

Bankruptcy and the Landlord Tenant Relationship

Introduction

In the context of a commercial lease setting, the default and/or filing for creditor protection by a tenant can trigger a number of issues that can require the advice and assistance of counsel. The typical triggering events are:

- a) Where the tenant is in bankruptcy under federal law, specifically the *Bankruptcy and Insolvency Act*, and has a trustee in bankruptcy appointed over the tenant's assets;
- b) Where the tenant is in receivership under provincial law and has a receiver appointed over the tenant's assets;
- c) Where the tenant has sought "creditor protection" by filing a notice of intention to make a proposal or by filing a proposal under the *Bankruptcy and Insolvency Act*; and
- d) Where the landlord wishes to pursue its remedies against the tenant defaulting under the lease outside of the above forms of insolvency proceedings.

This paper will review various legal issues faced by the lawyer in each of these circumstances, whether the lawyer is acting for the landlord or the tenant.

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I. Bankruptcy and the Landlord Tenant Relationship

A. Background

The bankruptcy of a tenant in a commercial leasing context can create havoc for the landlord, and for good reason. Not only is a stream of revenue from the tenant lost, the landlord must now deal with the complicated area of enforcing his rights as a landlord over the leased premises. At first glance, this would appear to be a straightforward process. The landlord simply repossesses the premises, finds a new tenant and carries on. The process, for a variety of reasons, is not that simple. The landlord must take special care and attention to protect and preserve its rights and remedies.

The ability of a Trustee in bankruptcy for the Tenant to occupy, retain, assign or disclaim can be quite disruptive to the landlord's business. Indeed, placing or petitioning a debtor tenant into bankruptcy is often an effective strategy used by the tenant's creditors to neutralize any threat a landlord can pose regarding distraining assets or terminating the lease. For as long as three months from the date of the Tenant's assignment into bankruptcy or receiving order, the landlord may be left with no control over the occupation of the premises, be entitled only to a subordinated preferential claim to any surplus assets on the leased premises after the claims of secured and prior preferred creditors have been paid in full, and may not have any claim against the Tenant's Trustee who does not occupy the lease premises.

B. Stay of Proceedings

By operation of, s. 69(1)(a), 69.1(1)(a), and s. 69.3(1) of the *Bankruptcy & Insolvency Act*, upon the debtor/tenant either being assigned or petitioned into bankruptcy or with the Tenant filing a Notice of Intention to make a proposal to its creditors, a stay of proceedings is imposed on any actions by creditors against the insolvent person. As a result no creditor has a remedy against the insolvent person (the tenant) or his property, or shall commence or continue any action, execution or other proceedings, for the recovery of a claim provable in bankruptcy.

The wide scope of the language used in the above provisions includes a landlord's remedies under its lease, including the right to possession (subject to the rights of the Trustee, as discussed below), the right to commence proceedings for damages for breach of lease and the right to distrain.

A landlord is however entitled to file a proof of claim with the Trustee for arrears of rent and accelerated rent pursuant to s. 136(1)(f) of the *Bankruptcy and Insolvency Act*.

Under s. 69.4 of the *Bankruptcy and Insolvency Act* a creditor may apply for a declaration that s. 69 to

s. 69.3 no longer restrict that creditor, and a Court will grant the declaration if the creditor is materially prejudiced by those sections or if it is otherwise equitable to do so. The term “materially prejudiced” has not been defined with precision by the Courts, and an Order under this section is a matter of the Court’s discretion.

C. Landlord’s Right of Distraint Prior to Bankruptcy

A “distraint” is a non-judicial procedure whereby the landlord, typically through a licenced bailiff, takes possession of the assets of the tenant upon the tenant’s failure to pay rent when due under the lease. The procedure is governed by the *Rent Distress Act* of BC. The question then is what happens to the landlord’s right to distraint when the tenant goes into bankruptcy.

The *Bankruptcy & Insolvency Act* provides that a landlord’s right to distraint on the goods and chattels of the tenant in priority to the claims of various classes of secured creditors is terminated by the bankruptcy. This applies to a landlord’s right to distraint as well (*Ford Credit Canada v. Crosbie Realty Ltd.* (1992), 12 C.B.R. (3d) 282, 301 A.P.R. 322 (Nfld. C.A.)).

A secured creditor gains first priority, followed by various classes of preferred creditors, and then by the landlord who has a limited claim to three months’ rent, per s. 136(1)(f) of the *Bankruptcy & Insolvency Act*. This gives secured creditors an incentive to defeat the landlord’s distress claim by petitioning the tenant into bankruptcy before the landlord can complete his distress. It is considered proper strategy for a secured creditor to promote a bankruptcy to permit the secured creditor to assert a claim over the assets of a bankrupt tenant in priority to the landlord (Williams and Rhodes, *Canadian Law of Landlord & Tenant*, 6th ed. (Toronto; Carswell, 1988) at p.8-23).

Section 73(4) of the *Bankruptcy and Insolvency Act* provides that any property under an ongoing distraint and any money realized therefrom which has not yet been paid to the landlord must be returned to the Trustee upon the bankruptcy order or assignment (*Clark’s Sporting Goods Inc. (Trustee of) v. Greystone Motel Ltd.* (1988), 72 C.B.R. (N.S.) 124 (Sask Q.B.))

If the landlord has completed the distress and has been paid by the bailiff, the Trustee will have no recourse (*Southern Fried Foods Ltd.* (1976), 21 C.B.R. (N.S.) 267 (Ont. S.C.)).

Even if the distraint is entirely completely before the bankruptcy, there are cases where the court held that there is a presumption of a fraudulent preference, thereby putting the onus on the landlord to rebut the presumption (*Thorne Ernst & Whinney Inc. v. Gazzola* (1986), 60 D.L.R. (4th) 590).

A key practice point when acting for a landlord is to consider whether it is worthwhile to levy distress under the *Rent Distress Act* prior to terminating the lease.

D. The Trustee's Right of Occupation

The concept of a Trustee's right of occupation to the defaulting Tenant's lease premises is often a thorny issue for the landlord. In the instance where a tenant breaches its lease by being assigned or petitioned into bankruptcy, the landlord in most cases simply wants the tenant out and to have the ability to re-let the premises to a new tenant of the landlord's choosing as soon as possible. On the surface, this seems to be only fair to the landlord.

However, s. 146 of the *Bankruptcy & Insolvency Act* provides that the rights of landlords are determined by the laws of the province. In British Columbia, the most notable statutory provisions in this regard are contained at s. 29 of the *Commercial Tenancy Act*. In particular, s. 29(2) of the *Commercial Tenancy Act* gives the Trustee an unconditional right to occupy the premises for three months from the date of the bankruptcy order or assignment where the lease does not create a monthly tenancy or has not yet been terminated at the date of bankruptcy (*Re Limestone Electrical and Supply Co. Ltd.*, 1955 3 D.L.R. 104, (1955) O.R. 591 (C.A.)).

This right is not exercisable where the landlord has validly re-entered and terminated the lease but is subject to a right of relief from forfeiture (*Re Custom Cresting Limited* (1975), 19 C.B.R. (N.S.) 282 (Ont. S.C.)).

An attempt to terminate the lease by the landlord after the date of the petition, but before a bankruptcy order is made, will be ineffective (*Raymond, Chabot, et al. v. Hyatt Construction Corp.* (1984), 51 B.C.L.R. 129., 50 C.B.R. (N.S.) 225 sub nom *Re Security Group N.A.C. Inc.* (C.A.)).

Likewise, where the lease states that upon bankruptcy of the tenant the lease is automatically terminated, the Trustee of the tenant is not vested with the tenant's interest. If on the other hand the lease states that upon the bankruptcy of the tenant the landlord has the option to terminate the lease, the tenant's interest vests with the Trustee. It is therefore critical at the onset to review the wording of the lease carefully. There is no such thing as a Standard "Commercial Lease". Does it contain a provision stating that the lease is automatically terminated on the bankruptcy of the tenant or does it merely state that on a bankruptcy of the tenant the lease terminates at the option of the landlord? The *Raymond, Chabot, Fafard, Gagnon Inc.* case indicates that where the lease states that a bankruptcy of the tenant terminates the lease automatically, the trustee of the tenant is not vested with the tenant's interest. If the lease

terminates at the option of the landlord (as was the case in the *Raymond, Chabot, Fafard, Gagnon Inc.* decision), the tenant's interest vests with the Trustee.

E. The Trustee's Right to Assign the Lease

The combined effect of s. 29(2), s. 29(3), and s. 29(4) of the *Commercial Tenancy Act* also gives a Trustee the right to elect to disclaim the lease or to assign it to a fit and proper person (*Campbell Saunders Ltd. v. Pontiac Holdings Ltd.* unreported March 1, 1991 (B.C.S.C.)).

Trustees in bankruptcy are generally wary of electing to affirm the lease as it may become a personal liability of the Trustee. However, if the lease space can be assigned to a third party as part of an effort to maximize recovery for the bankrupt tenant's estate, a Trustee may elect to affirm the lease.

In order for a Trustee assign the lease to a third party, the Trustee must elect to retain the remainder of the lease within three months of the date of the bankruptcy order or assignment. If the Trustee fails to make the election within this period, it loses the ability to make the assignment (*Davis, Daignault, Schick & Co. v. K & H Hldg. Ltd.* (1986), 3 B.C.L.R. 275 (B.C.C.A.)).

Section 29(3) of the *Commercial Tenancy Act* provides that if the lease contains a condition that the lease shall not be assigned without the leave or consent of the landlord, and the landlord refuses such consent, the Trustee may apply to Court for an order that such a condition is of no effect and that the Trustee's assignment of the lease to a third party be approved.

On an application for approval, reliance is placed on the judgment of the Trustee (*Re Sunnybrook Meat Markets (Yonge) Ltd.* (1973), 1 O.R. (2d) 537, 41 D.L.R. (3d) 46 (H.C.J.)). The approval may be given on terms (*Re FigurMagic International Ltd.* (1974), 19 C.B.R. (N.S.) 92 (Ont. H.C.J.)). There are numerous factors that the court will consider in approving the assignment:

- 1) Whether the tenant will be responsible and respectable, both personally and financially. It is not enough for the Trustee to merely establish that there is no fraud and that the transaction is at arm's length (*Peat Marwick Ltd. v. Kingswood Holdings Ltd. and Woodbrook Holdings Ltd.* (1983), 46 B.C.L.R. 267 (S.C.));
- 2) Whether the tenant will be both motivated and able to honour the covenants in the lease and whether it will make a fit and proper use of the premises. As a corollary, the landlord cannot require the assignee to be a more upscale tenant than the bankrupt (*Re Griff & Sommerset* (supra); *Elks Inc. (Trustee of) v. Simpson Ltd.* (1991), 5 C.B.R. (3d) 230 (Ont. Gen. Div.));

- 3) The reputation of the proposed tenant, the creditworthiness of the tenant, and the benefit to the estate of the bankrupt;
- 4) The intention of the proposed tenant to occupy the premises (*Re Niki's Palace Restaurant Ltd.* (1983), 48 C.B.R (N.S.) 236 (Ont. H.C.J.));
- 5) The provisions in the lease and the effect of a deviation from such provisions. For example, where the lease restricted the use of shopping centre premises to the sale of micro-wave ovens and strictly prohibited the sale of food, and the landlord had entered into restrictive covenants to this effect with other tenants, a proposed assignment to a food retailer was rejected by the court (*Micro Cooking Centres (Canada) Inc. (Trustee of) v. Cambridge Leaseholds Ltd.* (1988), 48 R.P.R. 32, 68 C.B.R. (N.S.) 60 (Ont. H.C.I.)). The courts' approach on this issue is varied (*Robinson, Little & Co. (Trustee of) v. Intra Land Corp.* (1987), 67 C.B.R (N.S.) 33, 56 Alta. L.R. (2d) 329 (C.A.) and *Re Robinson, Little & Co. (Trustees of) v. Marlowe Yeoman Ltd.* (1986), 5 B.C.L.R 67 (C.A.)).

F. Obligation Upon the Trustee to Pay Occupation Rent

As discussed, s. 29(2) of the *Commercial Tenancy Act* provides the Trustee with the right to “hold and retain” the leased premises on the same terms and conditions as those held by the tenant.

Section 29(7) of the *Commercial Tenancy Act* provides that a landlord cannot file a claim in the estate of the bankrupt tenant for the unexpired portion of the lease. However, the landlord can look to the Trustee to pay rent for the period which the Trustee “actually occupies” the premises.

The question then is whether a Trustee has merely “held and retained” the premises under s. 29(2) of the *Commercial Tenancy Act* (in which case the Trustee is not liable to pay occupation rent) or whether the Trustee has “occupied” the premises under s. 29(7) of the *Commercial Tenancy Act* (in which case the Trustee must pay rent).

The test for whether a trustee has occupied, rather than “held and retained”, a premises in question was laid out by the BC Court of Appeal in *Sawridge Manor Ltd. v. Western Canada Beverage Corp.* (1995) 33 C.B.R. (3d) 249, 61 B.C.A.C. 32. In *Sawridge*, the Trustee changed the locks without giving the landlord a key, employed the tenant's former plant manager and had him perform inspections and maintenance work on the line located on the premises, hired members of the tenant's staff to conduct inventories and show the premises to prospective purchasers, and had electricity, fax and phone lines continued on the premises at the Trustee's expense.

The Court of Appeal held in *Sawridge* that this went beyond merely “holding and retaining the premises” and amounted to occupying. The Trustee was required to pay occupation rent.

Not surprisingly, it is always a question of fact in each case as to whether or not the Trustee actually occupies the premises (*Re Beatty Ltd. Partnership* (1991), C.B.R. (3d) 225 (Ont. Ct. of Justice (Gen. Div.))).

G. Calculation of Occupation Rent

Occupation rent is generally calculated under the provisions of the lease. In *Provost Shoe Shops Ltd. (Trustee of) v. Markborough Properties Ltd.* (1993), 21 C.B.R. (3d) 153 (N.S.T.D.), the Court explicitly upheld the general principle that the terms of the lease apply to the calculation of occupation rent. In this case, percentage rent, and not just base rent, was therefore included as an element of compensation.

H. Landlord’s Preferred Claim for Accelerated Rent

The theory behind accelerated rent is to provide compensation to a landlord for the loss of tenancy due to the tenant’s bankruptcy. Under s. 136(1)(f) of the *Bankruptcy & Insolvency Act*, a landlord is granted a preferred claim for:

- (a) arrears of rent for three months prior to the bankruptcy; and
- (b) accelerated rent for a period not exceeding three months after the date of bankruptcy if so authorized under the lease, but the total amount payable shall not exceed realization from the property on the premises, and any payment for accelerated rent shall be credited against the Trustee’s occupation rent, if any. If there is no language in the lease authorizing payment of accelerated rent, the landlord cannot claim it (*Re Tentman* (1926), 7 C.B.R. 355 (Ont. Reg); Houlden and Morawetz, *Annotated Bankruptcy and Insolvency Act*, Toronto, Carswell, 1999, pp. 513-514).

Contrary to the preferred claim for three months’ arrears and three months’ accelerated rent provided for in s. 136(1)(f) of the *Bankruptcy & Insolvency Act*, s. 29(6) of the *Commercial Tenancy Act* provides that the landlord only has a general claim, and not a preferred claim, for those arrears and accelerated rent.

The case law resolves this inconsistency and makes clear that the provisions of s. 136(1)(f) of the *Bankruptcy & Insolvency Act* prevails and provides the landlord with preferred claims in this regard (*Sawridge Manor Ltd. v. Western Canada Beverage Corp.* (1995), 33 C.B.R. (3d) 249, 61 B.C.A.C. 32 and *Carpita Corp. (Trustee of) v. Douglas Shopping Centre Ltd.*, 52 B.C.L.R. (2d) (1990) 344 (S.C.)).

Arrears of rent are calculated for a three-month period ending on the day immediately prior to the bankruptcy and occupation rent commences to run from the date of the bankruptcy, regardless of the due date for rent under the lease (*Provost Shoe Shops Ltd. (Trustee of) v. Markborough Properties Ltd. (supra)*).

I. Accelerated Rent as a Preferred Claim Payable from Property on the Premises

As a precondition for the landlord to obtain any amounts for accelerated rent, there must be property of the bankrupt on the premises upon which the Trustee can make a realization. Section 136(1)(f) of the *Bankruptcy and Insolvency Act* has been described as a statutory mechanism that limits and restricts the landlord's preferred claim to the rent amount of the sum realized from the property on the premises (*Re Gladys's* (1995), 30 C.B.R. (3d) 172 (Ont. Bkcty.)). Under s. 136(1)(f) of *Bankruptcy and Insolvency Act*, a claim for accelerated rent cannot exceed amounts realized upon from the premises (*Re Head & Fish* (1975) 21 C.B.R. (N.S.) 94 (B.C.S.C.)). Only the landlord of the head offices of the tenant can look to accounts receivable for payment of its preferred claim (*Re St. Clair Paint & Wallpaper Corp.* 1998 Carswell Ont. 2050 (Ont. Gen. Div.)).

In *Modatech Systems Inc. vs. Bastion Development Corp* (1998) 59 BCLR (3d), the Court of Appeal held that a landlord's right to preferred rent is limited to chattels and goods of the tenant on the lease premises and did not extend to intangible property or chattels of an "incorporeal" nature- in that instance, source codes and software programs.

J. Landlord's Claim for Damages for the Unexpired Term of the Lease

Under s. 29(7) of the *Commercial Tenancy Act*, the landlord has no claim for damages for the unexpired term of the lease where the lease was not yet terminated at the date of bankruptcy and where the Trustee has disclaimed the lease after the date of bankruptcy.

Damages which are not provable after a disclaimer will include all loss of future rent and any expenses, including realty taxes and maintenance costs, which relate to the period after the date of disclaimer (*Re Vrablik* (1993), 17 C.B.R. (3d) 152 (Gen. Div.)). If the Trustee elects to disclaim a lease, all rights and obligations under the lease are terminated as of the effective date of the disclaimer, as if the lease had been surrendered with the consent of the landlord (*In re Mussens Limited* (1933), 14 C.B.R. 479 (S.C.O.)).

However, any damages which formed a valid cause of action in existence prior to the date of such disclaimer continue to be an obligation of the tenant provable as a general claim in the tenant's bankruptcy.

The reality facing a landlord then is that upon the bankruptcy of a tenant, the leased premises owned by the tenant can be effectively tied up by the Trustee (ie. "held and retained" per s. 29(2) of the *Commercial Tenancy Act*) with the landlord being limited to a claim of three months accelerated rent as a preferred creditor. Again, this preference may prove to be of little value because:

- (a) the landlord's preference is limited to the bankrupt's property on the premises (which maybe valueless); and
- (b) the landlord's claim is of course subject to the claims of secured creditors and preferred creditors with higher priority under s. 136(1)(f) of the *Bankruptcy & Insolvency Act*.

K. Former Landlord's Claim for Damages

As discussed, the rights and obligations of the landlord and trustee as set out in s. 136(1)(f) of the *Bankruptcy and Insolvency Act* and s. 29 of the *Commercial Tenancy Act* only apply to a landlord, in that capacity, as at the date of bankruptcy.

Likewise, if the lease has been terminated prior to the date of bankruptcy, the landlord becomes a general creditor for all damages that would otherwise have been payable at law by the tenant. As well, the landlord is not subject to the rights of the Trustee to occupy the premises, assign the lease, etc. as set out in s. 29 of the *Commercial Tenancy Act*.

L. Claims Against a Guarantor or Indemnitor

The law has previously been unsettled regarding the effect of the Trustee's disclaimer of the lease under the *Commercial Tenancy Act* upon the obligations of a guarantor or indemnitor. The law appears to now be settled, as a result of the case of *KKBL No. 297 Ventures Ltd. v. IKON Offices Solutions, Inc.*, 2004 BCCA 468. In that case, the BC Court of Appeal dealt with the effect of a tenant's bankruptcy on the obligations of an indemnitor under the lease. The Trustee had disclaimed the lease, pursuant to the *Commercial Tenancy Act*, following which the indemnitor successfully argued in the Court below that this disclaimer had the effect of releasing the indemnitor from its agreement to indemnify the landlord for the Tenant's lease obligations.

Between the date of the trial Court decision and the hearing at the Court of Appeal, the Supreme Court of Canada decision in *Crystalline Investments Ltd. v. Domgroup Ltd.*, 2004 SCC 3 was released. That decision dealt with a somewhat different fact pattern, concerning the obligations to the landlord of an assignor of leases where the assignee later “repudiated” the leases as part of a proposal under the *Bankruptcy & Insolvency Act*. The Court held that the repudiation provisions of the *Bankruptcy & Insolvency Act* were not intended to protect assignors of a lease from the consequences of their assignee’s repudiation of the lease, and that the repudiation of the leases in the present case did not affect the assignor’s obligation as the original lessee.

The Court then turned to a consideration of those cases in which a guarantor, rather than an assignor, seeks to avoid liability following the bankruptcy of the tenant. The Court specifically overruled the leading case of *Cummer-Yonge Investments Ltd. v. Fagot* (1965), 2 O.R. 152, aff’d (1965), 2 O.R. 157 (Ont. Court of Appeal) which had held that, when a bankrupt tenant’s lease was disclaimed by the Trustee, the guarantor’s obligations disappeared along with the bankrupt’s covenants under the lease. Referring to an English decision similar to *Cummer-Yonge*, the Court held at para. 42:

The House of Lords went on to overrule Stacey v. Hill. In my opinion, Cummer-Yonge should meet the same fate. Post-disclaimer, assignors and guarantors ought to be treated the same with respect to liability. The disclaimer alone should not relieve either from their contractual obligations.

The Court of Appeal in *IKON Office Solutions* regarded *Crystalline* as overruling the cases relied upon by the trial judge. The Court held that because the authorities relied upon by the trial judge no longer governed, having been overruled by the *Crystalline* case, that the trial judge’s decision must be overturned. The Court, therefore, allowed the appeal and held that the obligations of the indemnitor continued despite the bankruptcy of the tenant and the disclaimer of the lease by the Trustee pursuant to the *Commercial Tenancy Act*.

M. Rights of tenant on bankruptcy of landlord

If the landlord is insolvent and a trustee in bankruptcy is appointed, there should be no change in the position and legal rights of the tenants. The trustee is not able to use s. 30(1)(k) of the *Bankruptcy & Insolvency Act* to terminate a lease entered into prior to bankruptcy, as such matters are governed by provincial law (*Re Miller Investments Ltd.* (1984), 28 Man. R. (2d) 243 (Q.B.); *Re Palais des Sports de Montreal Ltee* (1960), 1 C.B.R. (N.S.) 260 (Que. Q.B.)). If a mortgagee goes into possession, however, the tenant’s position will depend on whether the lease or the mortgage is entitled to priority.

If property values decline significantly, tenants may be left in a position where they will have no legal recourse if the landlord or its trustee abandons the building and the mortgagee does not go into possession - the tenant might remain in the building, but be unable to obtain utilities or other services. This situation occurred in the National Trust Building, in Toronto, when the mortgagee's receiver obtained a Court order allowing it to abandon the building after it had gone into possession (*Globe & Mail, February 23, 1993*).

II. Filing by the Tenant of a Notice of Intention to Make a Proposal or the Filing of a Proposal Under the Bankruptcy & Insolvency Act

A. Background

A proposal is not a bankruptcy. In fact, in most instances it is an effort made by the debtor to avoid bankruptcy. In a basic sense, a proposal is an offer made by the debtor to any or all of its creditors regarding its debts. In practice, it is a contract between the debtor and his creditors. There are no real parameters for a proposal. They take many forms and are limited only by the imagination of the draftsman. Ultimately, the debtor's goal is to convince the creditors to accept the plan of compromise put forward. The contract is made binding on the parties subject to the proposal being accepted by the creditors and then approved by the Court.

B. Stay of Proceedings

Upon the filing of a notice of intention to make a proposal or a proposal, a stay of proceedings is imposed upon the landlord pursuant to s. 69(1) and s. 69.1(1) of the *Bankruptcy & Insolvency Act*, respectively. That stay applies to claims by the landlord for damages for breach of the lease, if any, that exist as at the date of the filing.

C. Rights of Termination Limited

Under s. 65.1(1) and (2) of the *Bankruptcy & Insolvency Act*, a landlord may not claim accelerated rent or terminate the lease by reason only of the insolvency of the tenant, the filing of the notice of intention or proposal by the tenant, or the arrears of the tenant to the date of the filing.

With that in mind, under s. 65.1(4)(a), a landlord may insist on immediate payment for rent on a going forward basis after the filing. In *Re Cosgrove-Moore Bindery Services Ltd.*, 48 O.R. (3d) 540 (Ont. S.C.), the tenant failed to pay the month's rent that was due on March 1 and then filed a notice of intention to make a proposal on March 3, before the landlord exercised any of its rights. The tenant then argued that it

need not pay rent for the period March 4 to 31 because that was all part of the rent that was due on March 1 and thus collection of it was stayed. The Court disagreed and required the tenant to pay daily rent from March 4 onward, consistent with the clear language of s. 65.1(4)(a).

Acceptance of rent by a landlord after the making of a proposal may terminate the right to forfeit the lease (*Re McKay; Ex Parte L. R. Steel Co., Ltd.* (1921), 2 C.B.R. 59, 64 D.L.R. 699 (Ont. S.C. in Bankruptcy)). A practice point if acting for landlord's: If a landlord wants the lease terminated ensure the landlord and all staff members understand that no payment after a Notice of Termination can be accepted. All payments must be declined/returned.

D. Tenant may Disclaim Leases

Under s. 65.2(1) of the *Bankruptcy & Insolvency Act*, at any time between the filing of a notice of intention and the filing of a proposal, or on the filing of a proposal, the tenant may disclaim a lease on giving thirty days' notice to the landlord in the prescribed manner.

Section 65.2(2) provides that within fifteen days after being given notice of the disclaimer, the landlord may apply to the court for a declaration that subsection (1) does not apply in respect of that lease. If the landlord does apply, then s. 65.2(3) provides that it is up to the tenant to show that the proposal will not be viable without the disclaimer of that lease and of any other leases that the debtor has disclaimed (*Re Superstar Group of Companies* (2001), 25 C.B.R. (4th) 119 (B.C.S.C.)).

Section 65.2(3) states that no declaration shall be made under subsection (2) if the court is satisfied that the tenant would not be able to make a viable proposal without the repudiation of that lease and all other leases that the tenant has repudiated under subsection (1). The onus of proof is on the tenant to show that the proposal would not be viable without the repudiation of the lease. The court must assess the likelihood of success of the proposal. If the Court decides that the proposal has only a slim chance of success, even if the lease is repudiated, the landlord's application will generally succeed. The making of the lease payment must be the factor that makes the proposal unworkable (*Re Carr-Harris & Co* (1993), 23 C.B.R. (3d) 74 (B.C.S.C.)).

Where the lease is disclaimed by the tenant, s. 65.2(4)(b) provides that the landlord has no claim for accelerated rent but the landlord may file a proof of claim for its actual losses arising from the disclaimer or for an amount equal to a prescribed percentage of lost rent.

III. Proceedings by the Tenant under the Companies Creditors Arrangement Act (“CCAA”)

A. Background

A company with debts in excess of \$5,000,000 may start proceedings under the *CCAA* in order to seek creditor protection while it tries to reorganize its affairs. The *CCAA* has been used as an effective restructuring tool where the debtor is also a Tenant of a number of leases that it wished to disclaim (i.e. Re: Air Canada)

Like a proposal under the *Bankruptcy & Insolvency Act*, there is a stay of proceedings but under the *CCAA* it is ordered by the court on terms set by the court.

B. Distraint and Termination

The initial Order that is granted by the court will typically stay any attempts by the landlord to distraint or terminate the lease.

On the other hand, that order may allow a tenant to terminate and thus disclaim any unwanted leases of premises (*Grafton-Fraser Inc. v. Canadian Imperial Bank of Commerce* (1992), 22 C.B.R. (3d) 161). The landlord in that situation is then typically given the right to claim for damages under the plan of the tenant under the *CCAA* (*Re Ambro Enterprises* (1993), 22 C.B.R. (3d) 80). *Under the 2009 amendments to the CCAA, a debtor tenant has the ability to resile from or disclaim lease agreements per 32(1).*

C. Right to Retain the Premises

The stay of proceedings will allow a tenant to stay in the premises so long as the rent following the date of the initial order is paid (as that rent is not typically stayed by the initial order).

As stated, with the 2009 amendments, the *CCAA* was amended to contain similar language to that in s. 65.2 (1) of the *Bankruptcy and Insolvency Act* to permit a debtor/tenant to disclaim leases as part of the overall restructuring plan.

D. Claim of the Landlord

The claim of the landlord in a *CCAA* proceeding is to be set out in the restructuring plan. There is otherwise no specific authority in the *CCAA* setting out the claim of the landlord (as compared to s. 65.2 of the *Bankruptcy and Insolvency Act*). Attempts have been made to argue that the landlord’s claim ought to mirror the statutory claims in the *Bankruptcy & Insolvency Act* but those attempts have not been

successful. The court will inevitably leave intact the broad flexibility afforded to the court and to the tenant under the CCAA (*Re Alternative Fuel Systems Inc.*, 2004 ABCA 31).

The restructuring plan may thus include a disclaimer of leases and in that case must include a formula for calculating the claim of the landlord. The plan then must ultimately be approved by the creditors. Under the CCAA, the creditors vote in classes. Likewise, a tenant will want to group the landlords in a larger class of creditors, so as to prevent one or more landlords from having a veto power if they were in their own class.

The courts have permitted this on the basis that the purpose of the CCAA, which is to help facilitate corporate reorganizations, would be defeated if an overly fragmented approach to classes was taken and thus jeopardizing the chances of the reorganization being successful (*Sklar-Pepler Furniture Corp. v. Bank of Nova Scotia* (1991), 8 C.B.R. (3d) 312, *Re San Francisco Gifts Ltd.* (2004), 5 C.B.R. (5th) 92, and *Re SAAN Stores Ltd.* (2005), 12 C.B.R. (5th) 35).

IV. Receivership of the Tenant under Provincial Law

A. Background

A Receiver is appointed, generally by a secured lender, to take possession of the debtor tenant's assets for the purposes of protecting the interest of the stakeholders to those assets. In the case of a secured lender, who typically has first priority to the assets, the Receiver will then realize on the assets first to the credit of the secured lender.

At law, a Receiver that is appointed over the entirety of the business of the debtor and is given the mandate to run the business of the debtor is known as a Receiver-Manager. The term "Receiver" in this paper will include a Receiver-Manager.

A Receiver is typically appointed under a general security agreement which grants security over the "personal" (i.e., non-real estate) property of the debtor, or a mortgage, which grants security over the real estate of the debtor, including leases granted to tenants.

A Receiver's appointment is then typically confirmed by the court at the instance of court proceedings by the secured lender. This allows the Receiver to have the greater powers of sale that the court will typically grant and the greater ability to enforce those powers.

B. Overall Rights and Duties of the Receiver

The appointment of a Receiver over a tenant (i.e. being the debtor under a general security agreement and/or a mortgage) will usually place the Receiver in the same position as the tenant with respect to any lease from a landlord.

A Receiver must act and manage the assets of the tenant prudently (Frank Bennett, *Bennett on Receiverships*, 2nd ed. (Scarborough: Carswell, 1998) at 338)).

In the context of a Receivership involving personal property of the tenant, s. 68(2) of the *Personal Property Security Act* will apply, which provides that all rights, duties or obligations of a Receiver shall be exercised or discharged in good faith and in a commercially reasonable manner.

C. Liability for Rent

If the Receiver wishes to retain the premises, the Receiver will be required to pay both the arrears owing to the landlord as well as the ongoing rent that accrues during the Receiver's occupation.

With this said however, a Receiver is generally not personally responsible for occupation rent (to the extent that the Receiver took occupation without payment up front to the landlord). Where a Receiver is appointed under a general security agreement or court order, title still remains in the tenant's name. As such, there is no privity of contract between the Receiver and the landlord (*Hand v. Blow*, [1901] 2 Ch. 721 (C.A.); *Consolidated Entertainments Ltd. v. Taylor*, [1937] 4 All E.R. 432).

In taking possession of the premises, the Receiver should therefore ensure that payments made to the landlord during the Receivership are made in the name of the debtor company and not in the name of the Receiver as otherwise, the landlord may be in a position to argue that a new tenancy was created with the Receiver personally (*Bank of Montreal v. Steel City Sales Limited et al.* (1983), 47 C.B.R. (N.S.) 15 (N.S.S.C.)).

If the Receiver does enter into a new agreement in its personal capacity, the Receiver must to be careful to ensure that there is also an ability to terminate the agreement, likely on terms which are far more in favour than under the tenant's lease with the landlord. The Receiver should ensure that it simply does not assume the terms of the existing lease.

D. Events of Default and Ability of Landlord to Terminate the Lease

Virtually all commercial leases have provisions stating that the insolvency or receivership of the tenant is a default under the lease. However, if the landlord accepts rent from the Receiver, or otherwise waives the breach by the tenant, the Receiver may be able to maintain the tenancy (so long as the rent payments are kept current and there are no other defaults under the lease). That is, the landlord will be prevented from arguing that in any subsequent month there is a new breach of the lease as a result of the continued Receivership of the tenant (*Canadian Freehold Properties Ltd. v. Tamarish Developments Ltd.*, [1975] W.W.D. 131 (B.C.Co.Ct.)).

Even if the receivership or insolvency of the tenant is not specifically an event of default under the lease, the landlord may still take the position that a court appointed Receiver is an unauthorized assignee of the lease and therefore not in valid possession of the premises (*Toronto Dominion Bank v. Almondgrove Holdings Ltd. et al.* (1977), 25 C.B.R. (N.S.) 170 (B.C.S.C.)). On the other hand, an instrument appointed Receiver is generally an agent of the debtor company, and therefore the landlord may not terminate the lease outside of a specific provision in the lease permitting termination in those circumstances.

If the landlord does not elect to terminate the lease as a result of the receivership, the Receiver will be in a position to occupy the premises subject to the terms of the lease and will be in a position to assign it or sublet the premises (subject to any restrictions in the lease) (*Coopers & Lybrand Limited v. William Schwartz Construction Co. Ltd.* (1980), 36 C.B.R. (N.S.) 256 (Alta. Q.B.)).

Where a Receiver is appointed by Court Order, the Order appointing the Receiver will often provide that no proceedings may be commenced against the Receiver without leave of the court. Such a clause is now part of the Model Receivership Order which is now required for a Court Appointment of a Receiver. Despite this, it will not likely be difficult for a landlord to obtain leave to sue the Receiver to enforce the landlord's rights under the lease (*Toronto Dominion Bank v. Almondgrove Holdings Ltd. et al.* (1977), 25 C.B.R. (N.S.) 170 (B.C.S.C.)).

In order to avoid the above problems, a secured creditor will often seek a non-disturbance agreement from the landlord at the time the security is granted. This agreement typically ensures continued occupation by the Receiver and certain rights to assign the lease on the part of the Receiver.

E. Receiver's Right to Seek Relief from Forfeiture

If the landlord insists on terminating the lease and evicting the Receiver, the Receiver may be able to obtain relief from forfeiture of the lease by court application under s. 24 of the *Law and Equity Act*, which

provides that the court may relieve against all penalties and forfeitures, and in granting the relief, may impose any terms as to costs, expenses, damages, compensations and all other matters that the court thinks fit.

Generally, the Receiver must pay all arrears of rent and the legal costs (perhaps on a solicitor and own client basis) of the landlord before the court will grant the relief sought (*Gleneagle Manor Ltd. et al. v. Finn's of Kerrisdale Ltd.* (1980), 116 D.L.R. (3d) 617 (B.C.S.C.); *Premji and Manji v. Milette et al.* (1981), 31 B.C.L.R. 62(S.C.)).

F. Landlord's Right to Distrain

1. Generally

There are typically two avenues for the landlord to take when the tenant does not pay rent when due under the lease, being either to distrain against the assets of the tenant or to terminate the lease of the tenant. As will be discussed, the landlord may not do both, as a termination of the lease ends the right to distrain.

As noted previously, a “distrain” is a non-judicial procedure whereby the landlord, typically through a licenced bailiff, takes possession of the assets of the tenant upon the tenant's failure to pay rent when due under the lease. The procedure is governed by the *Rent Distress Act* of BC. The question then is what happens to the landlord's right to distrain when the tenant is in receivership.

If the landlord allows the Receiver to take over the tenancy, the landlord still maintains its rights under the lease with respect to any arrears owing at the time of the Receivership. The landlord may distrain on account of those arrears (*Saskatoon Credit Union Ltd. v. Parklane Investments Ltd.* (1980), 112 D.L.R. (3d) 496 (Sask. Q.B.)).

In the case of a Court appointed Receiver, the Court order will usually provide that no steps or proceedings may be taken against the Receiver, thereby preventing the landlord from exercising its right of distress unless it obtains leave of the court (*Holy Spirit Credit Union v. Golden Mile Toyota et al.* (1980), 113 D.L.R. (3d) 285(Man. C.A.)). A landlord may nevertheless distrain prior to receiving actual notice of the order appointing a Receiver over the tenant (*Bank of Montreal et al. v. Woodtown Developments Ltd.* (1979), 99 D.L.R. (3d) 739 (Ont. H.C.)).

Subject to the exceptions discussed below, the fact that the landlord needs leave of the Court is not meant to take away any substantive rights of the landlord. Accordingly, if the Receiver is able to pay the rent arrears and tenders payment in that regard, the landlord will not be granted leave to distrain, as the landlord will have been made whole. On the other hand, if the arrears are not tendered, leave will likely

be granted. Leave will likely not be granted if the value of the assets exceeds the debt owed to the landlord, in which case the court may leave control of the disposition of the assets (in whatever fashion) with the Receiver in order to protect the remaining equity in the assets for the secured creditor or the tenant (see *Royal Bank of Canada v. South Pacific Waterbeds Ltd.* (1984), 52 C.B.R. (N.S.) 71 (Alta. Q.B.)).

2. Purchase Money Security Interest

One limitation on a landlord's right to distrain is set out in s. 3(4) of the *Rent Distress Act*. That section deals with the priorities between the landlord and a secured creditor and provides that a landlord's right of distraint has priority over a security interest in the goods of the tenant other than a purchase money security interest in goods or proceeds that is perfected at the date of distress.

A "security interest" is defined in s. 3(1) of the *Rent Distress Act* as "an interest in personal property that secures payment or performance of an obligation."

A "purchase money security interest" is defined in s. 3(1) as:

- (a) a security interest taken in collateral to the extent that it secures payment of all or part of its purchase price and the credit charges for the purchase, and
- (b) a security interest taken in collateral by a person who gives value for the purpose of enabling the tenant to acquire rights in the collateral, to the extent that the value is applied to acquire the rights ...

but does not include

- (c) an interest of a lessor under a transaction of sale by and lease back to the seller ...

A Receiver will therefore have priority over the landlord to the extent that the Receiver is appointed pursuant to a general security agreement which grants a purchase money security interest to the secured party, so long as the collateral is not merely under a sale by way of lease back to the tenant.

3. Intercepting Ongoing Distraint Pursuant to the *Bankruptcy and Insolvency Act*

As noted previously, s. 73(4) of the *Bankruptcy & Insolvency Act* provides that any property under an ongoing distraint and any money realized therefrom which has not yet been paid to the landlord must be returned to the Trustee upon the bankruptcy order or assignment. As a result, a secured creditor which does not have a purchase money security interest may wish to petition the tenant into bankruptcy.

The reason for this is that s. 136 of the *Bankruptcy & Insolvency Act* provides that the scheme of distribution to creditors is subject to the rights of secured creditors. Specifically, s. 136(1)(f) provides for a preferred claim for certain amounts owed to the landlord, after the claims of secured creditors. In this way, a secured creditor, and therefore a Receiver appointed under that security, is able to reverse the priority of the landlord that may otherwise exist without a bankruptcy (*Re Black Bros. (1978) Ltd.* (1982), 41 C.B.R. (N.S.) 163 (B.C.S.C.); *Re Gasthof Schnitzel House Ltd. and Sanderson*, [1978] 2 W.W.R. 756 (B.C.S.C.); *Re Public's Own Market (Prince George) Ltd.* (1984), 54 C.B.R. (N.S.) 222 (B.C.S.C.)).

4. Termination versus Distraint

A landlord may only distraint during the term of the lease. A landlord may not terminate the lease and then distraint (*JB Jackson Ltd. v. Gestas* (1926), 2 D.L.R. 721 and *Clarkson Company Limited v. Consortium Group Limited* (1983), 45 C.B.R. 273).

If the landlord elects to distraint, the locks may not be changed because to do so is a repudiation of the lease (*Beaver Steel v. Skylark Ventures Ltd.* (1983), 47 B.C.L.R. 99 and *Coopers Lybrand v. Royal Bank of Canada* (1982) 5 W.W.R. 156).

If, however, the tenant consents to the locks being changed and the distress being maintained, this will not be a termination (*Cisakowski v. Feteke* (1985), 2 W.W.R. 691).

G. Right of the Receiver to Assign a Lease

As previously stated s. 146 of the *Bankruptcy & Insolvency Act* provides that the rights of landlords are determined by the laws of the province. Section 29 of the *Commercial Tenancy Act* sets out the provisions which govern a landlord once a bankruptcy has occurred. The key provisions in the context of a receivership are contained in s. 29(2) and (3), which allow a bankruptcy Trustee (of a tenant) to occupy the leased premises and to assign the lease to a third party.

A Receiver may be able to use these sections to assist in assigning the lease to a third party when the cooperation of the landlord is not forthcoming. The immediate problem is of course the fact that it is the right of the Trustee to assign the lease, not that of the Receiver. The Receiver cannot force the Trustee to assign the lease to a third party of the Receiver's choice (*Re Hip Pocket Limited* (1977), 24 C.B.R. (N.S.) 249 (Ont. S.C.); *Re Royal Centre Incorporated* (1979), 27 C.B.R. (N.S.) 81 (Ont. S.C.)).

As a result, it should be possible for the Receiver and the Trustee to agree, to the benefit of both the secured creditor and the bankruptcy estate, on the use of s. 29(2) and (3) of the *Commercial Tenancy Act*. The mutual benefit, to the detriment of the landlord, is that the assignment of the lease may be made

without paying the arrears owing to the landlord under the lease (*Re Smitty's Place Ltd.* (1984), 53 B.C.L.R. 330 (S.C.)).

It must be remembered however that there must be some benefit to the bankruptcy estate in order for the Trustee to justify the use of these provisions. In the case of a dual appointment of the same person as a Receiver under the general security agreement and a Trustee under the *Bankruptcy & Insolvency Act*, this is a concern in light of the possible conflict of interest that may be created.

The right of the Trustee to invoke s. 29(2) and (3) will be subject to the lease not having already been terminated at the time of the bankruptcy. If the lease contains a provision automatically terminating the lease upon a bankruptcy, the lease will no longer be an asset available for the Trustee to assign under s. 29(3). If, however, the lease merely provides the landlord with an option to terminate the lease, that option is in and of itself not sufficient to prevent the Trustee from using s. 29(3) (*Raymond, Chabot et al v. Hyatt Construction Corp.* (1983), 47 C.B.R. (N.S.) 179 (B.C.S.C.)). Again, when advising the Landlord, the terms of the lease must be carefully reviewed.

V. Landlord's Remedies in Dealing with Tenant in Default Outside of Insolvency

A. Background

Most landlords in a commercial context have faced the unfortunate experience of having a tenant who is either continuously in default of its obligations under the lease or suddenly abandoning the premises altogether prior to the expiration of the term of the lease. Unless one has a crystal ball, it is likely not possible to predict with any certainty which tenants in the future may pose problems. When a crisis situation arises with a tenant, it can be of great assistance to the landlord in protecting its interests if he can move quickly. While most of the remedies available to a landlord require legal action of one kind or another, a landlord must assess his remedies in a business context.

A review of the lease is a basic starting point. The lease defines the parties intention on how the lease agreement is to be governed. Most commercial leases have provisions that set out the rights and remedies reserved to a landlord facing a defaulting tenant. It is not unusual for such leases to spell out clearly what events constitute an event of default (i.e. non payment of rent or taxes, abandonment) and what notices have to be supplied to the tenant by the landlord regarding default. In many cases a landlord will want to move in immediately and consider distraint or termination of the lease upon a default. It is critical that all procedural steps defined under the lease are followed by a landlord in pressing his remedy of choice. Service must properly be effected on the tenant in the manner prescribed. It is also important to serve any guarantors, indemnitors or subtenants so as to preserve the landlord's rights against those parties.

In British Columbia, there is no specific statutory authority permitting a landlord to re-enter premises for non-payment of rent or for breach of covenant (Williams and Rhodes (*supra*) at p.498). If the lease does not specifically authorize re-entry, a landlord must obtain a Court Order to re-enter the premises upon default (*Lease Default Remedies and Lease Notices, Annotated Lease Precedents, C.L.E. of B.C., 1998, p. 18A-2*).

A landlord must also assess whether there has been a surrender of the lease. If the lease has been surrendered, both the lease and the rent owing are also gone. This is the case regardless of whether the tenant remains liable for breaches of covenants committed prior to surrender (Williams and Rhodes (*supra*) at p. 12-7).

When advising the landlord, an important question to ask at the outset is what does the tenant have in the way of assets, both on the lease premises or otherwise, to provide recovery to the landlord. Another issue to consider is what other creditors of the tenant are lurking about. Conducting basic searches regarding the debtor's affairs is a cheap and efficient manner to get at least a bit of "intelligence" on the tenant's affairs. An on-line computer registry system for the Personal Property Registry system is a good starting point.

If distraint is the landlord's first remedy of choice due to assets on the premises that may have value, a Personal Property Registry search may aid the landlord in assessing whether the tenant has sufficient interest in the assets to warrant distress. Under section 4(3) of the *Rent Distress Act*, a landlord's right of distress does not have priority over a perfected purchase money interest ("PMSI"). The difficulty is that a Personal Property Registry search will not reveal whether a security interest registered over goods is a PMSI or not. To ascertain whether a security interest is in fact a PMSI requires further investigation in accordance with the definitions and requirements of the *Personal Property Security Act* (the "PPSA") (*Lease Default Remedies and Lease Notices (supra)*, p. 18A-2).

B. Remedies

Outside of insolvency proceedings, the rights of a landlord who wishes to pursue a tenant for breach of the lease are set out in *Highway Properties Ltd. v. Kelly Douglas & Co. Ltd.* (1971), 71 D.C.R. (3d) 710 (S.C.C.). In that case, the Court set out four mutually exclusive options for the landlord upon the default of the tenant, as follows:

1. Retain the Lease

The landlord may retain the lease and insist on the tenant's performance of the terms of the lease, including if necessary, through a claim for ongoing rent and damages on the grounds that the lease is still in force.

If the landlord elects to retain the lease and require the tenant to comply with its terms, the Landlord will be entitled to sue for rent only as and when it becomes owing. The landlord cannot sue for prospective damages.

It is likely at law that there is no duty to mitigate on the part of a landlord who has chosen to retain the lease and sue for rent (*Transco Mills Ltd. v. Percan Enterprises Ltd.* (1993), 76 B.C.L.R. (2d) 129). Despite this, a landlord is wise to attempt to mitigate and keep track of its efforts in so doing.

2. Re-Let the Premises to the Tenant's Account

The landlord may advise the tenant that the premises will be re-let to the tenant's account and enter into possession on those grounds. Where a landlord chooses to retain the lease and re-let it to another tenant, then there is a duty to mitigate (*Grouse Mechanical Co. v. Griffith* (1990), 14 R.P.R. (2d) 233 (B.C.S.C.)).

3. Terminate the Lease and Sue for Rent Accrued Due

The landlord may terminate the lease and retain the right to sue for rent accrued due and for damages to the date of termination for previous breaches of the lease. This remedy is superfluous, as a landlord that wishes to sue after the termination of the lease should always at least reserve its rights to sue for prospective damages, as set out in the next option.

4. Terminate the Lease and Notify the Tenant of a Claim for Prospective Damages

The landlord may terminate the lease and notify the tenant that damages will be sought for any arrears and for prospective damages based upon present value of the unpaid future rent for the unexpired period of the lease less the actual rental value for that period.

As stated, if a landlord elects to terminate the lease, it must avoid taking steps to affirm the lease such as accepting current rent after the notice of termination. At law this can be construed as a waiver of the termination (*Foreshore Projects Ltd. v. Warner Shelter Corp.* (1983), 49 B.C.L.R. 26 (Co. Ct.); *Delilah's Restaurants Ltd. v. 8-788 Holdings Ltd.* (1994), 39 R.P.R. (2d) 161 (B.C.C.A.)).

If a landlord seeks to terminate the lease and claim damages for the unexpired balance of the term, notice of this must be made in a clear and unequivocal fashion. The mutually exclusive nature of the Highway Properties options means that if a landlord fails to clearly notify a tenant of their election it may be barred from clarifying its choice or making a re-election at a later date (*Langley Crossing Shopping Centre Inc. v. North-West Produce Ltd.* (February 9, 2000) CA02525 1 (B.C.C.A.)). In the lower court decision in this matter the chambers judge ruled that it was not necessary to give notice of a claim for prospective loss before or contemporaneously with the termination of the lease (*Langley Crossing Shopping Centre Inc. v. North-West Produce Ltd.* (1998), 20 R.P.R (3d) 112 (B.C.S.C.)). Although the Court of Appeal found it unnecessary to rule on this issue, Esson J.A. did note that the authorities for this proposition derived from the situation where the tenant abandoned the lease before the landlord had a chance to give proper notice. It is risky for a landlord to assume that notice of which election of remedy the landlord is seeking can be delivered at a date beyond termination. A important practice point is to identify the remedy being sought and then advising the Tenant of the election in a clear and precise manner.

Where a landlord opts to terminate a lease, it has a duty to mitigate its losses. A landlord and any agents it retains to re-let the premises should keep a record of all efforts made to lease the premises. As well, if a landlord has out-of-pocket expenses for repairs or tenant inducements for the premises, such expenses can be claimed as part of the damages against the tenant (*West Edmonton Mall Ltd. v. McDonald's Restaurants of Canada Ltd.* (1995), 144 A.R 331, [1994] 2 W.W.R. 230, aff'd at 50 R.P.R. (2d) 1, [1996] 3 W.W.R 191 (Alta. Q.B.)).

As stated, the above options are mutually exclusive and usually irrevocable. For instance, if the landlord elects the first remedy and the landlord affirms the lease agreement, he cannot later terminate it and claim damages (*238709 B.C. Limited v. McCallum Equity Corp.* (22 May 1986), Vernon Registry (Yale Co. Ct)). Further, if the landlord decides to terminate the lease, he cannot later attempt to revive it.

C. Avoiding Unintentional Terminations

If the landlord elects to keep the lease alive it must avoid any actions that are viewed as terminating the lease. One example of this is changing the locks on a distraint without the tenant's consent or otherwise demonstrating an intent to keep the lease in force (*Cisakowski v. Feteke*, [1985] 2 W.W.R. 691 (Alta Q.B.); *Beaver Steel Inc. v. Skylark Ventures Ltd.* (1983), 47 B.C.L.R. 99 (S.C.); but see *Langley Crossing (supra)*).

An unintentional termination may also result from a landlord leasing the premises to another party as this is inconsistent with the tenant's right to exclusive possession. If the election to keep the lease alive and

re-let the premises to a new tenant, this election must be clearly stated and notice given to the tenant. If a new lease is to be entered into a landlord should first properly terminate the original lease and given the tenant notice of the same. In such a scenario, a landlord can look to the old tenant for any deficiency between the rent paid by the new tenant compared to that which could have been paid by the former tenant (see *International Aviation Terminals v. Flying Fresh Air Freight (supra)*). The landlord's acceptance of the keys to the premises from the tenant is not enough to justify the finding that the landlord treated the lease as at an end (*Sierra Pacific Holdings Ltd. v. Natterjack Animation Co.* (1999) 25 R.P.R. (3d) 1 (B.C.S.C.); *Marathon Realty Co. v. Pogon Professional Services* (1994) 36 R.P.R. (2d) 264)).

Further, if the landlord decides to terminate the tenant's lease and re-let the premises while claiming rent for the unexpired portion of the tenant's lease it is not enough to issue a writ and inform the former tenant that the premises will be re-let. To avoid confusion the landlord should clearly indicate that they are seeking damages for losing the benefit of the lease over its unexpired term including unpaid rent (*Wing Lee Holdings Ltd. v. Starboard Dungaree Ltd.* [1996] 83 B.C.A.C. 132, 16 R.P.R. (3d) 223).

D. Procedure for Obtaining Possession Under *Commercial Tenancy Act*

Sections 18 through 21 of the *Commercial Tenancy Act* provide the summary procedure for a landlord to obtain a Court-ordered Writ of Possession to remove a tenant who, on written demand from the landlord, wrongfully refuses to leave the premises after the expiration of his lease or right of occupation (s. 18, *Commercial Tenancy Act*).

There are three conditions precedent to granting such relief to a landlord:

- (a) the lease or right of occupancy must be terminated by a notice to quit or notice under the lease;
- (b) a written demand to the tenant to deliver up the premises must be delivered after the first condition is met;
- (c) the tenant must wrongfully refuse to give up possession.

(*2733 4th Avenue Development Ltd. v. Xavier* (1981) 33 B.C.L.R. 397 (Co. Ct.))

The basis of the notice to must be proven to be valid grounds for termination. For instance, if a notice to quit is issued on the basis of non payment of rent, and rent is later determined not owing, in that instance,

no proper demand has been made and the landlord's application will fail (*Tomol Holdings Ltd. v. Pimiskern Architectural Services* (1979) 16 B.C.L.R. 193 (Co. Ct.)).

In an application under s. 21 of the *Commercial Tenancy Act*, it should be noted that the landlord is permitted to cross-examine the tenant on a viva voce basis during the Application (*Kelowna Pacific Railway Ltd. v. Jonathon Hall and Burco-West Leasing Ltd.*, unreported, February 25, 2009, Docket 81133, Kelowna). This can be an effective tool in solidifying the landlord's position that a Writ of Possession is warranted.

Section 25 of the *Commercial Tenancy Act* also provides a summary procedure for obtaining possession of premises based on a breach of a covenant by a tenant. If a landlord seeks to bring an end to the tenancy for such a breach and seeks an order for possession, it must elect from the start whether to pursue the matter under s. 18 or s. 25. The crucial difference between the two sections is that s. 18 requires a termination or an end to the lease on the part of the landlord by notice, before the landlord can proceed under s. 18. This procedural step to end the lease is not required for the landlord to apply under s. 25. An application under s. 25 presupposes that the tenancy has not been terminated (*Burlington Northern Railroad Co. v. Baseline Industries Ltd.* (1993) 85 B.C.L.R. (2d) 363 (B.C.C.A.)).

A hearing under s. 25 and s. 26 of the *Commercial Tenancy Act* is referred to as a "show cause" hearing. The tenant is issued a summons and given an opportunity to show cause why the premises should not be vacated. If the landlord is successful, an Order to vacate the premises is issued. A sheriff may use force to evict the tenant if the tenant refuses to leave (s. 26(4), *Commercial Tenancy Act*).