

HBC's Efforts to Withhold Rent Due to Landlords' Failure to Maintain "First Class" Shopping Centres

COVID-19 | Commercial Landlord | Commercial Tenancies Act | Litigation | Litigation & Dispute Resolution | Retail Shopping

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Further Addendum

In *Hudson's Bay Company ULC Compagnie de la Baie D'Hudson SRI v. Oxford Properties Retail Holdings II Inc.*, 2022 ONCA 585 (CanLII), the Court of Appeal dismissed HBC's appeal, stating as follows:

I accept that the impact of COVID-19 and the restrictions on retail businesses that followed can be taken into account when setting the terms of relief for forfeiture. For example, the problems associated with COVID-19 may dictate a term allowing the tenant some additional time to bring itself into compliance with the lease. I do not, however, accept that the economic impact of COVID-19 can be taken as a basis for fundamentally altering the remedy from one of relief from forfeiture to one imposing new terms in the lease.

The Court of Appeal allowed the landlord's cross-appeal and determined that the motion judge erred in deferring HBC's rent obligations for reasons unrelated to HBC's ability to bring itself into compliance with the terms of the lease relating to rent payment. In the Court of Appeal's view, the length of any deferral should have reflected the time needed by HBC to bring itself into compliance with the lease.

During the COVID-19 pandemic, with consumers leery of indoor shopping and retailers being forced to keep their doors closed due to health regulations, many commercial tenants are staring down the barrel of eviction due to their failure to pay rent. One retailer in Canada, Hudson's Bay Company ("HBC"), which professes to be North America's oldest company, has decided to go on the offensive by filing a Statement of Claim in the Ontario Superior Court of Justice against a number of affiliated companies (the "Landlords") who own shopping centres in Canada in which HBC operates.

HBC's failure to pay rent during the pandemic has been widely [reported](#). There can be little doubt that the revenue from bricks and mortar retail stores has been dramatically impacted by the pandemic. According to HBC's Statement of Claim, however, negotiations with the Landlords regarding the payment of rent were halted when the Landlords "surreptitiously commenced litigation against HBC in Québec." [TheGlobe and Mail](#) has reported that the Québec lawsuit is part of a pattern of HBC's Landlords seeking court orders for unpaid rent including cases in West Vancouver and Miami. Recently, an interim decision of Justice Hainey in Ontario prevented HBC's eviction from Hillcrest Mall in Richmond Hill. Instead, Justice Hainey split the difference and [ordered](#) that 50% of the outstanding rent (or approximately \$660,000) to be paid to the Landlord.

It is perhaps not surprising, then, that a commercial tenant in HBC's position may attempt to turn the tables and blame its landlord for its inability to pay rent. HBC's Statement of Claim seeks, amongst other things, a declaration that HBC does not have to pay rent until certain breaches in the lease agreements are cured, a disgorgement of rent paid since April 2020 (for three locations in which they paid rent under "protest"), an order permitting HBC to access the air handling systems of the shopping centres, and an interim order preventing the landlords from evicting HBC.

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HBC alleges that customer traffic in the shopping malls has been down by 70% since reopening and sales have fallen by just as much. The claim highlights some facts that every retailer knows to be true, that "(c)ustomer traffic levels and dwell time have fallen precipitously".

At the heart of the claim lies an accusation that the Landlords have failed to provide "first class shopping centres" and the corresponding benefits of customer traffic. HBC alleges that a "first class shopping center" is perceived by the public to be clean and safe while providing high levels of customer traffic and a low vacancy rate. These characteristics are alleged to be lacking in the shopping centres due to the Landlords' breaches of the leases and "refusal to take appropriate measures" during COVID-19. Specifically, the Statement of Claim alleges that the Landlords have:

- refused to upgrade the HVAC systems to stop the transmission of the virus through aerosols;
- refused to install air filters to a certain high standard;
- refused to install touchless exterior and interior doors;
- refused to upgrade washrooms;
- refused to improve pedestrian controls; and
- refused to increase mall personnel to ensure compliance with proper safety protocols.

The Statement of Claim also takes issue with the lack of marketing the Landlords have undergone to reassure the public and a lack of information sharing regarding the air quality. Essentially, HBC alleges that they have been denied their right to "quiet enjoyment" of its leased properties. Obviously these are merely allegations and HBC's claim will be adjudicated or resolved in due course.

Courts are generally leery of a commercial tenant's complaints about a landlord's conduct when assessing a tenant's failure to pay rent. Absent a specific provision in a commercial lease, there is little recourse available to a tenant by way of demand for abatement or offset of unpaid rent. However, tenants can sue a commercial landlord for damages or terminate the lease on the basis of breach of the covenant of quiet enjoyment and/or duty to maintain the premises.

Commercial leases often contain an express or implied term for the right to "quiet enjoyment," which means that a landlord must not "substantially interfere" with a tenant's enjoyment of the premises. A landlord's interference with the quiet enjoyment of the tenant is actionable when it is "grave and permanent such that it renders the premises substantially less fit for the purposes for which it was leased": *London Prestige Ltd. v. Wellington Harlech Centre Inc.*, 2019 ONSC 2364 (CanLII) at para. 31, citing *Stearman v. Powers*, 2014 BCCA 206, 373 D.L.R. (4th) 539, at paras. 18-19.

If a tenant establishes that a landlord has breached the term of quiet enjoyment, the tenant may be able to establish a claim for damages. However, this does not lead to an automatic right of a tenant to refuse to pay rent or terminate a lease based on damages arising from the landlord's failure to provide quiet enjoyment.

In *Bassiouny v. Lo*, 2008 CanLII 68883 (ON SC), the Court determined that a restaurant's right to quiet enjoyment had been breached due to their landlord's refusal to fix fire damage and leaks in the roof which substantially interfered with the restaurant's business. The Court noted that being a restaurant made them particularly susceptible to the sanitary conditions of the premises and potential dangers to health. There was no evidence of intentional deprivation by the landlord of the tenant's enjoyment of the property. Nevertheless, the leaks in the roof and fire damage caused problems that were so extensive that they prevented the restaurant from carrying on business. The Court found that the landlord fundamentally breached the covenant to repair and to provide quiet enjoyment of the premises. The restaurant had ceased operating in the premises, however, so the Court did not have to address whether the restaurant could off-set damages against unpaid rent going forward.

In contrast, a landlord's failure to repair and maintain the building may amount to a fundamental breach of the lease, thereby entitling a tenant to terminate the lease. A "fundamental breach" entitles a tenant to terminate a lease, irrespective of whether or not it also amounts to a breach of the covenant for quiet enjoyment. The key distinction is whether the breach at issue is a breach of the covenant of quiet enjoyment giving rise to a damage claim, or whether the breach is one that makes further performance of the lease impossible or deprives the tenant of substantially the whole benefit of the lease: *Shun Cheong Holdings B.C. Ltd. v. Gold Ocean City Supermarket Ltd.*, 2002 BCCA 451 (CanLII) at para. 11. In commercial lease disputes, the term fundamental breach has been described as the premises being "uninhabitable": *Felton Brushes Limited v. Atlantis Properties Hamilton Inc.*, 2020 ONSC 2315 (CanLII) at para. 24.

Whether a failure to repair and maintain premises amounts to a fundamental breach depends on the wording of the terms in the lease.

In *1723718 Ontario Corp. v. MacLeod*, 2010 ONSC 6665 (CanLII), the Court addressed the issue of whether a landlord's failure or refusal to repair a broken boiler in the middle of a Canadian winter, thereby rendering the premises too cold for the tenant to conduct his medical practice, was a fundamental breach entitling the tenant to terminate the lease. In the lease at issue, the landlord had covenanted to be solely responsible for repairing and maintaining the heating system. The Court found that the landlord's failure to fulfill his obligations under the lease entitled the tenant to terminate the lease.

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Conversely, in *Vigin G.F.R. Holdings Ltd. v. Kinder Care*, 2018 ONSC 2429 (CanLII), affirmed 2020 ONCA 120 (CanLII), the tenant argued that the lease was fundamentally breached because the landlord failed to properly maintain the premises' HVAC systems. The express terms of the lease, however, provided that the tenant was responsible for building maintenance. The Court found that the HVAC systems were not structural elements of the building and were therefore the tenant's responsibility. Further, the tenant continued to use the premises for over a year after complaining about the HVAC, which meant the tenant had elected to affirm the lease even if there was a fundamental breach. In cases of alleged fundamental breach, the party alleging the fundamental breach is required to make an election at the time of the alleged breach to either terminate or affirm the contract: *Vigin G.F.R. Holdings* at para. 134.

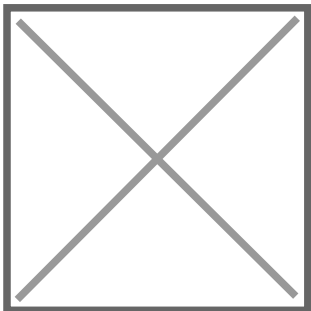
During the COVID-19 pandemic, there will be an unavoidable tension between commercial landlords and tenants given that all customer-facing businesses will require a perception of cleanliness and compliance with public health regulations in order to attract customers back to their stores. It remains to be seen whether a landlord's failure to modify buildings or shopping centres in order to comply with COVID-19 regulations amounts to either a breach of the covenant to provide quiet enjoyment or a fundamental breach of the lease. Landlords will likely only be required to show that the impact of their decisions do not amount to depriving the tenants of the entire benefit of the lease to avoid breaching the implied covenant of quiet enjoyment. Tenants will have to meet a high bar to show that their businesses are being interfered with by their commercial landlord's actions or inactions and not by government orders and the general atmosphere of concern among the general public. This will likely be a fact specific inquiry, and in HBC's case may require something more than pointing to air ventilation and a failure to maintain "first class shopping centres" (whatever that is ultimately determined by the courts to mean).

Addendum

In June 2021, the Ontario Superior Court of Justice determined that HBC's Landlord did not breach its lease by failing to meet operating standards or providing a first-class shopping centre. The court stated that making such a finding would lead to a commercial absurdity in that the Landlord would be put in a position of having to ignore provincial laws and public health guidelines in order to maintain what HBC determined was "a first-class mall". HBC was nevertheless granted relief from forfeiture as it was a model tenant before the pandemic and was attempting to navigate an unprecedented public health crisis. The court imposed payment terms so that HBC could bring its rent up-to-date: *Hudson's Bay Company ULC v. Oxford Properties*, 2021 ONSC 4515 (CanLII).

(This blog is provided for educational purposes only, and does not necessarily reflect the views of Gardiner Roberts LLP).

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