The Six-Minute Commercial Leasing Lawyer 2018

TENANT EXIT STRATEGIES

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with sincere thanks to Megan Reilkoff for her invaluable assistance

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Introduction

"*In the first place, an ounce of prevention is worth a pound of cure.*" - Benjamin Franklin

Benjamin Franklin, who is most known as one of the Founding Fathers of the United States of America, famously penned an anonymous letter entitled "Protection of Towns from Fire" to The Pennsylvania Gazette in 1735. Franklin's letter contained the above admonition to inhabitants of Philadelphia after he noted that his adopted city was ill-prepared to combat fires. Franklin embarked on a public awareness campaign that led to the establishment of organized firefighting and fire prevention. This transformed Philadelphia from being an unsafe city to one of the safest cities in America for fire prevention.

Although most people use Franklin's above axiom when referring to health, it is as relevant to the leasing context as it is to fire safety and health. Just as preventing fires is better than fighting them, so too is it better for the tenant to make sure it has a contingency plan in place before it signs its lease.

It may at first seem counterintuitive to the commercial tenant to be advised to plan for its exit before entering into a new lease, particularly when this coincides with the start of a new business, as this is generally when the tenant is feeling most optimistic about the future of its business. Exit strategies may be the furthest thing from the tenant's mind but what happens if growth is significantly more aggressive than the tenant had originally forecast and the premises are suddenly significantly too small for its burgeoning work force. Alternatively, while no one enters into a business contract with the expectation of failure, the business needs and circumstances of the tenant often change over time. As such, there are a variety of reasons why a tenant may want or need to get out of its lease at a later date, many of which are beyond its control, whether it be market forces and the economy in general or the unexpected departure of an anchor tenant of a shopping mall. It behooves a prudent tenant to plan for an early exit should circumstances change.

This paper is written from the tenant's perspective and will explore the most common lease exit strategies employed by tenants: (1) assignment and subletting, (2) early termination rights, (3) the right to contract and surrender all or part of the leased premises, (4) the right to "go dark", (5) judgement-proofing, and (6) repudiation. There are unique risks an advantages associated with each.

1. Strategy No. 1: Assignment and Subletting

When faced with premises that are no longer suitable for the tenant's purposes or are no longer affordable by the tenant, most tenants will first look to see if they can assign their lease or sublet their premises to someone else. Assigning/subletting is easily the most common exit strategy employed by tenants. This is because most leases include a right to assign or sublet with the landlord's consent. In seeking to assign or sublet, however, the tenant will be subject to a number of hurdles in addition to the requirement for landlord's consent. Before discussing these hurdles, however, let's first deal with the terminology and the legal difference between assignment and subletting.

Legal Distinction Between Assigning and Subletting

When a tenant assigns its lease, it transfers all of its right, title and interest in the premises to the assignee. Despite having assigned the lease, however, the assignor tenant is not released of its obligations under the lease and remains liable to the landlord for their performance. Despite this ongoing liability, however, the assignor tenant is not entitled to retake possession of the premises, even if its assignee goes into default.

By contrast, under a sublease, the tenant grants the subtenant the right to occupy all or part of the premises for a specified period of time and the tenant retains a reversionary interest in the premises. Typically, subleases are for the term of the lease less one day. The relationship of landlord and original tenant remains unaffected. The subtenant does not have a direct relationship with the landlord. If the subtenant defaults, the original tenant remains liable to the landlord but will, under the terms of the sublease, usually have the right to terminate the sublease and retake possession of the premises and thus mitigate its damages, either by re-occupying the premises or by re-subletting them to a new subtenant.

Landlord's Right to Consent

While a tenant has the right at law to assign its lease or sublet its premises, landlords have a legitimate interest in controlling who occupies their property and in the case of the shopping centre owner, maintaining the right tenant mix. For this reason, the assignment and subletting provisions of most leases restrict the tenant's ability to assign or sublet, typically, as noted above, by prohibiting any transfer of the lease or the premises without the landlord's prior written consent. Some leases specifically provide that this consent may be withheld arbitrarily. For this reason, tenants should consider including in their offer to lease, a provision confirming that the tenant has the right to assign/sublet subject to the landlord's consent, not to be unreasonably withheld.

Interestingly, the *Commercial Tenancies Act*[1] (the "Act") provides that every lease that restricts the tenant's ability to assign or sublet without the landlord's consent is deemed to include a proviso that such consent is not to be unreasonably withheld, unless the lease contains an express provision to the contrary.

In addition, if the landlord withholds its consent to an assignment or sublease, the Act[2] also permits the tenant to bring an application before a judge of the Superior Court of Justice for an order determining whether consent was unreasonably withheld and, where the judge determines that consent was unreasonably withheld, permitting the assignment or sublease. Many leases will provide that this is the tenant's only remedy should a landlord unreasonably withhold its consent (i.e. the tenant cannot sue the landlord for damages, as for example, as a consequence of its proposed transferee choosing not to proceed in light of the landlord's refusal to consent).

Grounds On Which Landlord's Consent May Be Denied

There are many grounds on which a landlord will likely be found to be acting reasonably in withholding consent, as for example, where the tenant is in default of the lease, or where the proposed use of the transferee would contravene an existing use restriction granted by the landlord to another tenant or is more demanding on the building than the existing use, where the proposed use in a retail setting would create traffic and parking

[1] R.S.O. 1990, c. L.7, subs. 23(1).
[2] *Ibid.*, subs. 23(2).

problems for other tenants or would adversely affect the business of other tenants in the shopping centre.[3] There is ample case law exploring the issue of the reasonableness of a landlord's decision to withhold consent but is beyond the scope of this paper. Suffice it to say, the analysis is fact-driven and based on the unique circumstances of each particular case.

Perhaps more importantly, most leases include a laundry list of circumstances that are deemed to constitute a reasonable withholding of consent. When acting for a tenant, it is important that this list be reviewed with a very critical eye as many of the listed grounds on which consent may be denied will significantly restrict the tenant's ability to transfer its lease and may be outside the usual test of reasonableness.

The Challenges in Securing a Transferee

The main obstacle to assigning or subletting is that it is difficult for the tenant to secure a subtenant or assignee, particularly later in the term. Often, it will not make economic sense for the transferee to incur the cost of relocating and improving the premises for its particular use where the remaining term is less than the full five years with a five year option to renew. Further, once a willing transferee is secured, it is highly unlikely that it will be willing to pay the full rent under the lease, thus leaving the tenant to bear the shortfall. Please note that if the transferee is not prepared to pay the full rent under the lease, the transfer must be structured as a sublease.

Release From Landlord

The tenant's exit from its lease obligations by an assignment or sublet would be most advantageous if there is a full release of the tenant from future liability, but the landlord will not agree to this except in exceptional circumstances. The landlord's consent to the transfer will invariably confirm that the tenant will remain liable to the landlord if the assignee or subtenant defaults under the lease. (Please note that even if the consent is silent on this point, the tenant is not released at law on either an assignment or sublease.) What the tenant can do, however, is limit its liability by not assigning its options to renew and, in the context of a sublease, not agreeing to extend the sublease term by agreeing to exercise its options to renew. It is better to try to hang tough and require the assignee/subtenant to do a direct deal with the landlord for the period of time after the expiry of the remaining term of the lease. The assigning tenant will also want to try to limit its liability to its then existing obligations for the then existing term (that is, not agreeing to extend the tenant's liability to include any amendments to the lease by its assignee).

Cost to Assign/Sublet

In determining whether it makes economic sense to assign or sublet, the tenant must also take into account the not inconsiderable costs in doing so. The tenant's costs will include real estate commissions, legal fees, the landlord's charges to consider the request for consent and to document the same should consent be given. It is also likely to include the cost of any inducements or alterations that the tenant will have to pay or perform in order to secure the transferee. This is particularly true in the case of a partial sublease where the tenant will need to demise the sublet space from the balance of its premises. Partial subleases are also challenging in that the originally demised space may not be easily subdivided. There are often access and security issues.

[3] William A. Rowlands, "Subleases: Seeking the Landlord's Consent", Lang Michener LLP Real Estate Brief Fall 2010, online: http://www.mcmillan.ca/101712.

Landlord's Conditions To Its Consent

Not only will the lease normally restrict the tenant from assigning or subletting without the landlord's consent, it will also normally include a number of conditions to the landlord's consent, if granted. In a landlord-centric lease, these conditions may include a right to increase the rent on a transfer, or require the tenant and its transferee to enter into the landlord's then current form of lease. In the case of a sublease, these conditions will almost certainly include the requirement that the subtenant waive its special protections under the *Commercial Tenancies Act*, including its right to protect its sublease if the tenant's lease is surrendered, terminated or disclaimed and to protect its property from distress.[4] In addition to requiring the subtenant to waive these rights, many leases permit the landlord to affirm the sublease at the landlord's discretion.

It is also very common to provide that that the tenant's "special" rights are not transferable, including any option to renew, right of first refusal/rights of first offer, audit right, signage rights, early termination rights, exclusive use rights, etc. Quite often, these restrictions also extend to special rights that aren't so special and are, in my view, more attributable to the amount of space the tenant is leasing than to the tenant itself, as for example, parking rights and storage space. The inability to transfer these rights (especially the special rights) will make the lease less attractive to the transferee and as such, will make it more difficult to secure a willing assignee or subtenant.

Landlord's Right to Terminate

Most leases permit the landlord to terminate the lease in lieu of giving its consent. In the context of an exit strategy, this may not be a bad result for the tenant. In an office lease, the tenant may be delighted that the landlord elects to terminate instead of consenting as this will release the tenant from any further obligation under the lease. For a retail tenant or a franchisee, this may be a terrible result as it would not permit them to sell their business as a going concern. Most landlords have some flexibility in waiving the right to terminate in particular circumstances. It is important to understand what your tenant may want/need to do in the future and ensure that the lease permits this. At the very least, a tenant that is concerned about the landlord's right to terminate instead of giving or denying its consent, should include a step-down provision permitting the tenant to withdraw its request for consent if the landlord exercises its termination right. Not a perfect solution by any means but this is often all that we can get for tenants with little leverage.

Tenants should not rely on the landlord's right to terminate as an exit strategy, however, as the landlord is not in any way obligated to exercise this right and will not do so unless it has a very compelling reason to do so, as for example, to accommodate the expansion requirements of another tenant.

Permitted Transfers

Every tenant's business is different. Given the hurdles in securing consent and the conditions that may attach to the landlord's consent, I suggest that tenant's counsel explore with the tenant if it anticipates sharing possession of its premises with anyone else (as for example, service providers, joint venture partners), or if it is part of a corporate family, whether intercorporate transfers are likely, or if it is part of a franchise system, whether a sale to another franchisee or the franchisor is possible, or if the tenant is a partnership, whether transfers between

[4] *Supra*, note 1, ss. 17, 21, 39(2) and 32(2).

the partners is likely. The landlord should be approached about carving out each of these events from the consent requirement.

Summary

Given the inherent difficulty (if not impossibility) in forecasting growth or unforeseen economic turns, it should not be surprising that many tenants will find themselves needing to exit their premises. What is surprising is how many tenants believe that it will be an easy matter to assign or sublet. Not only is it difficult to secure a ready, willing and financially capable transferee, the lease can make it inordinately difficult or financially unviable to complete the transaction. Any inroads that can be negotiated will, if the need arises, be worth their weight in gold and warrant some time and attention to these important terms of the lease at the outset of the relationship.

2. Strategy No. 2: Early Termination Rights

A right to unilaterally terminate the lease is the ultimate tenant exit strategy but, not surprisingly, few leases expressly give the tenant the right to terminate the lease at will and without recourse. Leases are for a fixed term and the landlord's financial analysis of the lease transaction presupposes that the tenant will occupy the premises and pay rent throughout the agreed term. That said, there are instances where the landlord will consider an early termination right but these rights tend to be subject to a very narrow set of circumstances that will trigger the right and almost always require the tenant to pay a termination fee.

I've seen early termination rights given to address very real concerns of the tenant regarding its funding. Tenants dependent of government financing are often able to secure a right to terminate if their funding is not renewed. In a retail lease where percentage rent is payable, the tenant may be successful in getting the landlord to agree that the tenant may terminate if landlord fails to satisfy stipulated co-tenancy obligations. A medical or lab tenant may be successful in securing a right to terminate if its licence to operate certain diagnostic equipment is not renewed. Finally, an internationally based company may be granted the right to terminate if it closes all or substantially all of its Canadian locations.

Unless the tenant has very significant leverage, the key to success is being very specific about what set of circumstances will trigger the tenant's option to terminate, and to the extent appropriate, limiting the time frame in which the tenant can exercise this right. (It will be easier for the landlord to agree to a termination right that is not exercisable during the first 5 years of a 10 year lease.) The amount of notice to be given will also play a role. If the landlord reasonably anticipates it will take a year to relet the premises, its losses (and therefore its reluctance to agree) will be mitigated if the tenant is required to give a year's notice. All this to say, the tenant must, to the extent possible, try to crystal ball what is likely to happen in the future and then tailor the request for an early termination right to address this as narrowly as possible. Otherwise, the landlord is highly unlikely to be prepared to even consider the request.

If the landlord is prepared to agree to an early termination right, it will invariably also require the tenant to reimburse the landlord its real estate commissions, legal fees incurred to prepare the lease, the unamortized cost of any allowances or other inducements, such as rent-free or rent-reduced periods, the cost of landlord's work and the like. It is also likely to require a termination payment, whether this be a stipulated number of months' rent or a fixed fee. This early termination payment will generally be payable in certified funds concurrent with the tenant's exercise of its option to terminate. Finally, the tenant should also be aware that exceptions made by the landlord in terms of the tenant's exit obligations (as for example, the right not to have

to remove leasehold improvements at the end of the term or limiting this obligation to non-standard leasehold improvements) do not always extend to and include an early termination by the tenant. Tenant's counsel will want to ensure that any such exceptions apply to an early termination.

In conclusion, if a tenant is to have any hope of negotiating an early termination right, it must be prepared to narrowly prescribe the circumstances that will trigger this right and the timing of the exercise. It should also anticipate having to pay a termination fee which, at the very least, reimburses the landlord its unamortized out-of-pocket costs.

3. Strategy No. 3: Partial Contraction Rights

A tenant with good leverage may also wish to negotiate contraction rights; that is, the right to surrender a part or parts of its premises, either at a fixed date or on a rolling basis. This is a particularly useful exit strategy for tenants leasing large premises. This right typically allows the tenant to give back part of its premises at specific junctures of the lease, as for example, the right to surrender a full floor at certain anniversaries of the commencement date or the right to contract by up to a specified percentage of the total originally leased rentable area.

Contraction rights are often discussed in tandem with expansion rights. It is important to both parties that the possible changing description of the leased premises be front of mind when negotiating these terms. The landlord may wish to expressly link the two by providing that the contraction rights are forfeited if the tenant exercises any expansion rights, or that the express percentage instead be capped at a square footage equal to the percentage of the tenant's original premises.

As with early termination rights, it will be easier for the landlord to agree to a contraction right that is not exercisable until a certain period of the term of the lease has passed. Again, the amount of notice to be given will also play a role. The more notice that the tenant will agree to give, permits the landlord a better opportunity to re-lease the surrendered premises.

Contraction rights differ from the early termination right, however, in that the landlord will be concerned that the surrendered area be re-leasable. In a retail context, the amount of frontage will be an issue. In an office lease, direct access to the elevators and the inclusion of exterior windows will be of concern. In either case, the state of the surrendered premises will need to be addressed. The tenant will want to surrender the space as is. The landlord will, however, have a legitimate interest in ensuring the space is returned in the best state to be re-let. These competing interests will need to be addressed.

As was the case regarding early termination, the landlord will almost always require the tenant to repay the landlord any out-of-pocket costs it incurred to originally lease the surrendered space to the tenant, including its real estate commissions, the unamortized cost of any allowances or other inducements, the cost of landlord's work and the like, except that in this case, these amounts need to be prorated based on the area of the surrendered premises over the total area originally leased (unless certain costs were specific to certain parts of the premises). Again, it is also likely that the landlord will require a surrender payment, whether this be a stipulated number of months' rent or a fixed fee and the tenant should anticipate that this surrender payment will be required to be paid in certified funds concurrent with the tenant's exercise of its option to contract. And finally, the tenant should also be aware that exceptions made by the landlord in terms of the tenant's exit obligations (as for example, the right not to have to remove leasehold improvements at the end of the term or

limiting this obligation to non-standard leasehold improvements) do not always extend to and include the tenant's early surrender of part of its premises.

Great care should also be taken in identifying whether the tenant's right to contract is a one-time right or a continuing right.

4. Strategy No. 4: Going Dark

There are a number of circumstances that may warrant a tenant electing to vacate its premises (i.e. go dark) without terminating the lease. By way of example, the tenant may have outgrown its space, or at the end of the term, its new space may come available before the term of the lease for its existing premises expires, or if it is a retail tenant, perhaps this is non-performing location and the tenant wishes to cut its losses by shutting its doors while continuing to pay rent.

Most landlord standard leases both require the tenant to actively carry on business from the leased premises and prohibit the tenant from vacating the premises. Thus, electing to cease carrying on business from the premises and allowing them to become unoccupied would constitute an event of default triggering the landlord's remedies, which probably include the right to accelerate rent, forfeit one or more of the tenant's special rights (including exceptions to the tenant's exit obligations) or to terminate the lease.

Tenants should consider pursing a right to go dark clause allowing the tenant to vacate the premises without being in default so long as the tenant continues to honour its obligations under the lease, including the timely payment of rent. This right may become a valuable asset to the tenant as part of a business restructuring. It gives the tenant the opportunity to vacate an unprofitable space, thus reducing its employee, inventory and utility costs to stop (or at least slow down) the bleeding while rent is payable.[5] It enables the tenant to re-tool and re-launch, change its use or find a subtenant or assignee.[6]

The availability of a go dark right depends on the type of lease, the quality of the development and tenant's brand, and the bargaining power of each party.

In a retail context, a continuous use covenant is clearly imperative to the landlord and it will be very difficult for the landlord to grant a go dark request. Retail leases typically include the payment of percentage rent and, as such, the landlord's revenue stream is dependent on ensuring the tenant maximizes its sales. Rent payment is not necessarily the only criteria that is important to the landlord. The prestige and viability of the development are closely linked to all space being leased and open for business, or the landlord may have to satisfy co-tenancy obligations which require that a certain percentage of the development be open for business.

In an office context, however, the typical retail analysis with respect to a go dark request does not usually apply unless there are retail or service tenants in the building (as for example, restaurants or other food services, drycleaner, barber, shoe repair), in which case the landlord will be concerned that the vacancy will not have any impact on the profitability or viability of its retail/food service tenants. Additionally, the vacancy of part of an

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[5] Susan D. Rosen, "Building in Lease Protections for the Landlord and the Tenant in Anticipation of Changes in the Marketplace", September 24, 2008, *Practice Gems: Commercial Leasing Essentials*, at 5-4.
[6] *Ibid.*

office building is not generally as apparent in an office building and thus the landlord's brand is much less likely to be impacted.

Ironically, it may be easier for the landlord to grant a small tenant the right to go dark, but it is, of course, the larger tenant that the landlord will be more likely prepared to accommodate.

Generally speaking, if the landlord agrees to permit the tenant to go dark, it will require the tenant to give reasonable prior notice that it intends to do so and requires the tenant to pay any additional insurance and security costs incurred by the landlord as a consequence the tenant's election to vacate its premises. The landlord will also generally want the right (not the obligation) to terminate the tenant's lease after a certain period of time. This right is generally without recourse – the tenant is not liable in damages. Retail and office tenants will often have differing concerns about this. Retail tenants will often be very concerned that the landlord not relet the premises for a similar use, particularly if the tenant has vacated but has either re-opened in a new or simply another location in the vicinity. Office and retail tenants will be concerned that the landlord's early termination right not be triggered if the premises are merely temporarily vacant, as for example, to accommodate temporary requirements of the tenant or to do renovations. Tenants will want to ensure that this is avoided and that, in any case, they have the right to void the landlord's termination notice by again re-occupying and carrying on business from the premises within a stipulated period of time.

5. Strategy No. 5: Judgement-Proofing

At its simplest, judgement-proofing is ensuring that the party entering into the lease as tenant, has no assets against which the landlord has any reasonable likelihood of securing its damage claim in the event the tenant defaults in its obligations under the lease. Many tenants will incorporate a new company to enter into the lease for a number of good and valid reasons, including a desire to avoid personal liability. There are not many landlords, however, that will accept a newco as a tenant without requiring personal guarantees from the principals.

Suffice it to say that if the tenant is judgement-proof, it has effectively dealt with its obligations under the lease and can exit the lease without risk of the landlord being able to enforce any judgement it might pursue against the tenant. That said, there are reputational issues at stake and these need to be taken into account in the tenant's dealings with the landlord.

6. Strategy No. 6: Repudiation

I saved this strategy for last because it should not be considered by the tenant except as a last resort and subject to an abundance of caution. Repudiation is a unilateral election by one party to a contract – in the context of a lease, when the tenant abandons the premises, stops paying rent and repudiates all of its obligations under the lease. These actions will render the tenant in default of its lease and put the tenant at very high risk of being sued by the landlord for damages.

A tenant in financial trouble may avail itself of this strategy in the hope that the landlord will prefer to negotiate a settlement over the prospect of spending years litigating in court. If the tenant is a shell corporation and/or does not have any assets of value which the landlord could use to satisfy a judgement, the tenant may decide that the benefit of walking away from its lease obligations outweighs any risks associated with doing so. The tenant will want to carefully assess these risks before choosing repudiation as a course of action.

The landlord may choose to not accept the repudiation. It has the legal right to treat the lease as continuing and insist on the performance of the terms, and claim for rent for the balance of the term or damages on the basis that the lease remains in force. In the alternative, the landlord may elect to accept the tenant's repudiation and terminate the lease while retaining the right to claim for arrears of rent and damages to the date of termination for previous breaches of covenant and, provided that it serves notice on the defaulting tenant, claim for damages for losing the benefit of the lease over the unexpired term.[7] Generally speaking, repudiation is most useful when dealing with a landlord who will not entertain any discussion regarding an early surrender of the lease. Sometimes the only way to get the landlord to the table is to stop paying the rent. This is particularly true in situations where the tenant is financially viable but for one reason or another needs to shed these particular premises, as for example, in the case of a successful franchise electing to close this location.

Although case law confirms that the landlord's options in the face of a repudiating tenant are mutually exclusive and the landlord has no positive duty to mitigate its damages when it chooses to keep the lease alive,[8] a prudent landlord will not sit back and do nothing to mitigate its losses.

The tenant and the principals of the tenant, should be made aware of the risks of a "midnight move". If the tenant fraudulently removes its goods and chattels from the premises, or if any person wilfully and knowingly assists the tenant in doing so (e.g. the principals of the company, their moving company), or in concealing them, they are at risk of a claim to pay to the landlord *double the value* of such goods and chattels.[9] The landlord is not limited to bringing its claim against the tenant. The *Commercial Tenancies Act* permits the landlord to seek its remedy against "any person" who "wilfully and knowingly aids or assists the tenant" in the removal or concealment. If the principals of the tenant knowingly conduct themselves with the intent to defeat the landlord's entitlement to rent, the court may hold them *personally* liable for *double the value* of such goods and chattels removed, even if the tenant company no longer has assets or is a shell.[10]

7. Good Faith and Honesty in Contract Performance: *Bhasin v. Hrynew*[11]

Regardless of which exit strategy is being considered, the tenant must remember to conduct itself in good faith, and with honesty and reasonableness.

Until a few years ago, it was unclear whether the common law imposed on parties to a contract any legal obligation to act in good faith. In *Bhasin v. Hrynew*, the Supreme Court of Canada articulated a new common law duty of honest performance that applies to all contracts and aligns with the reasonable commercial expectations of parties to a contract. The Court articulated two incremental steps in relation to good faith performance of contracts. The first step is to acknowledge that good faith contractual performance is a general organizing principle of the common law of contract. Good faith is not a free-standing rule, but rather a standard that underpins and is manifested in more specific legal doctrines and may be given different weight in different situations. The second is to recognize that, as a manifestation of this organizing principle of good faith, there is a common law duty which applies to all contracts to act honestly in the performance of contractual obligations.

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[7] *Highway Properties Ltd. v. Kelly, Douglas and Co. Ltd.*, [1971] S.C.R. 562 at p. 570.
[8] *7Marli Limited v Pet Valu Canada Inc.*, 2017 ONSC 1796 at para. 27. See also Robert J. Potts, "Avoiding Losses: A Landlord's Duty to Mitigate, February 1, 2002, online: http://www.blaney.com/files/article_avoiding_losses.pdf.
[9] *Commercial Tenancies Act*, *supra*, note 1, s. 50.
[10] *1268227 Ontario Ltd. (c.o.b. Seamus O'Brien's) v. 1178605 Ontario Inc.*, [2001] O.J. No. 3642, aff'd by [2003] O.J. No. 2002 (Ont. C.A.).
[11] *Bhasin v. Hrynew*, 2014 SCC 71.

While the precise content of honest performance will vary with context, parties are not permitted to contract out of the as yet undefined “minimum core requirements”.

This means that parties to all commercial contracts, including leases, are required to perform their respective contractual obligations honestly and reasonably.

What honesty and reasonableness in contract performance require will depend on the context, including the nature of the contract in question and the nature of the relationship between the parties. A lease is more than a transactional exchange. It is a long-term relational contract that depends on mutual cooperation and trust between a landlord and tenant. As such, a court will likely require a high level of good faith, honesty and reasonableness in the performance of obligations under a lease, perhaps a higher level than for a one-time transactional exchange.

A tenant should not, therefore, exercise an exit strategy, such as a “go dark” right, in a deliberate attempt to interfere with the maximization of gross sales (and thus percentage rent) or ruin the landlord’s property as such behaviour flies in the face of honesty and good faith. The landlord should not withhold its consent to a tenant transfer for ulterior motives, such as wanting to get rid of the tenant to get the space back to make another use of the property or benefit from an increase in market rent on the space, or refuse to respond to a tenant’s request for consent.

Conclusion

It is very difficult for tenant’s counsel to advise a tenant who needs to get out of its lease but has no express exit or termination rights in its lease. An astute tenant will consider and negotiate exit strategies into its lease before it signs on the dotted line. This will ensure that the tenant has at least some options to deal with its ongoing lease obligations should its circumstances change for the better or the worse, as they are wont to do.
