CITATION: DAA Holdings Ltd. v. Teranet Inc., 2024 ONSC 794
COURT FILE NO.: CV-23-1722-0000
DATE: 2024 02 06

SUPERIOR COURT OF JUSTICE – ONTARIO

491 Steeles Avenue East, Milton ON L9T 1Y7

RE: DAA Holdings Ltd.

AND:

Teranet Inc.

BEFORE: Conlan J.

COUNSEL: Robert D. Malen, for the Applicant
Dina Peat, for the Respondent

HEARD: February 5, 2024

ENDORSEMENT

I. The Application

[1] The Applicant, DAA Holdings Ltd. ("DAA"), applies for:

(i) a determination of rights under the Lease dated October 22, 2013 ("Lease") between DAA as the landlord and the Respondent, Teranet Inc. ("Teranet"), as the tenant, specifically a determination, under section 4.1(b) of the Lease, of the Minimum Rent payable for years 11-15 of the Lease;
(ii) a determination that Teranet has breached the said section of the Lease by not making good faith contractual efforts to reach an agreement on the Minimum Rent for those years;
(iii) an order that the Minimum Rent for those years shall be $19 net per square foot for year 11, $20 net per square foot for year 12, $21 net per square foot for year 13, $22 net per square foot for year 14, and $23 net per square foot for year 15, or such other

rental amounts that the Court determines having regard to the "fair market rental rate" as defined in the Lease*; and

(iv) other relief including costs.

*In oral submissions, to be consistent with an offer that was made by DAA after the Application was issued, Mr. Malen, counsel for DAA, indicated that DAA would be content with an order that the Minimum Rent for the five years in question be $18-$22 net per square foot (rather than $19-$23, as sought in the Application).

[2] The Application was heard at court in Milton, Ontario on February 5, 2024. As expected on an application, no *viva voce* evidence was called by either side. Submissions by counsel took about ninety (90) minutes total, on both sides, including reply. It was well argued by both Mr. Malen and Ms. Peat.

II. The Facts

[3] The facts are largely undisputed.

[4] The rental premises are located at 316 Watline Avenue in Mississauga, Ontario, a 12,763 square foot freestanding industrial building. Teranet is the sole occupant. It has occupied the premises since January 2014 under the 15-year Lease.

[5] The rent for years 11-15 is determined by section 4.1(b) of the Lease. That provision provides as follows.

> Notwithstanding anything to the contrary, the parties acknowledge and agree that the Minimum Rent for years 11-15, inclusive, of the Term shall be agreed upon by the parties not less than six (6) months and not more than nine (9) months prior to the expiry of the tenth (10^{th}) year of the Term and shall be established having recourse to the fair market rental rates paid by tenants for comparable improved space (excluding any data centre infrastructure installed by the Tenant) and term in comparable buildings in the 'Traders Business Park' market. If the parties fail to agree upon the Minimum Rent as aforesaid, then the parties agree that the Minimum Rent payable by the Tenant for the period commencing on the eleventh (11^{th}) anniversary of the Commencement Date to the expiry of the fifteenth (15^{th}) year of the Term shall be the Minimum Rent for tenth (10^{th}) year increased by the Inflation Factor.

[6] "Inflation Factor" and "Inflation" are defined terms in sections 1.1(y) and 1.1(x), respectively, of the Lease. If the Inflation Factor is applied here, it would result in a very modest increase in the rent from $8 in year 10 to $8.27 for years 11-15.

[7] Within the negotiation period set out in section 4.1(b) of the Lease, DAA had proposed a rental rate considerably higher than $8.27 for years 11-15. Based on a Broker Opinion of Value report obtained by DAA, it suggested various rental rates for the five years in question, culminating in an offer by DAA of $18 net per square foot in year 11 and rising $1 net per square foot each year to $22 net per square foot in year 15, which offer was at the very low end of the Broker Opinion of Value.

[8] Teranet did not agree to any of DAA's proposals.

III. The Positions of the Parties

[9] DAA suggests that Teranet has not acted in good faith but rather has simply rejected DAA's proposals, has counter-offered nothing reasonable for DAA to consider, and has simply stonewalled the negotiations in order to obtain a clear windfall that would result from a straight application of the Inflation Factor.

[10] Teranet, on the other hand, submits that it has complied with section 4.1(b) of the Lease. Simply put, according to Teranet, the parties do not agree, and thus, the rental rates for the years in question shall be determined in accordance with the clear wording of the contract – by application of the Inflation Factor.

[11] In summary, while DAA submits that Teranet has breached its duty to act in good faith, Teranet argues that it had no duty to negotiate at all.

IV. The Law

[12] Both sides rely upon the decision of the Supreme Court of Canada in *Bhasin v. Hrynew*, 2014 SCC 71, [2014] 3 S.C.R. 494. In that case, Justice Cromwell, writing for

the Court, posed this question, "[d]oes Canadian common law impose a duty on parties to perform their contractual obligations honestly?"; and Justice Cromwell answered that question in the affirmative (paragraph 1 of the decision).

[13] A review of the decision in *Bhasin, supra*, beginning at paragraph 63 and ending at paragraph 93 of Justice Cromwell's analysis, reveals the following principles:

> (i) parties generally must perform their contractual duties honestly and reasonably and not capriciously or arbitrarily;
> (ii) the organizing principle of good faith that applies to a contracting party is not a fiduciary duty, but it requires that a contracting party not seek to undermine, in bad faith, the legitimate interests of the contracting party on the other side;
> (iii) the duty of honest performance, which duty applies to all contracts as a manifestation of the general organizing principle of good faith, requires the parties to be honest with each other in relation to the performance of their contractual obligations;
> (iv) in each case, the understanding of what honesty and reasonableness in performance requires of a contracting party, and the determination of whether a contracting party has acted in good faith, calls for a highly context-specific analysis, giving appropriate consideration to the legitimate interests of both contracting parties; and
> (v) the principle of good faith is not meant to interfere with the well-recognized freedom of contracting parties to pursue their individual self-interests, even if that pursuit causes loss, even intentional loss, even substantial loss, to the other side.

V. Application of the Law to our Facts

[14] Respectfully, this Court is of the view that the position of DAA is preferable to that of Teranet. This Court concludes that Teranet's position is inconsistent with the jurisprudence and incompatible with a reasonable interpretation of section 4.1(b) of the Lease.

[15] With regard to the latter, the wording of section 4.1(b) is important. It must be read as a whole. The first part of the section requires (the word "shall" is employed) that the Minimum Rent be established by having recourse to the fair market rental rates paid by

tenants for comparable improved space (excluding any data centre infrastructure installed by the Tenant) and term in comparable buildings in the 'Traders Business Park' market.

[16] On the question of what the Minimum Rent should be, it is uncontroverted in the evidence that (i) DAA has made multiple proposals to Teranet, (ii) that those proposals were based on a professional's opinion of the fair market rental rate, which opinion in turn was based on comparables, precisely in accordance with the wording of the first half of section 4.1(b) of the Lease, (iii) that Teranet, beginning as early as only four days after DAA's initial proposal was sent for consideration, has simply taken the position that it does not accept DAA's proposals and, thus, there is no agreement, triggering the application of the Inflation Factor, and (iv) in taking that position, Teranet has commissioned no professional opinion of its own, and Teranet has not challenged the qualifications or the work product of the professional firm that prepared the Broker Opinion of Value report obtained by DAA, and Teranet has not referred to any of its own comparables, and Teranet has not produced any evidence of any kind that serves to challenge the reasonableness of any of the rental figures proposed by DAA.

[17] Essentially, the position of Teranet has been, from the very outset, akin to the following – we received your proposal; we disagree; Inflation Factor shall apply.

[18] In my view, that approach by Teranet does not accord with the contractual requirement in section 4.1(b) of the Lease that the Minimum Rent shall be established by having recourse to the fair market rental rates for comparable properties.

[19] In other words, the application of the Inflation Factor is triggered only if the parties fail to agree on the Minimum Rent. A failure to agree necessarily implies some modicum of effort to agree, albeit an unsuccessful one. For the section, 4.1(b), to make any common sense, the effort by the parties must be directed towards satisfying the requirement that the Minimum Rent shall be established by having recourse to the fair market rental rates for comparable properties. Clearly, Teranet made no effort to satisfy that requirement.

[20] Even if this Court considers the single offer of Teranet as summarized at paragraph 22 of the factum filed on its behalf, ignoring that the said offer is not evidenced anywhere in the Responding Record filed by Teranet, and ignoring further that the said reference in the factum appears to waive privilege over a "without prejudice" correspondence in circumstances where, at least arguably, that waiver is invalid, it matters not. The said offer was conditional on Teranet having the right to unilaterally terminate the Lease early. The said offer introduced something completely foreign to section 4.1(b) of the Lease. As such, the said offer was effectively no offer at all.

[21] With regard to the former, the jurisprudence, I conclude that the actions of Teranet were not in keeping with the organizing principle of good faith spoken about by Justice Cromwell in *Bhasin, supra*. Teranet's position to simply dismiss, almost immediately, and summarily, the first and every proposal made by DAA was absent any explanation, reason, or counter-proposal. It was, in my view, the very definition of a contracting party taking a capricious and arbitrary stance to the performance of its contractual obligations. It was not dishonest, but it was certainly unreasonable.

[22] In fact, I see nothing to distinguish our facts from those in *Empress Towers Ltd. v. Bank of Nova Scotia*, [1990] B.C.J. No. 2054 (B.C.C.A.), and those in *Jagtoo & Jagtoo Professional Corp. v. Grandfield Homes Holdings Ltd.*, [2021] O.J. No. 6275 (S.C.J.) and [2021] O.J. No. 6276 (S.C.J.), affirmed at [2023] O.J. No. 1378 (C.A.), which decisions in *Jagtoo, supra* referred to approvingly and applied the decision in *Empress Towers, supra*.

[23] In *Empress Towers, supra*, the Court faced a clause in a lease that was similar to section 4.1(b) of the Lease in our case. In both cases, the contract set out a default provision if the contracting parties did not agree on the rental rate. The Court in *Empress Towers* held that the section of the lease in question in that case carried with it an implied term that the parties would negotiate in good faith with the objective of reaching an agreement on

the rental rate and, further, an implied term that agreement on the rental rate would not be unreasonably withheld (page 4 of the reasons for judgment of the majority of the Court).

[24] I would make the same conclusions in our case. Clearly, Teranet did not negotiate in good faith. It did not negotiate at all.

[25] In *Jagtoo, supra*, again involving a not dissimilar provision in a lease, Leibovich J. held that, although not expressly stated in the contractual provision in question, the parties had a duty to negotiate the market rental rate in good faith, otherwise (absent an agreement between the parties) the default provision would be triggered (paragraph 13 of the decision with the O.J. citation ending in 6275). Justice Leibovich's decision was upheld by the Court of Appeal for Ontario.

[26] I would make the same conclusion in our case. Clearly, Teranet did nothing to fulfil that duty.

[27] Reviewing the able submissions made by Ms. Peat, counsel for Teranet, both in writing and orally, this Court would make the following observations:

(i) I disagree that Teranet had no duty to negotiate at all – that submission I find to be contrary to the Lease's section 4.1(b) itself and contrary to the leading jurisprudence;
(ii) I disagree that the position of DAA would effectively mean that the second half of section 4.1(b), the triggering of the Inflation Factor, would never be put into legal effect – it would be applied if the parties tried in good faith to agree but failed to agree on the Minimum Rent using the methodology set out in the first half of section 4.1(b);
(iii) I disagree that the decisions in *Empress Towers, supra* and *Jagtoo, supra* are not persuasive because they deal with lease renewal clauses – the organizing principle of good faith is not limited to any one particular type of contractual provision, including a renewal clause, and there is nothing in *Bhasin, supra* that would support the alleged distinction being relied upon by counsel for Teranet, nor is there any public policy reason or any other rationale that I can think of to justify such a distinction;

(iv) I disagree that the organizing principle of good faith is somehow premised on a finding that there is an ambiguity in the contractual provision under review, and where there is no ambiguity there can be no duty to negotiate in good faith - no authority was cited by Ms. Peat for that proposition advanced in oral argument;

(v) I disagree that DAA's position is commercially unreasonable – rather, it makes common sense to me; when market rental rates are lower than inflation, the landlord (DAA) would rather have the Inflation Factor applied but still has a duty to negotiate the rental rate in good faith; and, the inverse, when inflation is lower than market rental rates, the tenant (Teranet) would rather have the Inflation Factor applied but still has a duty to negotiate the rental rate in good faith; no matter the scenario, both parties are required to negotiate in good faith;

(vi) I disagree that Teranet's position pays respect to the first half of section 4.1(b) of the Lease – it does not; it effectively guts altogether the requirement that the Minimum Rent shall be established by having recourse to the fair market rental rates for comparable properties;

(vii) I disagree that there is anything inconsistent between this Court's acceptance of the position advanced by DAA and the general principles that apply to the interpretation of commercial contracts – rather, I respectfully observe that this Court's decision is, in fact, an application of those very principles outlined at paragraph 32 and following of the factum filed on behalf of Teranet and the decision of the Court of Appeal for Ontario in *All-Terrain Track Sales and Services Ltd. v. 798839 Ontario Limited*, 2020 ONCA 129, at paragraph 27;

(viii) I disagree that there is anything inconsistent between this Court's interpretation of section 4.1(b) of the Lease and section 3.2(7) of the Lease, which latter provision, titled "Extension of Term", states that, where the parties are unable to agree on the Minimum Rent during the Extended Term of the Lease, then there is a process that shall be followed in referring the dispute to arbitration – rather, this Court's decision is harmonious with that other provision in the contract; in both cases, the default provision (whether the application of the Inflation Factor or the referral to arbitration) is triggered only if the parties have tried in good faith but have been unable to agree; and, finally,

(ix) I disagree that this is all simply about DAA having regretted its bargain – rather, it is all about respecting the organizing principle of good faith as it applies to commercial contracts.

VI. Conclusion

[28] There is no request on behalf of Teranet that it be permitted some time to negotiate with DAA in order to reach an agreement on the Minimum Rent for the years in question, in the event that this Court prefers the position of DAA over that of Teranet, which it does. Teranet has asked simply that the Application be dismissed and an order be made that the Minimum Rent shall be established according to the application of the Inflation Factor.

[29] For all of these reasons, the Application by DAA is granted. The relief outlined at paragraph 1 of DAA's factum is granted, except that, regarding clause 1(c), the rental figures of $19 and $23 net per square foot are replaced with $18 and $22 net per square foot, respectively, as conceded by Mr. Malen on behalf of DAA in oral submissions.

[30] On costs, if they cannot be resolved between the parties, the Court will accept written submissions. Each submission shall not exceed three pages in length, excluding attachments. DAA shall file within thirty (30) calendar days after February 6, 2024. Teranet shall file within fifteen (15) calendar days after its counsel's receipt of DAA's submissions. There shall be no reply submissions delivered on the issue of costs.

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Conlan J.

Released: February 6, 2024