landlord can exercise the self-help right of termination. Alternatively, it can sue for arrears. If the landlord terminates, a duty to mitigate (make reasonable efforts to replace the tenant) arises. Concurrently, following Lease termination, the tenant may seek to reinstate the Lease. The deadline for such an application ("relief from forfeiture") is not legislated and therefore indeterminate.

A tenant who is desensitized to conflict (or just willing to play the game of chicken described above) may decide to withhold rent. This is the age-old standoff known as, "see you in court".

Tenants might feel a false sense of comfort during such a dispute because Courts have historically been reluctant to deny a tenant relief from forfeiture. This type of equitable relief is commonly granted to tenants, allowing them to rehabilitate and stay in business. Although usually awarded with conditions (e.g., payment of arrears plus interest, payment of legal fees, etc.), which may be onerous, relief from forfeiture remains readily accessible. Consequently, many landlords hesitate to terminate – a fact many tenants count on.

As each situation is fact-specific, we offer no simple answer. However, recent Court decisions offer insight as to when withholding rent may not be a successful strategy.

Hunt's Transport Limited v. Eagle Street Industrial GP Inc.

This Ontario case involved the non-payment of additional rent charges disputed by the Tenant, who operated a commercial trucking and logistics company throughout the COVID-19 pandemic. The 2018 Lease estimated additional rent at \$1.95 psf for year 1. The Landlord increased the estimate to \$2.50 psf for 2019. With the Landlord's year-end reconciliation, the rate rose to \$3.15 psf, and the Landlord provided its 2020 estimate at \$3.24 psf. Frustrated, the Tenant audited the Landlord's records and claimed that the invoices did not support the amounts billed, citing double charges as well as expenses the Lease excluded from additional rent. The Tenant withheld payments. The Landlord delivered a notice of default demanding \$173,415.24 in arrears, plus interest.

The Lease required continued performance of contractual obligations regardless of ongoing disputes, and payment of all rent without deduction, set-off, or abatement.

The Tenant applied for relief from forfeiture. It pled an intention to conserve resources during the pandemic. The Court was unsympathetic. In considering whether to grant the discretionary relief, it considered three factors established by the Supreme Court of Canada: (i) the conduct of the party seeking relief (particularly whether it was "wilful"); (ii) the gravity of the breaches; and (iii) the disparity between the property's value and the total damages caused by the breach.

The Court found the Tenant's conduct "wilful" and characterized the withholding as a "self-help" remedy not contemplated by the Lease. The Court viewed the Landlord's threat of termination as the only means of countering the Tenant's unreasonable conduct. The Tenant also argued that

businesses ineligible for government support should receive relief from the Courts. The Court refused to accept COVID-19 considerations as relevant. It noted that, despite the lack of government pandemic support for the Tenant's industry, it was never required to cease operations. As such, the Tenant's argument that it suffered from the economic downturn deserved little merit.

The Court held the Tenant had not satisfied its onus to demonstrate that relief should be granted. However, it exercised its discretion to order *temporary* relief from forfeiture for twenty days, conditional upon curing all unpaid amounts, plus interest. In short, the Court rapped the Tenant's knuckles, ordered it to pay all rent with interest, but kept the Lease alive.

Cherry Lane Shopping Centre v. Hudson's Bay Company ("HBC")

Immediately following the pandemic's announcement in March 2020, HBC decided to withhold rent as of April 1, notwithstanding that its Lease required payment of all rent without delay, set-off, or abatement. The Landlord issued a notice of default and terminated the Lease after the requisite period elapsed without cure.

HBC argued the Landlord should share the burden of the pandemic, and that it was entitled to pay reduced rent. It argued that the Landlord failed to maintain a first-class shopping centre. The parties executed a consent agreement in January, 2021 whereby HBC agreed to pay the Landlord 50% of the ongoing rent with the remainder paid into its solicitors' trust account. In its application for relief, HBC argued the Court should maintain the status quo

arrangement set out in the consent agreement rather than order HBC to pay all rent.

The Supreme Court of British Columbia awarded relief from forfeiture, conditional upon payment of all arrears, plus interest, and timely payments of future rent.

HBC v. Oxford Properties

As in *Cherry Lane*, the Tenant withheld rent starting April, 2020. The Landlord gave notice of default, which HBC did not remedy by the deadline, and exercised its right of forfeiture. HBC immediately moved for an injunction to restrain the Landlord from terminating AND sought relief from forfeiture. An interim ruling granted an injunction on payment of 50% of both arrears and ongoing rent, pending a full hearing on whether HBC was entitled to pay something less than all rent. Ontario's Superior Court of Justice heard full arguments on June 8, 2021 and gave its ruling on June 24, 2021: the Tenant was ordered to pay all rent, plus interest, as a condition of obtaining relief from forfeiture.

Conclusion

Tenants should not take relief from forfeiture for granted. Even if a Court grants relief, it may impose stringent conditions, including the obvious one: payment of rent. It is also possible (however unlikely) that relief may be denied. These cases show that tenants should be wary of advancing arguments to the effect that the negative economic impacts of COVID-19 may dilute the obligation to pay rent. Courts will slice through these excuses if the Lease does not expressly stipulate that such an event suspends the rent obligation (which most *force majeure* clauses typically do not do).

This publication is a general discussion of certain legal and related developments and should not be relied upon as legal advice. If you require legal advice, we would be pleased to discuss the issues in this publication with you, in the context of your particular circumstances.



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