MINDEN GROSS LLP BARRISTERS AND SOLICITORS
145 King Street West, Suite 2200, Toronto, ON M5H 4G2
P. 416.362.3711 ▪ F. 416.864.9223 ▪ @MindenGross ▪ www.mindengross.com

Commercial Leasing Bulletin

Rent Reset Arbitration: Words Matter

July 6, 2021

By: Catherine Francis – Commercial Leasing Group – Minden Gross LLP

Introduction

It is common for ground leases to provide that the rent payable during the course of the ground lease will be re-set from time to time based on a formula. It is also common for such leases to provide that, in the event the parties are unable to agree on the rent payable, the matter will be decided by binding arbitration. Similarly, many shorter-term leases provide for arbitration of the rent payable under an option to renew.

The recent decision of the Ontario Superior Court of Justice in *Parc-IX Limited v. The Manufacturer's Life Insurance Company*, 2021 ONSC 1252 (CanLII) is a cautionary tale of the difficulties that can be encountered in interpreting an apparently very simple and straightforward rent reset clause in a ground lease. The clause has spawned decades of hard-fought litigation, which has repeatedly spilled from the arena of private arbitration into the courts. The most recent spat began in 2014 and has yet to be finally resolved. This bulletin summarizes the importance of the case to landlords and tenants and takeaways in drafting rent reset and arbitration clauses and in arbitrating such disputes.

What Happened

Manulife is the owner of certain land which was leased by Parc-IX pursuant to a ground lease dated August 15, 1964. The land is improved with a 17-storey residential apartment building operated by Parc-IX. Under the ground lease, the rent payable by Parc-IX must be re-set every 25 years. The current rental term began on August 15, 2014. The rent was to be re-set at "a sum equal to 6¾% of the fair market value of the property as if it were unimproved" as of March 15, 2014.

Manulife and Parc-IX were unable to agree on the ground rent for the renewal. The ground lease provided that in the absence of agreement, the market value of the land would be determined by arbitration with the decision of the arbitrator to be "final and binding".

Manulife and Parc-IX jointly appointed an arbitrator to determine the market value of the land. The matter was complicated by the fact that Parc-IX and Manulife's predecessor had arbitrated the previous rent reset before a panel of three arbitrators to determine the market value of the land as

of March 15, 1989. The main issue was whether the value of the land should now be determined based on the land's value as a condominium. The panel held that it should not. The landlord brought a review application before the Divisional Court, which held that the panel should have determined the market value based on the land's condominium value, but deferred to the panel's decision because it was not "patently unreasonable" and therefore could not be set aside.

Fast forward more than 25 years later. Both sides argued that the arbitrator should be bound by the previous decision. Parc-IX argued that the 1990 decision of the previous arbitration panel should apply. Manulife argued that the interpretation of the Divisional Court should apply. So the parties sought a preliminary ruling from Justice McEwen of the Ontario Superior Court of Justice, who ruled in favour of Parc-IX in a decision released on June 15, 2018.

The new arbitrator was then required to interpret the 1964 ground lease, the 1990 decision of the prior arbitration panel, and the 2018 decision of Justice McEwen. The arbitrator ruled in favour of Manulife's proposed interpretation and awarded Manulife almost $900,000 in costs of the arbitration. This led to a review application before the courts, which was decided by Justice Koehnen in early 2021. He dismissed Parc-IX's complaint and enforced the arbitrator's award.

This is not the end of the story.

What's Happening Now

Parc-IX is now seeking leave to appeal the decision of Justice Koehnen to the Ontario Court of Appeal. There is no automatic right of appeal from a decision to uphold or set aside an arbitrator's award. The proposed appellant must satisfy the Court of Appeal that leave to appeal should be granted. The criteria for leave are not defined and the Court of Appeal typically does not give reasons for its decision. Leave applications can take weeks to months to decide. If leave is granted an appeal decision could be another 6–12 months away.

Key Takeaways

It is beyond the scope of this bulletin to delve into the intricacies of the legal and factual issues in dispute between the parties.

Words Matter

The point of this story is that words matter. A very simple clause in a lease can be open to different interpretations and can result in years (or in this case, decades) of very costly litigation. Every single clause in a lease can be important, sometimes very important, if the events contemplated by the lease come to pass. In the case of a rent reset clause, it is critical to draft the clause very carefully, perhaps with the advice of an experienced valuator.

Even with Binding Arbitration, Court is Still Possible

Binding arbitration doesn't necessarily insulate the decision from court review. Even if there is no right of appeal, as in this case, one of the parties can seek review of the decision on a number of grounds, including lack of jurisdiction or failure to provide procedural fairness. Parties cannot contract out of these review provisions. So, while it is important to draft the arbitration clause to preclude rights of appeal, bear in mind that this doesn't necessarily mean that the dispute will not spill into the court system.

We will continue to provide updates on commercial leasing topics of interest. If you have any questions or would like to obtain legal advice on any leasing issues or litigation, please contact any lawyer in our Commercial Leasing Group.

Commercial Leasing Group

Stephen Posen
Chair, Commercial Leasing Group
e: sposen@mindengross.com
p: (416) 369-4103

Ian Cantor
Partner, Litigation Group
e: icantor@mindengross.com
p: (416) 369-4314

Christina Kobi
Partner, Commercial Leasing Group
e: ckobi@mindengross.com
p: (416) 369-4154

Benjamin Radcliffe
Partner, Commercial Leasing Group
e: bradcliffe@mindengross.com
p: (416) 369-4112

Steven Birken
Associate, Commercial Leasing Group
e: sbirken@mindengross.com
p: (416) 369-4129

Alyssa Girardi
Associate, Commercial Leasing Group
e: agirardi@mindengross.com
p: (416) 369-4104

Catherine Francis
Partner, Litigation Group
e: cfrancis@mindengross.com
p: (416) 369-4137

Michael Horowitz
Partner, Commercial Leasing Group
e: mhorowitz@mindengross.com
p: (416) 369-4121

Boris Zayachkowski
Partner, Commercial Leasing Group
e: bzayachkowski@mindengross.com
p: (416) 369-4117

Melodie Eng
Associate, Commercial Leasing Group
e: meng@mindengross.com
p: (416) 369-4161

Leonidas Mylonopoulos
Associate, Commercial Leasing Group
e: lmylonopoulos@mindengross.com
p: (416) 369-4324

Benji Wiseman
Associate, Commercial Leasing Group
e: bwiseman@mindengross.com
p: (416) 369-4114