

**ONTARIO
SUPERIOR COURT OF JUSTICE
IN BANKRUPTCY AND INSOLVENCY**

IN THE MATTER OF THE BANKRUPTCY OF
CURRICULUM SERVICES CANADA/
SERVICES DES PROGRAMMES D'ÉTUDES CANADA
OF THE CITY OF TORONTO, IN THE MUNICIPALITY OF TORONTO
IN THE PROVINCE OF ONTARIO

FACTUM OF THE TRUSTEE

December 17, 2018

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PART I - OVERVIEW

1. This motion concerns the entitlement of a landlord to a preferred claim under section 136(1)(f) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985 c. B-3 (“**BIA**”) and to an unsecured claim under section 136(3) of the BIA for damages alleged to have been incurred due to the disclaimer of a lease by a trustee in bankruptcy.
2. RSM Canada Limited is the trustee in bankruptcy (the “**Trustee**”) of the bankruptcy estate of Curriculum Services Canada / Services des Programmes D’Etudes Canada (“**Curriculum**” or the “**Bankrupt**”), a bankrupt which filed an assignment for the general benefit of creditors on March 28, 2018.
3. The moving party, Medallion Corporation as authorized agents for 280 Richmond Street West Limited (the “**Landlord**”), brings this motion to appeal from the partial disallowance of its Proof of Claim dated April 20, 2018 (the “**Proof of Claim**”) by the Trustee. The Landlord seeks, among other things, an order setting aside the Notice of Partial

Disallowance issued by the Trustee, together with a declaration that the Landlord is entitled to an unsecured claim for the balance of its accelerated rent claim pursuant to section 136(3) of the BIA.

PART II - SUMMARY OF FACTS

Background to the Motion

4. The Bankrupt conducted a business out of premises at 280 Richmond Street West, 6th Floor, pursuant to a lease dated May 26, 2017 between the landlord and Curriculum. The lease was for 8,322 square feet of space for a term of ten years and six months, commencing on July 1, 2017 and expiring on December 31, 2027.

Reference: Affidavit of Joseph Cacciola sworn October 16, 2018 ("Cacciola Affidavit") at paras. 4 and 5, Motion Record of Medallion Corporation ("MR"), Tab 2, p. 2

5. On March 28, 2018, Curriculum filed an assignment for the benefit of its creditors. On March 29, 2018, Curriculum became bankrupt and the Trustee was appointed.

Reference: Cacciola Affidavit at paras. 8 and 10, MR, Tab 2, p. 4

6. On or about April 20, 2018, the Landlord filed a Proof of Claim with the Trustee claiming: (1) a preferred claim for three months' accelerated rent in the amount of \$100,558.59 under section 136(1) (f) of the BIA; and (2) an unsecured claim in the amount of \$4,028,111.23 for the unexpired portion of the term of the Lease under section 136(3) of the BIA.

Reference: Proof of Claim of Landlord, Exhibit "C" to Cacciola Affidavit, MR, Tab 2C, pp. 114-118

7. On April 23, 2018, the Trustee issued to the Landlord a Notice of Disclaimer of Lease pursuant to the BIA, effective on that date.

Reference: Disclaimer of Lease by Trustee, Exhibit "D" to Cacciola Affidavit, MR, Tab 2D, p. 120

8. Upon review by the Trustee and its counsel of the Proof of Claim filed by the Landlord, the Trustee issued a Notice of Partial Disallowance of Claim pursuant to s. 135(3) of the BIA. The Notice of Partial Disallowance disallowed in part the claim made for priority in the amount of \$100,558.59 on the basis that the realization by the Trustee from the assets (office equipment) on the leased premises totaled \$24,571.00. Accordingly, the Trustee admitted a claim for \$24,571.00 with priority under section 136(1)(f) of the BIA, in addition to the occupation rent of \$25,698.31 (\$14,831.65 plus HST of \$1,928.12 for April 1-15, 2018 and the occupation rent of \$7,910.21 plus HST of \$1,028.33 for April 16-23, 2018) that the Trustee paid to the Landlord .

Reference: Notice of Partial Disallowance of Claim by Trustee, Exhibit "E" to Cacciola Affidavit, MR, Tab 2E, p. 122

9. With respect to the initial claim by the Landlord for the unexpired portion of the term of the Lease in the amount of \$4,028,111.23 (as is discussed further in the "Statement of Issues, Law and Authorities" section below) the Trustee disallowed the claim in its entirety. The reason for the disallowance was that, due to the operation of the provisions of section 146 of the BIA and sections 38 and 39 of the Ontario *Commercial Tenancies Act*, R.S.O. 1990, c. L.7 ("CTA"), the disclaimer of a lease in Ontario by a trustee in bankruptcy is deemed to be a consensual surrender of the lease by the tenant to the landlord, and consequently no claim for damages can be founded on such a secession of obligations under the lease.

Reference: Notice of Partial Disallowance of Claim by Trustee, Exhibit "E" to Cacciola Affidavit, MR, Tab 2E, pp. 122-123

10. On or about October 17, 2018, the Landlord brought a motion returnable October 24, 2018 to appeal from the Notice of Disallowance. The Trustee acknowledges that this motion was brought within the requisite appeal period for an appeal from a Trustee's disallowance under the BIA.

11. Following the disclaimer, the Landlord was successful in mitigating its damages for the unexpired portion of the term in the amount of \$4,028,111.23 by obtaining another tenant to lease the premises. Accordingly, the Landlord is amending its claim for the unexpired portion of the term claimed in the Proof of Claim, to now make a claim in the Affidavit of Joseph Cacciola sworn October 16, 2018, and in its Notice of Motion, for recovery of the tenant inducements provided to the Bankrupt under the terms of the Lease, being the amount of leasehold improvements provided at the Landlord's cost under the Lease (the "**Improvements**") in the amount of \$45,280, and the free rent for a six-month period (the "**Free Rent**") totalling \$175,225.28.

Reference: Notice of Appeal from Disallowance of Claim dated October 17, 2018 and Cacciola Affidavit, MR, Tabs 1 and 2, pp. 1-19

PART III - STATEMENT OF ISSUES, LAW & AUTHORITIES

12. The issues to be decided on this motion are:
 - (a) whether the Landlord has a priority claim under section 136(1)(f) of the BIA and, if so, the amount of that claim; and

- (b) whether the Landlord has an unsecured claim for damages in respect of the Improvements and Free Rent under section 136(3) of the BIA.

A) Does the Landlord Have a Priority Claim under Section 136(1)(f) of the BIA

13. Pursuant to section 136(1)(f) of the BIA, a landlord has a priority claim (with a respective ranking) for rental arrears for the three-month period preceding the bankruptcy and the three-month period following the bankruptcy, if entitled to accelerated rent under the lease. The amount of the priority claim cannot exceed the realization from the property on the leased premises. The section in its entirety reads:

136(1)(f) the lessor for arrears of rent for a period of three months immediately preceding the bankruptcy and accelerated rent for a period not exceeding three months following the bankruptcy if entitled to accelerated rent under the lease, but the total amount so payable shall not exceed the realization from the property on the premises under lease, and any payment made on account of accelerated rent shall be credited against the amount payable by the trustee for occupation rent;

Reference: Bankruptcy and Insolvency Act, R.S.C., c. B-3 [BIA], s. 136(1)(f)

14. Citing Houlden & Morawetz, *Bankruptcy and Insolvency Law of Canada*, (“**Houlden & Morawetz**”) the Alberta Court of Appeal in its 2011 decision in *Dancole Investments Ltd. v. House of Tools Co. (Trustee of)* described the priority claim for accelerated rent under section 136(1)(f) as follows:

“However, rent payable by the receiver for its use and occupation of the property is distinct from any accelerated rent provided by the lease, and does not arise from the same legal foundation. Accelerated rent is not based on use or occupancy of the leased property during the three months following the bankruptcy. The basis on which accelerated rent is payable is set out in Houlden and Morawetz at 5-254 - 55, as follows:

... accelerated rent is not in reality a sum payable in respect of three months following the bankruptcy; rather, it is a further sum equivalent to three months' rent payable in respect of the demised term by reason of its sudden termination. The amount payable is designed to compensate the landlord for the possible vacancy consequent upon the loss by the landlord of its tenant and for the loss of the right of distress.”

Reference: Dancole Investments Ltd. v. House of Tools Co. (Trustee of), 2011 ABCA 145, 2011 CarswellAlta 774 [Dancole Investments] at para. 27, citing Houlden & Morawetz, Bankruptcy and Insolvency Law of Canada, (4th ed.) loose-leaf (updated to Release 9, 2010) (Toronto: Thomson Reuters Canada Limited, 2009), Brief of Authorities of the Trustee dated December 17, 2018 (“Trustee’s BOA”), Tab 1

15. As outlined above, the Trustee admitted a claim for \$24,571.00 with priority under section 136(1)(f) of the BIA, being the total amount realized by the Trustee from assets on the leased premises (in addition to the occupation rent paid by the Trustee to the Landlord in the cumulative amount of \$25,698.31). Based on the express limitation in section 136(1)(f) that a landlord’s priority claim cannot exceed the realization from the property on the leased premises, the Trustee cannot admit any higher amount than \$24,571.00 as a priority claim under section 136(1)(f) of the BIA.

B) Does the Landlord Have an Unsecured Claim for Damages in respect of the Improvements and Free Rent under Section 136(3) of the BIA?

16. Pursuant to section 136(3) of the BIA, a creditor whose rights are restricted by section 136 is entitled to rank as an unsecured creditor for the balance of any claim due to him.

Reference: BIA, supra, s. 136(3)

17. However, this does not mean that landlords in every bankruptcy across the country are entitled to make an unsecured claim for any remaining damages. This is because, pursuant to section 146 of the BIA (subject to priority of ranking for arrears of rent and accelerated

rent) the rights of lessors are to be determined according to the law of the province in which the leased premises are situated. Accordingly, as articulated by the Alberta Court of Appeal in its 2015 decision in *York Realty Inc. v. Alignvest Private Debt Ltd.*,

“...[t]he nature and extent of a landlord's claim for rent and damages for the unexpired term of a lease are determined by the law of the province in which the leased premises are situated.”

Reference: BIA, supra, s. 136(3); York Realty Inc. v. Alignvest Private Debt Ltd., 2015 ABCA 355, 2015 CarswellAlta 2108 [York Realty Inc.] at para. 32, Trustee's BOA, Tab 2; Houlden & Morawetz, Bankruptcy and Insolvency Analysis, G§§140-141, Trustee's BOA, Tab 3

18. Sections 38 and 39 of the CTA, which govern a landlord's rights on the bankruptcy of a tenant in Ontario, are silent as to whether a landlord can pursue an unsecured claim for its damages over and above its preferred claim. This is to be contrasted with certain provincial legislation which expressly provides that a landlord has no right to claim as a debt any unexpired term of the lease, such as the *Landlord's Rights on Bankruptcy Act*, R.S.A. 2000, c. L-5, which was the Alberta statute at issue in the *York Realty Inc.* case. Accordingly, it is necessary to turn to the jurisprudence interpreting the CTA to determine whether a landlord can pursue an unsecured claim for damages in a tenant's bankruptcy in Ontario.

Reference: Commercial Tenancies Act, R.S.O. 1990, c. L.7, ss. 38-39; York Realty Inc., supra, Trustee's BOA, Tab 2

19. Registrar Nettie considered the issue of whether there is a damages remedy for landlords in Ontario beyond section 38 of the CTA and section 136 of the BIA in *Re Linens N Things Canada Corp.* and ultimately concluded that there is not. Registrar Nettie was persuaded

by the fact that neither the CTA, nor the BIA provide for this type of claim and, even more importantly, that nearly a century of Ontario case law has held that

“...the effect of a surrender or disclaimer by a trustee in this Province is as if there was a consensual surrender of the lease. In other words, it is at an end, and no claim for damages can possibly be founded from such a cessation of obligations under the lease.”

Reference: Linens N Things Canada Corp., Re, 2009 CarswellOnt 2849 (S.C.J.) at paras. 12-24, Trustee’s BOA, Tab 4

20. Houlden & Morawetz confirms that, after a disclaimer or surrender of a lease by a trustee, “there is no right in Ontario to claim damages for the unexpired portion of the lease”.

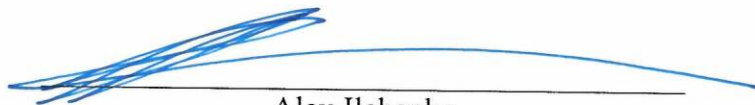
Reference: Houlden & Morawetz, Bankruptcy and Insolvency Analysis, G§§140-141, Trustee’s BOA, Tab 3

21. Accordingly, the Landlord is not entitled to make an unsecured claim for damages in the bankruptcy estate in respect of the Improvements and Free Rent, or for any remaining amount of preferred claim under S.136(1)(f) of the BIA that exceeds the value of the assets on the premises.

PART IV - ORDER REQUESTED

22. The Trustee respectfully requests an order dismissing this motion.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 17th day of December, 2018.



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SCHEDULE "A"

LIST OF AUTHORITIES

1. *Dancole Investments Ltd. v. House of Tools Co. (Trustee of)*, 2011 ABCA 145, 2011 CarswellAlta 774
2. *York Realty Inc. v. Alignvest Private Debt Ltd.*, 2015 ABCA 355, 2015 CarswellAlta 2108
3. Houlden & Morawetz, *Bankruptcy and Insolvency Analysis*, G§§140-141
4. *Linens N Things Canada Corp., Re*, 2009 CarswellOnt 2849 (S.C.J.)

SCHEDULE "B"

TEXT OF STATUTES, REGULATIONS & BY - LAWS

Commercial Tenancies Act, R.S.O. 1990, c. L.7

...

Lien of landlord in bankruptcy, etc.

38. (1) In case of an assignment for the general benefit of creditors, or an order being made for the winding up of an incorporated company, or where a receiving order in bankruptcy or authorized assignment has been made by or against a tenant, the preferential lien of the landlord for rent is restricted to the arrears of rent due during the period of three months next preceding, and for three months following the execution of the assignment, and from thence so long as the assignee retains possession of the premises, but any payment to be made to the landlord in respect of accelerated rent shall be credited against the amount payable by the person who is assignee, liquidator or trustee for the period of the person's occupation. R.S.O. 1990, c. L.7, s. 38 (1).

Rights of assignee

(2) Despite any provision, stipulation or agreement in any lease or agreement or the legal effect thereof, in case of an assignment for the general benefit of creditors, or an order being made for the winding up of an incorporated company, or where a receiving order in bankruptcy or authorized assignment has been made by or against a tenant, the person who is assignee, liquidator or trustee may at any time within three months thereafter for the purposes of the trust estate and before the person has given notice of intention to surrender possession or disclaim, by notice in writing elect to retain the leased premises for the whole or any portion of the unexpired term and any renewal thereof, upon the terms of the lease and subject to the payment of the rent as provided by the lease or agreement, and the person may, upon payment to the landlord of all arrears of rent, assign the lease with rights of renewal, if any, to any person who will covenant to observe and perform its terms and agree to conduct upon the demised premises a trade or business which is not reasonably of a more objectionable or hazardous nature than that which was thereon conducted by the debtor, and who on application of the assignee, liquidator or trustee, is approved by a judge of the Superior Court of Justice as a person fit and proper to be put in possession of the leased premises. R.S.O. 1990, c. L.7, s. 38 (2); 2006, c. 19, Sched. C, s. 1 (1).

Lien of landlord in bankruptcy, etc., further provisions **Election to surrender**

39. (1) The person who is assignee, liquidator or trustee has the further right, at any time before so electing, by notice in writing to the landlord, to surrender possession or disclaim any such lease, and the person's entry into possession of the leased premises and their occupation by the person, while required for the purposes of the trust estate, shall not be deemed to be evidence of an intention on the person's part to elect to retain possession under section 38. R.S.O. 1990, c. L.7, s. 39 (1).

Rights of sub-tenants

(2) Where the assignor, or person or firm against whom a receiving order has been made in bankruptcy, or a winding up order has been made, being a lessee, has, before the making of the assignment or such order demised any premises by way of under-lease, approved or consented to in writing by the landlord, and the assignee, liquidator or trustee surrenders, disclaims or elects to assign the lease, the under-lessee, if the under-lessee so elects in writing within three months of such assignment or order, stands in the same position with the landlord as though the under-lessee were a direct lessee from the landlord but subject, except as to rental payable, to the same liabilities and obligations as the assignor, bankrupt or insolvent company was subject to under the lease at the date of the assignment or order, but the under-lessee shall in such event be required to covenant to pay to the landlord a rental not less than that payable by the under-lessee to the debtor, and if such last mentioned rental was greater than that payable by the debtor to the said landlord, the under-lessee shall be required to covenant to pay to the landlord the like greater rental. R.S.O. 1990, c. L.7, s. 39 (2).

Settlement of disputes

(3) In the event of any dispute arising under this section or section 38, the dispute shall be disposed of by a judge of the Superior Court of Justice upon an application. R.S.O. 1990, c. L.7, s. 39 (3); 2006, c. 19, Sched. C, s. 1 (1).

...

Bankruptcy and Insolvency Act, R.S.C. 1985 c. B-3

...

Scheme of Distribution

Priority of claims

136 (1) Subject to the rights of secured creditors, the proceeds realized from the property of a bankrupt shall be applied in priority of payment as follows:

(a) in the case of a deceased bankrupt, the reasonable funeral and testamentary expenses incurred by the legal representative or, in the Province of Quebec, the successors or heirs of the deceased bankrupt;

(b) the costs of administration, in the following order,

(i) the expenses and fees of any person acting under a direction made under paragraph 14.03(1)(a),

(ii) the expenses and fees of the trustee, and

- (iii) legal costs;
- (c) the levy payable under section 147;
- (d) the amount of any wages, salaries, commissions, compensation or disbursements referred to in sections 81.3 and 81.4 that was not paid;
 - (d.01) the amount equal to the difference a secured creditor would have received but for the operation of sections 81.3 and 81.4 and the amount actually received by the secured creditor;
 - (d.02) the amount equal to the difference a secured creditor would have received but for the operation of sections 81.5 and 81.6 and the amount actually received by the secured creditor;
- (d.1) claims in respect of debts or liabilities referred to in paragraph 178(1)(b) or (c), if provable by virtue of subsection 121(4), for periodic amounts accrued in the year before the date of the bankruptcy that are payable, plus any lump sum amount that is payable;
- (e) municipal taxes assessed or levied against the bankrupt, within the two years immediately preceding the bankruptcy, that do not constitute a secured claim against the real property or immovables of the bankrupt, but not exceeding the value of the interest or, in the Province of Quebec, the value of the right of the bankrupt in the property in respect of which the taxes were imposed as declared by the trustee;
- (f) the lessor for arrears of rent for a period of three months immediately preceding the bankruptcy and accelerated rent for a period not exceeding three months following the bankruptcy if entitled to accelerated rent under the lease, but the total amount so payable shall not exceed the realization from the property on the premises under lease, and any payment made on account of accelerated rent shall be credited against the amount payable by the trustee for occupation rent;
- (g) the fees and costs referred to in subsection 70(2) but only to the extent of the realization from the property exigible thereunder;
- (h) in the case of a bankrupt who became bankrupt before the prescribed date, all indebtedness of the bankrupt under any Act respecting workers' compensation, under any Act respecting unemployment insurance or under any provision of the *Income Tax Act* creating an obligation to pay to Her Majesty amounts that have been deducted or withheld, rateably;
- (i) claims resulting from injuries to employees of the bankrupt in respect of which the provisions of any Act respecting workers' compensation do not apply, but only to the extent of moneys received from persons guaranteeing the bankrupt against damages resulting from those injuries; and

(j) in the case of a bankrupt who became bankrupt before the prescribed date, claims of the Crown not mentioned in paragraphs (a) to (i), in right of Canada or any province, rateably notwithstanding any statutory preference to the contrary.

Payment as funds available

(2) Subject to the retention of such sums as may be necessary for the costs of administration or otherwise, payment in accordance with subsection (1) shall be made as soon as funds are available for the purpose.

Balance of claim

(3) A creditor whose rights are restricted by this section is entitled to rank as an unsecured creditor for any balance of claim due him.

...

Application of provincial law to lessors' rights

146 Subject to priority of ranking as provided by section 136 and subject to subsection 73(4) and section 84.1, the rights of lessors are to be determined according to the law of the province in which the leased premises are situated.

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