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Head leases: Residential or commercial tenancy agreements?

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A recent decision of the Landlord and Tenant Board (the "**Board**") has drawn some interest in the social housing community. By way of some context, some time ago, a supportive housing provider (the "**SHP**") entered into a lease with an owner of an apartment building (the "**Private Sector Landlord**") to rent a rental unit. The purpose of the lease, from the SHP's perspective, was to sublet the rental unit to a tenant who participated in the SHP's programs. This is a fairly common arrangement for social housing providers. For reasons that I do not know, and that do not matter for the purposes of this discussion, the Private Sector Landlord applied to the Board for an order to terminate the SHP's tenancy because it, or someone it permitted in the residential complex, substantially interfered with, among other things, the reasonable enjoyment of the Private Sector Landlord.

On May 6, 2014, the parties appeared at the Board for the hearing of the Private Sector Landlord's application. The Board, however, on its own initiative, adjourned the hearing and asked the parties to make written submissions as to whether the Board had the jurisdiction to hear the Private Sector Landlord's application. This presumably came as a surprise to the parties, as they appear to have assumed that the Board had jurisdiction over the matter.

After reviewing the parties' written submissions, on June 19, 2014, the Board determined that the SHP's relationship with the Private Sector Landlord was not governed by the *Residential Tenancies Act, 2006* (the "**RTA**"), and that, therefore, the Board did not have the jurisdiction to hear the matter. This decision was made in spite of the fact that the parties both believed and intended that the RTA would govern their relationship. This decision was also made in spite of the fact that the Board had come to the opposite conclusion in a previous application that was heard by the Board and that involved the same SHP operating a similar program. In the end, the Board was of the view that the SHP rented the rental unit in connection with its business of providing supportive housing and support services, and that, therefore, the Private Sector Landlord and the SHP were in a commercial tenancy relationship.

In coming to the determination that the SHP's relationship with the Private Sector Landlord was not governed by the RTA, the Board considered the definitions of "*landlord*" and "*tenant*" in the RTA and found that the SHP could not be both a landlord and a tenant. In addition to the foregoing, the Board also considered subsection 202(1) of the RTA (which mandates the Board to, among other things, ascertain the real substance of all transactions relating to a rental unit) and determined that the real substance of the transaction between the parties was that of a commercial tenancy.

That said, shortly after the Board rendered its decision, the SHP appealed the order to the Divisional Court, and also requested that the Board initiate a review of the order (the "**Board Review**"). I am of the view that, while the Board was wrong to hold that a party cannot be both a residential landlord and a tenant, the Board ultimately arrived at the right decision. That is, I am of the opinion that the RTA does not govern the tenancy between the landlord and the head tenant in these circumstances. This appears to be the preferred approach adopted by the court and the Board in the cases that have been recently decided.

The Issue

The courts and the Board have been grappling with this jurisdictional issue for quite some time. Plainly put, the issue is: does the RTA govern the relationship between a landlord and a head tenant where the landlord rents a residential rental unit to a head tenant who will not personally reside in the rental unit but will instead, as part of its business, sublease the rental unit to a subtenant in furtherance of its business?

We know that the relationship between the head tenant and its subtenant is governed by the RTA. Further, I am of the view that the relationship between the subtenant and the landlord is also governed by the RTA. The applicability of the RTA to the relationship between the landlord and the head tenant, however, is much less certain. This *infoON* will explore this issue by reviewing the cases that have dealt with this issue in the past, and will also provide the ONPHA members with some helpful tips as to how a social housing provider, as head tenant, can best protect itself when it negotiates a lease with a landlord .

The RTA v. CTA

As set out above, I am of the view that the RTA does not govern the relationship between a landlord and a head tenant in these circumstances. Assuming that my view is correct, and the RTA does not apply to the relationship between the landlord and the head tenant (although, as is set out below, this position is open to question), the tenancy between the landlord and the head tenant would essentially be considered a commercial tenancy, with the result that the *Commercial Tenancies Act* (the "**CTA**") would apply to the parties' relationship.

The significance of this cannot be overstated.

The purposes of the RTA are to provide protection for residential tenants from unlawful rent increases and unlawful evictions, to establish a framework for the regulation of rents, to balance the rights and responsibilities of residential landlords and tenants, and to provide for the adjudication of disputes. To this end, the RTA provides residential tenants with a significant package of rights and protections. Moreover, the RTA provides residential

tenants and landlords with recourse to the Board which, relatively speaking, is an extremely quick and cost effective process to resolve disputes.

The CTA, on the other hand, does not provide tenants with the significant rights and protections found in the RTA. Rather, to a large extent, the parties are left alone to negotiate the terms that will govern their relationship. Of greater significance, perhaps, is that the CTA does not provide tenants or landlords with recourse to the Board. Instead, to resolve disputes, the parties are essentially forced to initiate proceedings at the Superior Court of Justice, which is a much more expensive and time-consuming process.

The Case Law

The Matlavik Case

The appropriate starting point for our discussion is the Divisional Court's decision rendered on March 16, 1979 in *Matlavik Holdings Ltd. v. Grimson* (the "**Matlavik Case**"). This appears to be one of the earliest decisions that dealt with this issue, and it is arguably the most influential decision. In the Matlavik Case, the head tenant had rented 31 rental units from the landlord in order to sublet same as part of its business of providing furnished accommodation to subtenants on a short-term basis.

At some point during the course of the head tenant's tenancy, the landlord applied for rent review pursuant to the *Residential Premises Rent Review Act* (the "**RPRRA**"), which legislation was in effect at the time but no longer exists. The applicability of the RPRRA to the relationship between the landlord and the head tenant, as well as the Rent Review Officer's jurisdiction, was raised as an issue. The majority of the Divisional Court panel that heard the matter held that this issue could be resolved based on the plain words of the RPRRA. Specifically, the majority noted that section 3 of the RPRRA provided that the RPRRA applied to tenancies of "*residential premises*" (it should be noted that this section is substantially similar to section 3 of the RTA). The majority then considered the definition of "*residential premises*", which, according to the RPRRA, meant "*any premises used or intended to be used for residential purposes*" (which definition is substantially similar to the definition of "*rental unit*" contained in the RTA). Ultimately, the majority concluded that, because the rental units were ultimately used for residential purposes, the rental units in question were indeed "*residential premises*" within the meaning of the RPRRA and that, therefore, the RPRRA applied.

In essence, the Divisional Court held that a court had to engage in a two-part inquiry to determine whether the residential tenancy legislation applied: first, the court had to determine whether there was a tenancy within the scope and meaning of the legislation, and second, the court had to determine whether the premises were used or intended to be used for residential purposes. This two-part approach was reiterated by the Divisional Court in its subsequent decision in *Queen Elizabeth Hospital v. Campbell* (the "**Queen Elizabeth Case**"), which reached a similar conclusion in considering the applicable provisions of the *Landlord and Tenant Act* (the "**LTA**").

Having said that, the dissenting opinion that was given by one of the judges that heard the Matlavik Case (the "**Matlavik Dissent**") must be noted. In broad strokes, the dissenting judge was of the view that the parties had entered into a commercial agreement under which the head tenant acquired rental units to add to its inventory of units that it used in its business of providing short-term furnished apartments. For this reason, the dissenting judge was of the view that the RPRRA, which applied only to tenancies of residential premises, did not apply.

Subsequent cases
A review of the cases that were decided subsequent to the Matlavik Case and that dealt with this issue demonstrates that, for the most part, the courts and the Board (or its predecessor tribunals) appeared to have preferred the reasoning of the Matlavik Dissent over the decision of the majority of the Divisional Court panel that heard the Matlavik Case. However, because these decision-making bodies were ranked lower than the Divisional Court, they were arguably bound to follow the decision rendered by the majority. As a general principle, a lower court is bound to follow the decision of a higher court where the higher court considered the same or similar facts as are present in the case before the lower court. That being said, when a lower court wants to deviate from a decision made by a higher court, the lower court will not necessarily let arguably binding precedent stand in its way. Rather, the lower court may get creative and find a way to distinguish the facts before it, which is precisely what the decision-makers hearing the cases subsequent to the Matlavik Case appear to have done.

In *Deerhurst Investment Ltd. v. FPI Management Systems Ltd.*, a case heard by the Ontario County Court in April, 1984, the head tenant rented 11 rental units from the landlord for the purpose of "using the apartments to carry on a business [that can be characterized as] providing transient living accommodation to members of the public". The landlord wished to regain vacant possession of the rental units, and initiated proceedings under the LTA, which at that time governed both commercial and residential tenancies. The landlord argued that the tenancy agreement with the head tenant was a commercial tenancy (which would allow the landlord to terminate the tenancy), while the head tenant argued that the tenancy agreement was a residential tenancy and relied on the Matlavik Case and the Queen Elizabeth Case (collectively the "**Divisional Court Cases**"). The judge distinguished the Divisional Court Cases by finding that the head tenant operated a hotel business, and found that the relationship between the landlord and the head tenant was a commercial tenancy. This decision was upheld on appeal to the Divisional Court.

In *European Style Bldgs. Ltd. v. 191 St. George Street Ltd.*, a case heard by the Ontario District Court in June, 1987, the landlord rented an entire apartment building consisting of 100 rental units to a corporate head tenant who, in turn, subleased the rental units to subtenants who resided in the rental units. The judge took notice of the Matlavik Case, but held that the case before him could be distinguished from the Matlavik Case and that the relationship between the landlord and the head tenant was a commercial tenancy for the purposes of the LTA.

In *Lee v. Corporate Residences Inc.*, a case dealing with similar issues that was heard by the Ontario Rental Housing Tribunal (the "**ORHT**") in November, 2003, the ORHT determined that the relationship between the landlord and the head tenant was of a "business nature" and was not governed by the *Tenant Protection Act, 1997* (the "**TPA**"), the immediate predecessor to the RTA. The ORHT reached this conclusion because the head tenant did not intend to live in the subject rental unit and therefore did not "conform to the definition of Tenant" as defined by the TPA (similar to the RTA, the TPA defined a "*tenant*" as including "*a person who pays rent in return for the right to occupy a rental unit*").

In *Optimal Space Inc. v. Margana Holdings Inc.*, a case heard by the Ontario Superior Court of Justice in December, 2005, the head tenant leased rental units for the purpose of using same to operate its business of providing therapeutic and rehabilitative services to brain-injured persons. To determine whether the TPA applied to the relationship between the landlord and the head tenant, the court considered a number of factors, including the purpose and use made of the rental units, and whether the nature of sublet premises determined the nature of the head lease. Having done so, the judge held that the lease between the landlord and the head tenant was a

commercial agreement, and that the Divisional Court Cases could be distinguished because "*tenancy agreement*" was defined differently in the RPRRA and the LTA than in the TPA.

In *Port Sarnia Property Professionals v. Gateway Property Management Corp.*, a case heard by the ORHT on March 15, 2006, the ORHT had another opportunity to deal with the applicability of the TPA to the relationship between the landlord and the head tenant. To determine this issue, the ORHT considered the definitions set out in the TPA of, among other things, "*tenant*" and "*rent*", the latter of which was defined as including "*the amount of any consideration paid or given or required to be paid or given by or on behalf of a tenant to a landlord…for the right to occupy a rental unit…*". The ORHT ultimately concluded that the head tenant did not meet the definition of "*tenant*", as it was not paying rent to occupy the rental units but, rather, was paying rent to have the right to rent the rental units to other people

Discussion

This now brings us full circle to the case that inspired this *infoON*, being the case between the SHP and the Private Sector Landlord. On March 13, 2015, the Board rendered its decision in respect of the Board Review. Notably, the Board determined that the relationship between the SHP's tenant and the Private Sector Landlord was governed by the RTA. The Board also refrained from making a determination as to whether a party can be both a residential landlord and a tenant. Finally, and most importantly, the Board determined that the agreement between the Private Sector Landlord and the SHP "is not a residential tenancy agreement governed by the RTA".

The Board's decision in respect of the Board Review was rendered after I wrote this *infoON*, but before same was published. Originally, I had concluded this *infoON* by stating, among other things, that the issue discussed herein is far from settled, and that there will be some uncertainty in the law until the Divisional Court has another opportunity to deal with same. I now believe that, while the issue remains somewhat unsettled, ONPHA's members can expect that the Board's recent decision will be followed by the Board in subsequent cases dealing with similar issues.

Negotiating a new head lease agreement

Given the foregoing, as a matter of prudence, it makes good sense from the head tenant's perspective to assume that the RTA will not apply to its relationship with its landlord. It follows that the head tenant should also assume that it will not automatically have the significant package of rights and protections that are given to residential tenants by virtue of the RTA. Consequently, to protect itself, the head tenant will need to negotiate appropriate lease terms that will provide it with similar rights and protections. Specifically, the head tenant will want to carefully review and take note of the provisions in the RTA that provide residential tenants with rights and protections, and then negotiate a lease that contains similar provisions. By way of example, the head tenant will want to negotiate terms in the lease that will limit rent increases and evictions, that define the parties' respective rights and responsibilities, and that provide for the cost-effective adjudication of disputes.

Current head lease agreements

For those head tenants that have already entered into leases with their respective landlords in circumstances where the parties had assumed that the RTA applied to their relationship, I would recommend that these head tenants carefully review their written leases (if any), as well as the CTA, in order to obtain a better understanding as to the scope and nature of their rights and remedies. Often, these leases will contain provisions that provide that

the RTA applies to the tenancy. Accordingly, it may be possible to argue that a lease incorporates by reference the provisions contained in the RTA. The success of such an argument would depend on, among other things, the wording contained in the lease and the conduct of the parties. I would also suggest that, as the terms of their leases are coming to an end, these head tenants plan to renegotiate their leases, or enter into new leases, with a view to including provisions that provide them with rights and protections that are similar to those found in the RTA.

Conclusion

While I fear that this will sound like a shameless plug, I truly think that the smartest thing that a head tenant in these circumstances can do before it negotiates a new lease and/or attempts to enforce an existing lease is to contact a lawyer. As discussed above, in a commercial tenancy, the lease will govern the parties' relationship and, for this reason, the terms of the lease are extremely important. It follows that the negotiation, drafting and/or enforcement of the lease will likely be a complicated process that will require expert knowledge of both residential and commercial tenancy law. A lawyer that practices in these areas of law is best suited to accomplish this task.