Court File No. C66626

COURT OF APPEAL FOR ONTARIO

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

MEDALLION CORPORATION, in its capacity as authorized agent for 280 RICHMOND STREET WEST LIMITED

Appellant

- and -

RSM CANADA LIMITED in its capacity as trustee in bankruptcy of CURRICULUM SERVICES CANADA/SERVICES DES PROGRAMMES D'ETUDES CANADA

Respondent

BOOK OF AUTHORITIES OF THE RESPONDENT

July 2, 2019

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Medallion Corporation as authorized
agents for 280 Richmond Street West
Limited

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TAB 1

2019 ONSC 1114
Ontario Superior Court of Justice

In the Matter of the Bankruptcy of Curriculum Services Canada

2019 CarswellOnt 2545, 2019 ONSC 1114, 302 A.C.W.S. (3d) 466, 68 C.B.R. (6th) 278

IN THE MATTER OF THE BANKRUPTCY OF Curriculum Services Canada/Services Des Programmes D'Etudes Canada of the City of Toronto in the Province of Ontario

V.R. Chiappetta J.

Heard: January 21, 2019
Judgment: February 15, 2019
Docket: 13-2360759

Counsel: Catherine Francis, for Appellant, Medallion Corporation as authorized agents for 280 Richmond Street West Limited
Alex Ilchenko, for Trustee, RSM Canada Limited

Subject: Insolvency; Property

Related Abridgment Classifications

Bankruptcy and insolvency
X Priorities of claims
X.4 Claims by landlord
X.4.e Accelerated rent
X.4.e.i Entitlement to claim

Headnote

Bankruptcy and insolvency --- Priorities of claims — Claims by landlord — Accelerated rent — Entitlement to claim
Landlord filed Proof of Claim with Trustee claiming: preferred claim for three months' accelerated rent in amount of $100,558.59 under s. 136(1)(f) of Bankruptcy and Insolvency Act — Landlord appealed Notice of Disallowance — Appeal dismissed — Registrar in caselaw concluded that law in Ontario was as Trustee advocated on appeal: that after disclaimer there was no right in Ontario for landlord to claim damages on unexpired portion of lease.

Table of Authorities

Cases considered by *V.R. Chiappetta J.*:

Crystalline Investments Ltd. v. Domgroup Ltd. (2004), 2004 SCC 3, 2004 CarswellOnt 219, 2004 CarswellOnt 220, 46 C.B.R. (4th) 35, 234 D.L.R. (4th) 513, 316 N.R. 1, 16 R.P.R. (4th) 1, 184 O.A.C. 33, 43 B.L.R. (3d) 1, [2004] 1 S.C.R. 60, 70 O.R. (3d) 254 (note), 2004 CSC 3, 70 O.R. (3d) 254 (S.C.C.) — considered

Cummer-Yonge Investments Ltd. v. Fagot (1965), [1965] 2 O.R. 152, 8 C.B.R. (N.S.) 62, 50 D.L.R. (2d) 25, 1965 CarswellOnt 40 (Ont. H.C.) — considered

Cummer-Yonge Investments Ltd. v. Fagot (1965), 8 C.B.R. (N.S.) 62 (note), 50 D.L.R. (2d) 30 (note), [1965] 2 O.R. 157 (note) (Ont. C.A.) — referred to

Highway Properties Ltd. v. Kelly, Douglas & Co. (1971), [1971] S.C.R. 562, [1972] 2 W.W.R. 28, 17 D.L.R. (3d) 710, 1971 CarswellBC 239, 1971 CarswellBC 274 (S.C.C.) — considered

Hindcastle Ltd. v. Barbara Attenborough Associates Ltd. (1996), [1997] A.C. 70, [1996] 2 W.L.R. 262, [1996] 1 All E.R. 737 (U.K. H.L.) — considered

Linens 'N Things Canada Corp., Re (2009), 2009 CarswellOnt 2849, 53 C.B.R. (5th) 232 (Ont. S.C.J.) — considered

Mussens Ltd., Re (1933), 14 C.B.R. 479, [1933] O.W.N. 459, 1933 CarswellOnt 52 (Ont. S.C.) — considered

Stacey v. Hill (1901), [1901] 1 Q.B. 660 (Eng. C.A.) — considered

Statutes considered:

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

Generally — referred to

s. 30(1)(k) — considered

s. 65.2 [en. 1992, c. 27, s. 30] — considered

s. 65.2(3) [en. 1992, c. 27, s. 30] — considered

s. 135(3) — considered

s. 136 — considered

s. 136(1)(f) — considered

s. 136(3) — considered

s. 146 — considered

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

Generally — referred to

s. 38 — considered

s. 39 — considered

Landlord's Rights on Bankruptcy Act, R.S.A. 2000, c. L-5

s. 4 — referred to

APPEAL by landlord from Notice of Disallowance.

***V.R. Chiappetta J.*:**

Background

1 Pursuant to a Lease dated May 26, 2017 (the "Lease"), Curriculum Services Canada/Services Des Programmes D'Etudes Canada (the "Tenant" or "Curriculum") rented the sixth floor of 150 John Street West, Toronto, Ontario (the "Premises") from Medallion Corporation. Medallion Corporation is the authorized agent for 280 Richmond Street West Limited (the "Landlord"). Curriculum went bankrupt in March 2018. The Landlord brought this claim in April 2018 under s. 136 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (the "BIA") for three months' accelerated rent and the unexpired portion of the term of the Lease.

2 The Lease was for 8,322 square feet of space at the Premises for a term of ten years and six months, commencing on July 1, 2017 and expiring on December 31, 2027, with basic rent payable as follows:

(i) Months 1-42: $21.50 per square foot per annum;

(ii) Months 43-78: $23.50 per square foot per annum; and

(iii) Months 79-126: $25.50 per square foot per annum.

3 In addition to basic rent, the Tenant was required to pay additional rent as defined in the Lease. Section 16 of the Lease deals with defaults and remedies. Section 16.1 reads in relevant part:

If any of the following shall occur:

...

(f) Tenant, any assignee or a subtenant of all or substantially all of the Premises makes an assignment for the benefit of creditors or becomes bankrupt or insolvent or takes the benefit of any statute for bankrupt or insolvent debtors or makes any proposal, assignment, arrangement or compromise with its creditors or Tenant sells all or substantially all of its personal property at the Premises other than in the ordinary course of business (and other than in connection with a Transfer requiring Landlord's consent and approved in writing by Landlord), or steps are taken or action or proceedings commenced by any person for the dissolution, winding up or other termination of Tenant's existence or liquidation of its assets (collectively called a "*Bankruptcy*");

(g) a trustee, receiver, receiver-manager, manager, agent or other like person shall be appointed in respect of the assets or business of Tenant or any other occupant of the Premises;

...

then, without prejudice to and in addition to any other rights or remedies to which Landlord is entitled hereunder or at law, the then current and the next three (3) months' Rent shall be forthwith due and payable and Landlord shall have the following rights and remedies, all of which are cumulative and not alternative, namely:

(i) to terminate this Lease in respect of the whole or any part of the Premises by written notice to Tenant (it being understood that actual possession shall not be required to effect a termination of this Lease and that written notice, alone shall be sufficient); if this Lease is terminated in respect of part of the Premises, this Lease shall be deemed to be amended by the appropriate amendments, and proportionate adjustments in respect of Rent and any other appropriate adjustments shall be made;

...

(v) to obtain damages from Tenant including, without limitation, if this Lease is terminated by Landlord, all deficiencies between all amounts which would have been payable by Tenant for what would have been the balance of the Term, but for such termination, and all net amounts actually received by Landlord for such period of time;

(vi) to suspend or cease to supply any utilities, services, heating, ventilating, air conditioning and humidity control to the Premises, all without liability of Landlord for any damages, including indirect or consequential damages, caused thereby;

(vii) to obtain the Termination Payment from Tenant;

(viii) if this Lease is terminated due to the default of Tenant, or if it is disclaimed, repudiated or terminated in any insolvency proceedings related to Tenant (collectively "Termination"), to obtain payment from Tenant of the value of all tenant inducements which were received by Tenant pursuant to the terms of this Lease, the agreement to enter into this Lease or otherwise, including, without limitation, the amount equal to the value of any leasehold improvement allowance, tenant inducement payment, rent free periods, lease takeover, Leasehold Improvements or any other work for Tenant's benefit completed at Landlord's cost or any moving allowance, which value shall be multiplied by a fraction, the numerator of which shall be the number of months from the date of Termination to the date which would have been the natural expiry of this Lease but for such Termination, and the denominator of which shall be the total number of months of the Term as originally agreed upon.

4 On March 28, 2018, Curriculum filed an Assignment for the General Benefit of Creditors (the "Assignment"). Amy Coupal, an officer and director of Curriculum, swore a Statement of Affairs dated March 28, 2018 in which she swore that Curriculum had assets totaling $1,903,563.87 and liabilities totaling $5,605,253.28, resulting in a deficiency of $3,701,689.41. The single largest liability shown on the Statement of Affairs was Curriculum's liability to the Landlord, which was reflected as follows:

(i) Unsecured claim: $3,986,725.25; and

(ii) Preferred claim: $100,558.59.

5 On March 29, 2018, pursuant to the Assignment, Curriculum became bankrupt. RSM Canada Inc. was appointed as Trustee.

6 On April 20, 2018, the Landlord filed a Proof of Claim with the Trustee claiming:

(i) A preferred claim for three months' accelerated rent in the amount of $100,558.59 under s. 136(1)(f) of the BIA, which reads as follows:

> **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:
>
> . . .
>
> (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;

and;

(iii) An unsecured claim in the amount of $4,028,11.23 for the unexpired portion of the term of the Lease under s. 136(3) of the BIA, which reads as follows:

> **136(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.

7 On April 23, 2018, the Trustee issued a Notice of Disclaimer of the Lease pursuant to s. 30(1)(k) of the *BIA*, effective that date.

8 On September 19, 2018, pursuant to s. 135(3) of the *BIA*, the Trustee disallowed part of the Landlord's preferred claim for $100,558.59, on the basis that the Trustee had realized only $24,571 from the assets on the leased premises (i.e. the office equipment). The Trustee therefore admitted the Landlord's preferred claim for $24,571 under s. 136(1)(f) of the *BIA*, in addition to the occupation rent that the Trustee paid to the Landlord.

9 The Trustee disallowed the entirety of the Landlord's claim for the unexpired portion of the term of the Lease in the amount of $4,028,111.23. The Trustee reasoned then, and now argues on appeal, that s. 146 of the *BIA* and ss. 38 and 39 of the *Commercial Tenancies Act*, R.S.O. 1990, c. L.7 (the "*CTA*") operate to deem the disclaimer of a lease in Ontario by a trustee in bankruptcy as a consensual surrender of the lease by the tenant to the landlord, and consequently no claim for damages can be founded on the cessation of obligations under the lease.

10 Following the Disclaimer, the Landlord successfully mitigated its damages for the unexpired portion of the term of the Lease by obtaining another tenant. The Landlord has therefore amended its claim for the unexpired portion of the

term to seek recovery of the tenant inducements provided to Curriculum under the terms of the Lease. These inducements were leasehold improvements provided by the Landlord under the Lease, costing $45,280 and free rent for a six-month period, worth a total of $175,225.28. The Landlord also seeks the balance of its claim for accelerated rent.

11 The Landlord appeals the Notice of Disallowance. It argues that there is no legal principle under which the Landlord should be disentitled from filing a proof of claim for its damages for the unexpired term of the Lease. It argues that these are contractual damages, and should be treated equally with any contractual damages potentially suffered by any of Curriculum's other creditors.

12 For reasons that follow, I disagree. There is long-established legal precedent that bars the claims made by the Landlord. The appeal is therefore dismissed.

Analysis

13 The Landlord's appeal requires the court to consider whether it remains the law in Ontario that the disclaimer of a lease by a trustee in bankruptcy prevents a landlord from claiming unsecured damages.

14 Pursuant to s. 136(3) of the *BIA*, a creditor whose rights are restricted by s. 136 is entitled to rank as an unsecured creditor for the balance of any claim due to him. Pursuant to s. 146 of the *BIA*, subject to priority 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. In Ontario, unlike in other provinces like Alberta, the statute that governs a landlord's rights on the bankruptcy of a tenant (the *CTA*) is silent as to whether a landlord can pursue an unsecured claim for its damages over and above its preferred claim (ss. 38 and 39 of the *CTA*; *Landlord's Rights on Bankruptcy Act*, R.S.A. 2000, c. L-5, s. 4).

15 The issue of whether there is a damage remedy for landlords in Ontario beyond s. 38 of the *CTA* and s. 136 of the *BIA* was most recently considered by a Registrar in *Linens N Things Canada Corp., Re* (2009), 53 C.B.R. (5th) 232 (Ont. S.C.J.). Relying on *Mussens Ltd., Re*, [1933] O.W.N. 459, 14 C.B.R. 479 (Ont. S.C.), the Registrar concluded that the law in Ontario is as the Trustee advocates on this appeal: that after a disclaimer there is no right in Ontario for a landlord to claim damages on the unexpired portion of the lease.

16 In *Linens 'N Things*, the Landlord of the bankrupt *Linens 'N Things* appealed the bankruptcy trustee's disallowance of amounts it claimed under the lease, including the costs of building the structure expressly for the *Linens 'N Things*, tenant allowance and leasing commission. The Landlord went "to great lengths at the hearing to characterize its disallowed claim as one for damages for breach of the contract contained in the lease." It relied on the Supreme Court of Canada's decision in *Highway Properties Ltd. v. Kelly, Douglas & Co.* [1971] S.C.R. 562 (S.C.C.) for the proposition that a lease of real property is both a lease and a contract. Based on this, it argued that it should have recourse not only to its rights as a landlord, but to contractual damages for breach of the lease contract: *Linens 'N Things* at paras. 12-13.

17 The Registrar distinguished *Highway Properties* on one very important fact: that case did not involve any insolvency. In the context of an insolvency, s.146 of the *BIA* and ss. 38 and 39 of the *CTA* apply. The Registrar stated that through these enactments "both the Dominion and Provincial Parliaments have spoken in determining that a trustee in bankruptcy may surrender or disclaim a lease. The effect of such is as if the parties had consensually ended 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 a lease": *Linens 'N Things* at paras. 16-18.

18 In coming to this conclusion, the Registrar relied on *Mussens Ltd.*. In this 1933 case, Rose C.J.H.C. dismissed a landlord's claim for damages for breach of covenant to pay future rent in its tenant's bankruptcy proceedings. His Honour interpreted the predecessor to s. 39 of the *CTA* as giving the bankrupt tenant a statutory right to breach the lease without liability:

> [T]he statute means I think that whether the lessor is or is not willing the liquidator may surrender possession or disclaim the lease, and that if he does . . . the tenant in liquidation shall be in the same position as if the lease had

> been surrendered with the consent of the lessor. Of course if the lease were surrendered with the consent of the lessor there could be no suggestion of any further liability on the part of the lessee to pay rent and no suggestion that by failing to pay rent the tenant was committing a breach of covenant and was rendering himself liable for liquidated or unliquidated damages.

19 Based on this decision, the Registrar in *Linens 'N Things* stated that "the *CTA* and its predecessors has been found for the better part of a century to have the effect of a consensual ending of the lease, and the cases recognize that this is a statutorily permitted breach for which there is no damage remedy, beyond the s. 38 *CTA* and s. 136 *BIA* preferred claim": para. 21.

20 The Landlord submits that the decision in *Linens 'N Things* is flawed as the Registrar failed to consider the Supreme Court's decision in *Crystalline Investments Ltd. v. Domgroup Ltd.*, 2004 SCC 3, [2004] 1 S.C.R. 60 (S.C.C.). It argues as follows. In finding against the landlord in *Linen 'N Things*, the Registrar relied heavily on *Mussens*. *Mussens* was adopted and applied in *Cummer-Yonge Investments Ltd. v. Fagot*, [1965] 2 O.R. 152 (Ont. H.C.) , aff'd [1965] 2 O.R. 157 (note) (Ont. C.A.). *Cummer-Yonge* was overruled by the Supreme Court in *Crystalline Investments Ltd.*. It follows then that *Mussens* was also overturned such that the rights of landlords survive the issuance of a disclaimer.

21 I disagree.

22 In *Cummer-Yonge*, a landlord sought unpaid past and future rents from the guarantors of a lease after the trustee of the bankrupt tenant had disclaimed it. The guarantee clause in the lease stated that the defendants guaranteed "the due performance by the Lessee of all its covenants in this lease . . . " The plaintiff landlord argued that a disclaimer did not have the legal effect of a surrender, such that the guarantor's liability survived the bankrupt tenant's disclaimer (p. 155):

> It was his submission that while a surrender operates to determine a lease and to preclude any subsequent accrual of rent, the trustee's disclaimer divested only himself of the rights and obligations under the lease, and had the effect in law of revesting these rights and obligations in the bankrupt tenant, the person from whom they originally came. While conceding that these obligations would be unenforceable against the tenant because of the provisions of the Bankruptcy Act, counsel argued that since the bankrupt's theoretical liability continued, the liability of the guarantors continued as well. [Emphasis added.]

23 To reject this suggested distinction between a surrender and a disclaimer, the defendants cited *Mussens* (p. 155):

> In answer to this suggested distinction between a surrender and a disclaimer, counsel for the defendants relied upon the case of *Re Mussens Ltd., Petrie Ltd.'s Claim*, [1933] O.W.N. 459, 14 C.B.R. 479, a decision of Rose, C.J.H.C. Although this case involved a liquidator under the Dominion Winding-Up Act, it turned on an interpretation of s. 38 of the Landlord and Tenant Act, which applies equally to a trustee in bankruptcy. There, the liquidator purported "to surrender possession or disclaim" the lease, and the lessor alleged that, while the liquidator was no longer liable for rent under the lease, the tenant in liquidation was in breach of its covenant to pay rent and was liable in damages for this breach. In rejecting this contention, the learned Chief Justice stated (at pp. 460-1):
>
> > By his letter of June 21st, 1932, confirming an earlier letter, the liquidator exercised his right "to surrender possession or disclaim" the lease, and when he had exercised that right the obligation of the tenant, the insolvent company, to pay rent was at an end. It did not require a statute to confer upon the liquidator power to surrender possession or disclaim the lease with the consent of the lessor; the statute means that, whether the lessor is or is not willing, the liquidator may surrender possession or disclaim the lease, and that, if he does so surrender possession or disclaim the lease, the tenant in liquidation shall be in the same position as if the lease had been surrendered with the consent of the lessor. Of course, if the lease were surrendered with the consent of the lessor, there could be no suggestion of any further liability on the part of the lessee to pay rent and no suggestion that, by failing to pay rent, the tenant was committing a breach of covenant and was rendering himself liable for liquidated or unliquidated damages.

24 The Registrar noted that Rose C.J.H.C. did not distinguish between a surrender and a disclaimer in *Mussens*, and "the clear inference is that, in the opinion of the learned Chief Justice, the legal effect of each is the same": p. 156.

25 After considering the defendants' submissions on *Mussens*, the Registrar made his conclusions on a different basis (p. 156):

> Apart entirely from this decision, however, I am not persuaded that a disclaimer of a lease by a trustee in bankruptcy has the consequence contended for by counsel for the plaintiff in this action. Assuming, for purposes of argument, that his submission that the sole effect of the trustee's disclaimer is simply to divest him of his entire interest in the lease is correct, it nevertheless does not follow in law that that interest thereupon reverts to the bankrupt tenant. As indicated previously, whatever interest the tenant had in the lease prior to bankruptcy was, by the operation of s. 41(5) of the Bankruptcy Act, vested in the trustee upon the filing of the assignment. In my view, when the trustee subsequently disclaimed that interest, all the rights and obligations which he inherited from the bankrupt were wholly at an end.

26 The Registrar supported this analysis by examining the *BIA*, finding that "an examination of the Act yields no authority for [the plaintiff landlord's position]: p. 157. Ultimately, the Registrar found that upon the bankruptcy of the tenant, all of its rights and obligations passed to the trustee, such that there were no covenants in the lease which the tenant was required to perform, and the guarantee of the "due performance by the Lessee of all its covenants in this lease" therefore became inoperative.

27 *Cummer-Yonge*, therefore, stood for the proposition that the disclaimer of a lease in bankruptcy extinguishes the lease obligations of any guarantor. *Mussens* was referenced to the extent of the suggested distinction between a surrender and a disclaimer as advanced by the plaintiff. Apart from *Mussens* and accepting a difference for the purposes of argument, the Court remained unconvinced of the plaintiff landlord's position, relying on the *BIA*. Furthermore, the proposition that a bankruptcy trustee's disclaimer ended the obligations of the bankrupt tenant was not at issue in *Cummer-Yonge*. It was not disputed by the parties or considered by the Registrar.

28 *Crystalline Investments Ltd.* overturned *Cummer-Yonge*. The case considered the effect of a bankruptcy trustee's disclaimer of a lease from the perspective of an assignor of a lease, not a guarantor. The plaintiff landlords had leased premises to the defendant, who had assigned the leases to a wholly owned subsidiary which it subsequently sold, and which subsequently became insolvent. Under the leases, the landlords' consent was not required for the assignments. The insolvent assignee's trustee repudiated the leases under s. 65.2 of the *BIA* as part of a court-approved proposal. The landlords received payments equivalent to six months' rent under the leases pursuant to s. 65.2(3) of the *BIA*.

29 The question before the Supreme Court was whether the insolvent assignee's repudiation of the lease ended the obligations of the assignor. The Supreme Court held that s. 65.2 should be read narrowly. It held that the plain purposes of the section were to free the insolvent from its obligations under a commercial lease, to compensate the landlord, and to allow the insolvent to resume viable operations as best it could. Nothing in s. 65.2, or any part of the Act, protects third parties from the consequences of an insolvent's repudiation of a commercial lease.

30 The Court noted that this result is consistent with the concept of assignments in general. When a lease is assigned, the original tenant remains liable should the assignee not pay the rent. The bankruptcy of the assignee destroys the original tenant's right to require the assignee to discharge the obligations of the lease, and impairs the original tenant's right of indemnity against the assignee if the original tenant must discharge the obligations itself, but the assignee's bankruptcy has no effect on the original tenant's liability towards the lessor, which continues unaffected.

31 The Court dismissed the suggestion that the original tenant's right of indemnity against the insolvent assignee would frustrate the scheme of the *BIA*. The Court reasoned that the original tenant's claim would be dealt with according to the scheme of the Act, joining other unsecured creditors.

32 A unanimous Supreme Court therefore held that the disclaimer of the lease alone did not affect the obligations of the assignor.

33 Having decided the issue before it (the post-disclaimer obligations of an assignor), the Court went on to provide guidance on the post-disclaimer liability of a guarantor.

34 The Court questioned the correctness of the decision in *Cummer-Yonge* (para. 39):

> *Cummer-Yonge* has created uncertainty in leasing and bankruptcy. Not only have drafters of leases attempted to circumvent the holding in *Cummer-Yonge* by playing upon the primary and secondary obligation distinction, but courts have also performed what has been called "tortuous distinctions" in order to reimpose liability on guarantors. See J. W. Lem and S. T. Proniuk, "Goodbye '*Cummer-Yonge*': A Review of Modern Developments in the Law Relating to the Liability of Guarantors of Bankrupt Tenants" (1993), 1 D.R.P.L. 419, at p. 436.

35 The Court further noted that the English case *Stacey v. Hill*, [1901] 1 Q.B. 660 (Eng. C.A.), which had come to the same conclusion as and was applied in *Cummer-Yonge*, had been overruled by the House of Lords in *Hindcastle Ltd. v. Barbara Attenborough Associates Ltd.*, [1996] 1 All E.R. 737 (U.K. H.L.). In overruling it, Lord Nicholls stated that treating the guarantor and the assignor of a lease differently in the case of the current tenant's insolvency "would make no sort of legal or commercial sense": p. 754.

36 Ultimately, the Court in *Crystalline Investments Ltd.* held that, like *Stacey v. Hill*, *Cummer-Yonge* should be overruled. It concluded that "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": para. 42.

37 The Court stated, therefore, that there should be no distinction in the post-disclaimer liability of assignors and guarantors. Consistent with its holding on the liability of assignors, and contrary to the holding in *Cummer-Yonge*, the Court held that a disclaimer alone should not relieve a guarantor from its obligations. The comments of the Court were *obiter dicta* but, in my view, carry significant weight with respect to the issue of whether a guarantor's assurances survive a tenant's bankruptcy. They are not relevant, however, to the issue presented by this appeal.

38 Neither the *ratio decidendi* nor the *obiter dicta* of *Crystalline Investments Ltd.* address whether a landlord can claim unsecured damages in the bankruptcy proceedings of its tenant upon the disclaimer of a lease by the trustee in bankruptcy. The principle in *Mussens* remains the law on this issue in Ontario as correctly applied in *Linen 'N Things*.

Conclusion

39 The Appeal is therefore dismissed.

Appeal dismissed.

TAB 2

2010 SKQB 17
Saskatchewan Court of Queen's Bench

Royal Bank v. Insley

2010 CarswellSask 47, 2010 SKQB 17, 184 A.C.W.S. (3d) 303, 352 Sask. R. 56, 64 C.B.R. (5th) 105

IN BANKRUPTCY AND INSOLVENCY

IN THE MATTER OF THE BANKRUPTCY OF KRISTYN JOELLE INSLEY

ROYAL BANK OF CANADA (APPLICANT) AND KRISTYN JOELLE INSLEY (RESPONDENT)

Reg. Lian M. Schwann

Judgment: January 19, 2010
Docket: Bankruptcy 14313, Estate No. 23-883167

Counsel: Jim Kroczynski for Royal Bank of Canada
Jeff Lee for Dr. Insley
Mary Lou Senko for Canada Student Loans
Marla Adams for Trustee, Deloitte & Touche Inc,

Subject: Insolvency; Corporate and Commercial
Related Abridgment Classifications
Bankruptcy and insolvency
IX Proving claim
IX.1 Provable debts
IX.1.m Miscellaneous
Headnote
Bankruptcy and insolvency --- Proving claim — Provable debts — Miscellaneous
Expunging allowed claims — Debtor was discharged from bankruptcy subject to payment of $193,000 to trustee — Bank was major creditor, holding $193,000 as non-government student loan and $7,577 credit card debt — Other claims came to light which bank originally claimed had not been disclosed but later conceded had been filed — Bank brought application to expunge claims — Application dismissed — Trustee is required to examine every proof of claim under s. 135 of Bankruptcy and Insolvency Act — Application to expunge under s. 135(5) of Act is appeal against allowance — Bank made no argument that denial of claim was improper after it abandoned argument that claims not filed in timely manner — Section 135 of Act does not confer unqualified right to challenge proven claims, and should not be used as entry point to attack other processes or decisions by trustee.
Table of Authorities
Cases considered by *Reg. Lian M. Schwann*:
Business Development Bank of Canada v. Pinder Bueckert & Associates Inc. (2009), 2009 CarswellSask 776, 2009 SKQB 458 (Sask. Q.B.) — considered
Canadian Imperial Bank of Commerce v. 433616 Ontario Inc. (1993), 17 C.B.R. (3d) 160, 1993 CarswellOnt 193 (Ont. Gen. Div.) — referred to
EnerNorth Industries Inc., Re (2009), 2009 ONCA 536, 2009 CarswellOnt 3886, 55 C.B.R. (5th) 1, 96 O.R. (3d) 1, (sub nom. *EnerNorth Industries (Bankrupt), Re)* 254 O.A.C. 235 (Ont. C.A.) — considered
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Lamont Hi-Way Service Ltd. v. Bunning (2003), 2003 ABQB 297, 2003 CarswellAlta 903, 44 C.B.R. (4th) 91 (Alta. Master) — considered

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Marsuba Holdings Ltd., Re (1998), 8 C.B.R. (4th) 268, 1998 CarswellBC 2792 (B.C. Master) — followed

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Weihs, Re (2005), 2005 CarswellMan 173, 2005 MBQB 108, 12 C.B.R. (5th) 118, (sub nom. *Weihs (Bankrupt), Re)* 194 Man. R. (2d) 70 (Man. Q.B.) — considered

Statutes considered:

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

Generally — referred to

s. 37 — referred to

s. 135 — considered

s. 135(4) — considered

s. 135(5) — considered

s. 136 — referred to

s. 141 — considered

s. 178 — referred to

s. 178(1) — considered

s. 178(1)(g) — considered

s. 192(1)(n) — referred to

Canada Student Financial Assistance Act, S.C. 1994, c. 28

Generally — referred to

Canada Student Loans Act, R.S.C. 1985, c. S-23

Generally — referred to

APPLICATION by creditor bank to expunge claims.

***Reg. Lian M. Schwann*:**

1 The Royal Bank of Canada ("RBC"), the major creditor in Kristyn Insley's bankruptcy, applies to expunge or reduce the proofs of claim of 'CRA - Govt Programs (Non Tax) Acct Maint' and of 'Trustees of Saskatchewan Student Aid Fund' (the "impugned claims") pursuant to s. 135(5) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*"). The application is opposed by Kristyn Insley ("Insley"), Canada Student Loans ("CSL") and the trustee.

Facts

2 Insley assigned into bankruptcy on July 19, 2006. As her discharge was opposed by the RBC, a hearing ensued before me which culminated in my decision of October 26, 2007, reported at 2007 SKQB 383 (Sask. Q.B.) (the "decision").

Pursuant to that decision, Insley was granted her discharge from bankruptcy conditional upon consenting to judgment in favour of the trustee in the amount of $193,000.

3 The Statement of Affairs filed at the time of assignment listed in excess of $287,000 of unsecured debt of which $193,000 was owed to RBC for a 'non-government student loan'. RBC had additional claims of $7,577 on a credit card debt along with Royal Bank (government guaranteed) student loans of $7,458 and $7,641 respectively. She also reported a debt owed to 'National Student Loans' in the amount of $69,829.

4 The Claims Register submitted with the Trustee's Report in March 2007 reveals the following in relation to the impugned claims:

Unsecured Creditor	Amount of Claim	Amount filed	Admitted
National Student Loans	$69,829	$55,244	$55,244
Royal Bank Student Loans	$7,458	$7,180	$0.00
Royal Bank Student Loans	$7,641	$7,357	$0.00

5 A subsequent Claims Register was prepared in July 2007 for the discharge hearing depicting the following with regard to the claims in issue:

Unsecured Creditor	Amount of Claim	Amount filed	Admitted
Canada Revenue Agency (Account Maintenance Unit)	unknown	$62,588	$62,588
Royal Bank Student Loans	$7,458	$7,180	$0.00
Royal Bank Student Loans	$7,641	$7,357	$0.00

6 Another Claims Register was prepared in 2009 for dividend distribution purposes with the only meaningful change between this one and the previous one being the inclusion of the 'Trustees of Saskatchewan Student Aid Fund' with a claim filed and admitted in the amount of $7,167. The two RBC student loans continue to be shown on this document however they are now identified as no proof of claim having been filed.

7 The trustee and CSL explain the discrepancies in amounts and with names of creditors in the following way. The creditor initially described as 'National Student Loan' is Her Majesty the Queen in right of Canada as represented on collections by the 'CRA Account Maintenance Unit'. They filed an initial claim of $55,244 but later enlarged it to $62,588 when $7,344 was added from one of the Royal Bank student loans. Both Royal Bank student loans (as opposed to the non-government student loan of $193,000) were guaranteed by the two levels of government and on Insley's assignment, the RBC was paid out with $7,344 of debt assumed by Canada and the other debt of $7,167 assumed by the Trustees of the Saskatchewan Student Aid Fund.

8 In September 2009, following extensive correspondence with the trustee, the RBC expressly asked the trustee to disallow (expunge) the impugned claims. The trustee responded in writing as follows: "Please be advised that, Deloitte & Touche Inc., in its capacity as Trustee in Bankruptcy, in accordance with section 135(5) of the *BIA* hereby declines to interfere in this matter".

9 At the outset of this application counsel for the RBC conceded that proofs of claim for the impugned claims were in fact filed and disclosed by the trustee but sought to have them expunged on other grounds.

Position of the Parties

RBC

10 RBC advanced three grounds to expunge the impugned claims:

(a) the impugned claims were not filed prior to Insley's discharge or were not disclosed by the trustee at or prior to the discharge hearing;

(b) the impugned claims survive bankruptcy accordingly are required to be paid regardless of any condition imposed upon the bankrupt for discharge including the award of Judgment;

(c) the award of Judgment was not intended to benefit claims which survived bankruptcy or those which were not filed or disclosed prior to the discharge hearing.

11 The first ground - that the impugned claims were not filed prior to discharge or disclosed by the trustee - was conceded by counsel for RBC once it became aware of the updated Claims Register and the explanation provided by CSL. RBC proceeded to argue that, notwithstanding this concession, the legislative language in s. 135(5) stands on its own and presents to creditors an unqualified right to expunge admitted claims where 'the trustee declines to interfere.'

12 RBC contends that once the trustee opens the door by an express refusal to interfere with an allowed claim, the Court has the unconstrained discretion to expunge claims. They urge me to do so in these circumstances because the RBC would otherwise receive a much smaller dividend than expected and thereby suffer prejudice, and secondly because my earlier decision implicitly excluded 'government student loans' from sharing in the fruits of the consent judgment.

13 RBC points to the considerable time and expense expended in opposing Insley's discharge with the net result being a sizeable consent judgment the RBC believed was theirs and theirs alone. The RBC further argues that as the impugned claims survive bankruptcy discharge by virtue of s. 178 of the *BIA*, those creditors have expanded rights and are able to collect both now and in the future. The CSL and Saskatchewan Student Loans would not therefore suffer any prejudice if their claims were expunged, they argue.

14 Finally, RBC contends that the discharge decision specifically precluded student loan creditors from sharing the fruits of Insley's judgment. The fact this court failed to address sharing by other creditors, they argue, must be interpreted as judicial direction barring sharing of dividends.

Canada Student Loans

15 CSL characterizes RBC's position as an 'ironic' one. The RBC filed two government student loan claims (both slightly in excess of $7,000) which were subsequently fully redeemed by the two levels of government through government guarantees. In short, RBC has been made whole on the full value of those loans - which were clearly before the Court at the time of Insley's discharge hearing - but now advances the position that it would be unfair for the guarantors to share in dividend distribution.

16 Furthermore, even though the CSL debt survives discharge by operation of s. 178, CSL is entitled to share rateably on distribution of dividends as a function of legislation and there is no law to support the position advanced by RBC. Expunging these claims, particularly at this late stage of estate administration, would constitute a significant change to the law of rateable distribution and an indirect attempt to re-argue Insley's discharge application.

Insley

17 Counsel for Insley begins by pointing out that RBC presented no evidence that the impugned claims did not exist prior to Dr. Insley's discharge hearing or of the claims not otherwise being legitimate. To give effect to RBC's position, he argues, is inconsistent with the plain wording of s. 141 of the *BIA* which clearly provides that all claims -without distinction - are to be paid rateably. There is nothing in the *Act* or case authority to support RBC's proposition that s.178 survivable claims do not share in dividend distribution. Reliance is placed on the Manitoba cases of *Weihs, Re*, 2005 MBQB 108, 12 C.B.R. (5th) 118 (Man. Q.B.) and *Stoski Estate (Trustee of) v. Royal Bank*, 2009 MBQB 17, 51 C.B.R. (5th) 40 (Man. Q.B.).

18 Counsel for Insley also points out that RBC will suffer no prejudice simply because student loan creditors are included in the proposed distribution for the simple reason that such approach reflects the scheme of distribution in the *BIA* and is consistent with case authority. In fact, to the extent there is prejudice, it would be borne by Insley if the RBC prevails. Finally, Insley argues that RBC's application amounts to a collateral attack on the discharge decision. If RBC was dissatisfied with that decision, the proper recourse was to appeal.

Trustee

19 Until discharged, the trustee has an ongoing duty to examine and review all claims which are lodged and to admit for dividend, or disallow where appropriate. The rights of creditors with survivable debts do not impact on these duties.

20 The trustee emphatically maintains that both Canada and Saskatchewan student loan debts were disclosed in the trustee's reports. The Claims Register is not static; it can and often does change as the estate moves along such as where creditors amend their claim or where they are subsequently withdrawn. In any event, the trustee points out that the date for admittance of claims is the date of distribution, not the date of the bankrupt's discharge. In response to RBC's secondary argument, they submit that the scheme of distribution in s. 136 applies regardless of the rights of s. 178 creditors.

Issues

21 The issues raised in this application are the following:

(a) What is the test to be applied by a party seeking relief under s. 135(5)?

(b) Are creditors with a s. 178 'surviving' debt entitled to participate and share in distribution of estate dividends?

(c) Did this Court's decision exclude government student loan creditors from sharing in estate dividends?

(A) The Test Applied to Expunge a Claim under s. 135(5) of the BIA

22 Section 135 of the *BIA* sets out the provisions for admitting and disallowing claims with ss. 135(4) and (5) governing the procedures on appeal of disallowance and for expunging or reducing any proven claim. It provides:

> 135.(1) The trustee shall examine every proof of claim or proof of security and the grounds therefor and may require further evidence in support of the claim or security.
>
> (1.1) The trustee shall determine whether any contingent claim or unliquidated claim is a provable claim, and, if a provable claim, the trustee shall value it, and the claim is thereafter, subject to this section, deemed a proved claim to the amount of its valuation.
>
> (2) The trustee may disallow, in whole or in part,
>
> (a) any claim;
>
> (b) any right to a priority under the applicable order of priority set out in this Act; or
>
> (c) any security.
>
> (3) Where the trustee makes a determination under subsection (1.1) or, pursuant to subsection (2), disallows, in whole or in part, any claim, any right to a priority or any security, the trustee shall forthwith provide, in the prescribed manner, to the person whose claim was subject to a determination under subsection (1.1) or whose claim, right to a priority or security was disallowed under subsection (2), a notice in the prescribed form setting out the reasons for the determination or disallowance.

(4) A determination under subsection (1.1) or a disallowance referred to in subsection (2) is final and conclusive unless, within a thirty day period after the service of the notice referred to in subsection (3) or such further time as the court may on application made within that period allow, the person to whom the notice was provided appeals from the trustee's decision to the court in accordance with the General Rules.

(5) The court may expunge or reduce a proof of claim or a proof of security on the application of a creditor or of the debtor if the trustee declines to interfere in the matter.

23 I find it helpful to begin by placing the whole of s. 135 in its proper context. This section imposes a statutory obligation on trustees to examine every proof of claim and every security for the purpose of determining if the claim or security, as the case may be, is valid. (Houlden and Morawetz, *Bankruptcy and Insolvency Law of Canada*, vol. 2, p. 5-180; *Canadian Imperial Bank of Commerce v. 433616 Ontario Inc.* (1993), 17 C.B.R. (3d) 160 (Ont. Gen. Div.)). If unsatisfied with the proof of claim or its supporting material, the trustee has not only a right but a corresponding duty to demand sufficient evidence to establish the validity of the claim. The trustee is given many tools under the *BIA* to fulfil this function including, where necessary, examination of parties and requiring production of documents. (Houlden and Morawetz, vol. 2, p. 5-181)

24 Following examination, the trustee either allows the claim or disallows it in whole or in part. A disallowance is final and conclusive unless appealed by the aggrieved creditor within the time permitted for doing so under s. 135(4). Section 135(5) is the flip side of a disallowance. Where a claim is admitted, s. 135(5) permits creditors or the bankrupt to apply to expunge or reduce the claim *if the trustee declines to interfere in the matter.*

25 An application to expunge pursuant to s. 135(5) has been characterized by the courts as an *appeal* against allowance. "In effect, the motion under section 135(5) is an appeal by a creditor or the debtor against an allowance by the trustee of a proof of claim or proof of security" (Houlden and Morawetz, vol. 2, p 5-205 (cites omitted); see also s. 192(1)(n) *BIA*).

26 In *Lamont Hi-Way Service Ltd. v. Bunning*, 2003 ABQB 297, 44 C.B.R. (4th) 91 (Alta. Master), para. 20 and 21, an application to expunge was described in this fashion:

> Section 135 creates a two sided token. If a trustee disallows a creditor's claim the creditor's only remedy is given by s.-s. (4).....If a trustee allows a claim other creditors and the bankrupt are adversely affected, so s.-s. (5) gives then a right to challenge the trustee's decision. There is little case law on s.-s. (5). Houlden & Morawetz, Bankruptcy & Insolvency Act (The 2002 Annotated) say that 'in effect' a motion under the s.-s. is an appeal by a creditor or the bankrupt of the trustee's disallowance of a claim, p. 551.

27 *Marsuba Holdings Ltd., Re* (1998), 8 C.B.R. (4th) 268 (B.C. Master) is another case where a s. 135(5) application was explored. At paragraphs 14 and 15 the learned Master examined the scope of the provision, commenting as follows on the applicable test.

> Counsel for the trustee says the applicant must show that the trustee acted unreasonably or improperly in accepting the proof of loss. Counsel would have it that so long as the trustee acted reasonably, the actual legitimacy of the claim is irrelevant. I respectfully disagree.
>
> Quite apart from questions of natural justice raised by this position....this construction of s. 135(5) is contrary to the tenor of s. 135 as a whole. The first four sub-sections deal with the procedure to be followed where a creditor appeals the *disallowance* of a claim by a trustee, and in such cases the appeal is decided simply on the basis of the legitimacy of the claim. There is no reason at all why different considerations should apply to appeals of a decision by the trustee to allow a claim. The only question should be whether the claim is indeed legitimate.
>
> [emphasis added]

28 No further elaboration was offered in *Marsuba* as to what constitutes a "legitimate" claim nor did the Court expand upon whether an appeal under this subsection proceeds on the record or is *de novo* in nature.

29 Regardless of the nature of a s. 135(5) appeal, the standard of review also remains an open issue unexplored in the referenced cases. This Court summarized the standard of review in the context of appeals from disallowance under s. 135(4) in the following manner: "Where the trustee's decision involves a question of law or the interpretation of a statute, the standard of review is correctness. On the other hand, where the matter under consideration is factual in nature or involves a discretionary element, the standard of review is reasonableness." (*Business Development Bank of Canada v. Pinder Bueckert & Associates Inc.*, 2009 SKQB 458 (Sask. Q.B.) at para. 24; see also *Eskasoni Fisheries Ltd., Re* (2000), 16 C.B.R. (4th) 173 (N.S. S.C.); *Lloyd's Non-Marine Underwriters v. J.J. Lacey Insurance Ltd.*, 2008 NLTD 9, 41 C.B.R. (5th) 137 (N.L. T.D.).)

30 The application before me is one to expunge two claims filed and admitted by the trustee. The onus rests with RBC to establish error on the part of the trustee, or in keeping with the approach taken in *Marsuba*, to establish these were not "legitimate" claims. In my view there is no need to explore the contours of what is or is not a legitimate claim, or other collateral issues arising on appeal (issues not argued by the parties) for the simple reason that RBC abandoned its initial argument that the impugned claims were not filed prior to Insley's discharge or disclosed by the trustee. In any event, no argument was advanced nor evidence presented concerning the underlying validity of the claims or their allowance. There is no suggestion whatsoever that the trustee improperly interpreted the law, ignored crucial facts, exercised its discretion improperly or acted outside of its authority in the course of exercising its function under s. 135. For all of these reasons, RBC's initial argument fails.

(B) Are Section 178 'Survivable Debts' Excluded from Sharing in Dividends?

31 RBC advances this line of argument through the vehicle of a s. 135(5) appeal, accordingly it must be considered within that context. As noted, the RBC does not challenge the validity of the claim but instead attempts to use s. 135(5) to disrupt the trustee's intended scheme of distribution of estate dividends. This argument is premised on the proposition that once the pre-condition to s. 135(5) exists, i.e. the trustee 'declines to interfere in the matter', a creditor possess an unqualified and unconstrained right to challenge the proposed distribution scheme in the face of an otherwise valid and allowed claim.

32 In *EnerNorth Industries Inc., Re*, 2009 ONCA 536, 55 C.B.R. (5th) 1 (Ont. C.A.) the Ontario Court of Appeal examined the scope of an application to expunge under s. 135(5) in the context of a debt arising from a valid and enforceable judgment. That court's observations concerning the purpose of s. 135(5) applications is summarized at para. 38:

> The appellants' argument that they have an 'unqualified right' to challenge Oakwell's proof of claim under section 135(5) is based on the unsupported theory that the *only* precondition to a creditor being entitled to a hearing under s. 135(5) is that the trustee must have declined to interfere in the matter. I do not read the provision in such a restricted manner. [emphasis in original]

33 Although *EnerNorth* dealt with an attack in bankruptcy proceedings of an otherwise valid and enforceable judgment, the decision, in my view, stands for the broad principle that s. 135(5) does not confer on creditors an unqualified right of challenge to proven claims. Something more is required apart from the trustee merely declining to interfere in the matter.

34 Neither, in my judgment, should s. 135(5) be used as an entry point to overturn or disrupt other processes or decisions made by the trustee in the course of estate administration. Section 135(5) constitutes a right of challenge limited to allowed or disallowed claims and should not be viewed more broadly than that. The right to challenge other decisions made by the trustee in the course of estate administration is available through s. 37 of the Act where an aggrieved person seeks court oversight over those decisions.

35 Even if I am wrong, there is nothing in the Act or in decided cases which supports RBC's position. Section 178(1) carves out a list of eight distinct types of debts which survive bankruptcy and which are not extinguished on the bankrupt's discharge. Debts or obligations in respect of a loan made under the *Canada Student Loans Act*, R.S.C. 1985, c. S-23, the *Canadian Student Financial Assistance Act*, S.S. 1994, c. 28, or an enactment of the province which provides student loans or guarantees of loans is a "survivable debt" if assignment is made within the prescribed time frames. (s. 178(1)(g))

36 Section 141 makes clear that *subject to any provision of the Act*, all claims proved in a bankruptcy are to be paid rateably. There is nothing in this section, s. 178 or s. 136 (which addresses priorities on distribution) precluding s. 178 surviving creditors from sharing in dividends or in any manner adjusts the concept of rateable distribution prescribed by s. 141. In fact, case law supports the opposite position. Houlden and Morawetz make the following observation at vol. 3, p. 6-230:

> The claims listed in s. 178(1) are properly provable in bankruptcy. Proofs of claim may be filed for them and the creditor can receive a dividend on them: *Trusts & Guarantee Co. v. Brenner* (1932), 13 C.B.R. 518; affirmed in part 15 C.B.R. 112 (S.C.C.); *B. (S.M.A.) v. H. (J.N.)* (1993), 23 C.B.R. (3d) 81, 87 B.C.L.R. (2d) 241, [1994] 4 W.W.R. 281, affirmed (1994) 31 C.B.R. (3d) 302.
>
> [emphasis added]

37 The decisions in *Weihs, Re* (para. 7) and *Stoski Estate* (para. 25) confirm this approach.

38 In the absence of clear legislative direction, or case authority interpreting the effect of s. 178 claims otherwise, I conclude that Insley's government student loan creditors are entitled to share in the dividends intended to be dispersed by the trustee in accordance with s. 136 of the *BIA*. It follows that this basis to expunge these claims also fails.

(c) Did the decision in Insley, Re exclude government student loan creditors from sharing dividends in the bankruptcy estate?

39 RBC argues that my failure to squarely address sharing of estate assets with Insley's government student loan creditors was intended to exclude them from distribution of estate dividends.

40 The mere fact the present line of argument was not addressed in my decision was simply because it was not put in issue at the time of the discharge hearing. The *Act* speaks for itself in relation to the scheme of distribution and in the event of ambiguity or misunderstanding concerning the sharing in dividend distribution, this decision serves to resolve those questions.

Conclusion

41 RBC's application to expunge the claims of the CRA - Govt Programs (Non Tax) and the Trustees of Saskatchewan Student Aid Fund is dismissed. CSL shall have costs fixed at $500 payable from the estate.

Application dismissed.

TAB 3

2006 CarswellOnt 3933
Ontario Superior Court of Justice

Harding v. Fraser

2006 CarswellOnt 3933, 23 M.P.L.R. (4th) 288, 81 O.R. (3d) 708

Maria Harding (Applicant) and John Peter Fraser (Respondent)

John Peter Fraser (Applicant) and The Corporation of the Township of Shuniah (Respondent)

Pierce J.

Heard: May 18, 2006
Judgment: June 1, 2006
Docket: Thunder Bay CV-06-0151, CV-06-0267

Counsel: Chantelle J. Bryson for Applicant, Maria Harding, Township of Shuniah
Francis J. Thatcher for Respondent, Applicant, John Peter Fraser

Subject: Public; Torts; Civil Practice and Procedure; Municipal

Related Abridgment Classifications

Municipal law
IV Council members
IV.8 Conflict of interest
IV.8.f Practice and procedure
Municipal law
X Attacks on by-laws and resolutions
X.1 Grounds
X.1.e Ultra vires
X.1.e.ii Beyond power of municipality
X.1.e.ii.D Miscellaneous

Headnote

Municipal law --- Council members — Conflict of interest — Practice and procedure
Township intended to hire full-time fire chief and by-law enforcement officer — Township's part-time chief was candidate for new position — Township's administrative officer noticed councillor was mentioned as part of team of professionals working for chief's corporation — Officer concluded councillor was in serious conflict of interest with respect to anticipated hiring and had been in conflict of interest concerning other interactions in past — Council passed resolution to apply to courts for determination of whether councillor had violated by-laws by discussing and voting on matters involving chief while having undeclared pecuniary interest — Township reeve brought application for declaration of conflict of interest and removal of councillor from position — Councillor brought application for order quashing resolution — Application granted — Resolution was ultra vires authority of township and application was to be stayed — Council had no standing to initiate application under municipal legislation — Reeve could apply for declaration of conflict of interest in personal capacity — But council had no authority to reimburse reeve for legal expenses when such fees were incurred outside exercise of office — Such reimbursement would constitute improper use of municipal funds — Township overlooked existing authority to request judicial inquiry into allegations regarding councillor's misconduct.
Municipal law --- Attacks on by-laws and resolutions — Grounds — Ultra vires — Beyond power of municipality — Miscellaneous
Township intended to hire full-time fire chief and by-law enforcement officer — Township's part-time chief was candidate for new position — Township's administrative officer noticed councillor was mentioned as part of team of professionals

working for chief's corporation — Officer concluded councillor was in serious conflict of interest with respect to anticipated hiring and had been in conflict of interest concerning other interactions in past — Council passed resolution to apply to courts for determination of whether councillor had violated by-laws by discussing and voting on matters involving chief while having undeclared pecuniary interest — Township reeve brought application for declaration of conflict of interest and removal of councillor from position — Councillor brought application for order quashing resolution — Application granted — Resolution was ultra vires authority of township and application was to be stayed — Council had no standing to initiate application under municipal legislation — Reeve could apply for declaration of conflict of interest in personal capacity — But council had no authority to reimburse reeve for legal expenses when such fees were incurred outside exercise of office — Such reimbursement would constitute improper use of municipal funds — Township overlooked existing authority to request judicial inquiry into allegations regarding councillor's misconduct.

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s. 273(1) — referred to

s. 273(2) "by-law — — referred to

s. 273(5) — referred to

s. 274(1)(a) — referred to

s. 444 — considered

s. 444(c) — considered

Municipal Conflict of Interest Act, R.S.O. 1990, c. M.50

Generally — referred to

s. 1 "elector" — referred to

s. 9 — considered

s. 10 — considered

s. 10(2) — referred to

APPLICATION for order quashing resolution passed by council.

***Pierce J.*:**

Introduction

1 Mr. Fraser, a township councillor, asks the court to quash a resolution authorizing payment of the reeve's legal fees in her suit against him on behalf of the township council. He also seeks a stay of Reeve Harding's application to find him in breach of the *Municipal Conflict of Interest Act*. Finally, he moves for orders prohibiting the township's solicitors from acting for the township so long as he is on council, and from acting as solicitors of record in this litigation.

The Facts

2 The Township of Shuniah intended to hire a full-time fire chief and bylaw enforcement officer. The township's part-time fire chief, whom I will refer to as the fire chief, was a candidate for the position. In reviewing the fire chief's information, Shuniah's chief administrative officer, Mr. Collingwood, noticed that township councillor, John Fraser, was mentioned as part of the "team of professionals" working for the fire chief's corporation.

3 Mr. Collingwood, concluded that Councillor Fraser was in "a serious conflict of interest" with respect to the anticipated hiring of a full-time fire chief; he also concluded that Fraser had been in a conflict of interest concerning other interactions between the part-time fire chief, his corporation, and the township.

4 The township passed a bylaw several years ago requiring ethical behaviour from its councillors. The bylaw authorizes the chief administrative officer to advise the council of allegations of unethical conduct by councillors; it also empowers him to make inquiries regarding unethical conduct and report to council.

5 Before consulting Mr. Fraser, Mr. Collingwood tabled a report with council, advising that Councillor Fraser was involved in the business operated by the fire chief. Council had previously purchased an emergency plan from the fire chief's business. It was Collingwood's view that Fraser had not declared his pecuniary interest in this contract. Mr. Fraser met with Mr. Collingwood and expressed shock at the allegations in the report.

6 The day after the report was tabled, a special meeting of council was convened to discuss hiring a full-time fire chief. Councillor Fraser did not attend this meeting, indicating that he intended to obtain a legal opinion concerning the allegations against him.

7 Subsequently, Mr. Fraser queried Mr. Collingwood as to the propriety of disclosing to third parties confidential township information obtained *in camera*. Collingwood sought a legal opinion on the question from the township's solicitors, Buset and Partners.

8 Meanwhile, the investigation into conflict allegations continued. The chief administrative officer reviewed past council minutes to determine Councillor Fraser's participation in issues involving the fire chief or his company. Mr. Collingwood identified the minutes that he felt raised concern. These he placed before council at a special meeting called February 9, 2006. Later that month, an elector made inquiries of Mr. Collingwood concerning Councillor Fraser's potential conflict of interest in matters involving the fire chief. This elector was informed that minutes of council disclose Fraser voted in the past on issues involving the fire chief and the purchase of capital equipment. At his request, the elector was given copies of these minutes.

9 On February 27, 2006, Collingwood tabled a full report as to his findings concerning possible conflict of interest on Mr. Fraser's part. Mr. Fraser did not attend that meeting.

10 That report identified the meetings of council that might give rise to possible conflict, but acknowledged the investigation was incomplete. Collingwood recommended Councillor Fraser be asked certain questions, including declarations of pecuniary interest involving the fire chief and his business. Armed with this additional information, he would make a further report to council. In due course, council authorized him to do so.

11 Having taken legal advice, Councillor Fraser advised Mr. Collingwood that he was not in a conflict of interest. The township's legal counsel were asked to investigate the website that Fraser created for the fire-chief's business.

12 Mr. Fraser answered the questions authorized by council and Mr. Collingwood reported at an *in camera* session on March 9, 2006, which Mr. Fraser attended. Council then voted to apply to the courts for a determination of whether Councillor Fraser had violated the *Municipal Conflict of Interest Act* by discussing and voting on matters involving the fire chief and his company while having a direct or indirect pecuniary interest which was not declared.

13 Shuniah's ethics bylaw authorizes council to investigate allegations of unethical behaviour by councillors. It also provides an opportunity for the councillor who is being criticized to appear before council and/or submit a brief before council makes any decision. While Mr. Fraser answered questions put to him by council, he did not file a brief. He disputes that he had the opportunity to defend himself against the allegations before the township decided on March 9, 2006 to put this matter before the courts.

14 In the absence of Councillor Fraser, Shuniah council passed resolution #1138/06 authorizing an application pursuant to the *Municipal Conflict of Interest Act* which states:

> Whereas concerns have been raised by a number of electors as it relates to a possible contravention of the *Municipal Conflict of Interest Act* by Councillor Fraser;
>
> And whereas Councillor Fraser has expressed complete support for the concept of enforcing ethical conduct by Councillors;
>
> And whereas the Council of the Township of Shuniah has an interest in preserving the integrity of its processes in an open and transparent manner;
>
> Therefore be it resolved that Council shall;
>
> 1. Adopt the report and its attachments as Schedule "A" to this Resolution;
>
> 2. seek volunteers from Council to make application to the court pursuant to the *Municipal Conflict of Interest Act*;

3. authorize the Township to cover the costs associated with such an application;

4. confirm that the Township's insurance will cover 90% of Councillor Fraser's legal fees in association with the above application (subject to the legal fees being taxed), provided that the court concludes that no contravention of the *Municipal Conflict of Interest Act* occurred; and

5. confirm that the Township will cover the remaining 10% of Councillor Fraser's legal fees relating to the above application (subject to the fees being taxed), provided the court concludes that no contravention of the *Municipal Conflict of Interest Act* has occurred.

The township did not pass a bylaw with respect to this application.

15 On March 10, 2006, Maria Harding, the reeve of the township, represented by the township's solicitors, began an application for a declaration that Fraser had contravened the *Municipal Conflict of Interest Act.* In that application, she seeks an order removing Councillor Fraser from office and prohibiting him from running for municipal office for seven years.

16 Mr. Fraser has countered with an application against the township. His application seeks an order quashing resolution 1138/06; and an order for removal of Buset and Partners as counsel for the township for so long as Mr. Fraser serves on council. In the reeve's action, he claims a stay of the application, pursuant to s. 106 of the *Courts of Justice Act*, and an order removing the Buset firm as counsel of record.

Should the Resolution be Quashed? Should the Application be Stayed?

17 Councillor Fraser contends that resolution 1138/06 should be quashed on the basis that it is *ultra vires* the powers of the municipality. He argues that a municipality has no standing to bring an application pursuant to the *Municipal Conflict of Interest Act.* He submits it should be stayed.

18 The township counters that its resolution flows from the bylaw regulating ethical conduct. That being so, the township says that Fraser is out of time to challenge the bylaw, given the 1 year limitation found in s. 273 (5) of the *Municipal Act, 2001.* Shuniah also submits that it is entitled to enforce bylaws under the authority of s. 444 of the *Act.*

19 Mr. Fraser does not seek to quash the bylaw dealing with ethical conduct. His argument is that the bylaw does not extend to the authorization of an application under the *Municipal Conflict of Interest Act.* The power of the court to quash a resolution of council is found in s. 273(1) and (2) of the *Municipal Act, 2001.*

20 To evaluate these arguments, it is necessary to look at the statutory provisions and the bylaw.

21 The full text of the bylaw is set out in the Appendix to these reasons. The bylaw gives Council authority to investigate complaints or inquiries and to initiate an examination of unethical conduct of a council member. Paragraph 4.07 of the bylaw concludes with the powers of Council upon determining that its code of ethics has been breached:

> Where the Township Council determines the conduct referred to it does breach the Code of Ethics, the complainant shall be so advised in writing and the Council may
>
> (a) instruct the Council Member to divest himself/herself of the outside interest or transfer it to a trust;
>
> (b) take disciplinary action in the form of:
>
> (i) public statement outlining Council's position
>
> (ii) removal of appointments to standing committees

(c) take any other action Council deems appropriate.

22 Dealing with the application by the reeve to find Mr. Fraser in conflict, s. 9 of the *Municipal Conflict of Interest Act* permits an *elector*, within 6 weeks of learning that a member of council has breached the Act's provisions for conflict of interest, to apply to a judge to determine the matter. If the judge determines a contravention of the Act has occurred, he may, pursuant to s.10:

(a) declare the member's seat vacant;

(b) disqualify that person from being a member for up to 7 years; or

(c) require restitution where personal gain has resulted from the conflict.

23 If he finds the conflict arose through inadvertence or an error in judgment, the judge can, by virtue of s 10(2), decline to impose penalties of forfeiture of office and future disqualification.

24 Critical to this argument is the definition of "elector," found in s. 1 of the *Act*. An "elector," for purposes of the *Municipal Conflict of Interest Act*, is..."a person entitled to vote at a municipal election in the municipality...." The reeve is an elector within the definition of the Act; however the Township of Shuniah is not.

25 Shuniah cites ss. 107(1) and 444 of the *Municipal Act, 2001* in support of its position.

26 Section 107 (1) states:

> Despite any provision of this or any other Act relating to the giving of grants or aid by a municipality, subject to section 106, a municipality may make grants, on such terms as to security and otherwise as the council considers appropriate, to any person, group or body, including a fund, within or outside the boundaries of the municipality for any purpose that council considers to be in the interests of the municipality.

The township contends this provision authorizes council to pay legal fees in the conflict of interest application. The resolution makes no provision for liability for costs, should they be awarded against the reeve.

27 Section 444 of the *Municipal Act, 2001* is titled "Right to enforce agreements, etc." and provides:

> Where a duty or liability is imposed by statute or agreement upon any person in favour of a municipality or in favour of some or all of the residents of a municipality, the municipality may enforce it and obtain such relief as could be obtained...
>
> (d) in a proceeding by the residents on their own behalf or on behalf of themselves and other residents.

28 The township argues that s.444 enlarges the reach of the corporation, and expands the ability of the municipality to pursue relief in other legislation. I do not accept this submission. The plain meaning of s. 444 supports it gives the municipality powers akin to rights of subrogation.

29 The recent trend in jurisprudence involving municipalities is to move away from the principle that municipal powers are closely circumscribed by their governing statute, and to interpret powers conferred on municipalities broadly. This approach defers to the decisions of locally elected officials. See *Croplife Canada v. Toronto (City)*, [2005] O.J. No. 1896 (Ont. C.A.).

30 However, that deferential approach cannot, in my view, extend to giving a council standing to do indirectly what the Legislature has not authorized it to do directly. Council has no standing to initiate an application under the *Municipal Conflict of Interest Act*.

31 The *Municipal Act, 2001*, is an Act of general application. The *Municipal Conflict of Interest Act* is a specialized statute and comprises a complete code dealing with conflicts of interest. Thus, conflict of interest legislation takes precedence over a general statute to the extent of inconsistencies under the principle of statutory interpretation: *generalia specialbus non derogant.* See *Sullivan and Driedger on the Construction of Statutes* (4th ed.) by Ruth Sullivan, Butterworths Canada, 2002. At p. 273, the author explains:

> When two provisions are in conflict and one of them deals specifically with the matter in question while the other is of more general application, the conflict may be avoided by applying the specific provision to the exclusion of the more general one. The specific prevails over the general; it does not matter which was enacted first.

32 The narrow issue is whether the reeve is a "straw woman" for purposes of the application to find Councillor Fraser in conflict. It is clear on the record that the council knew that it had no standing as a body to make an application under the *Municipal Conflict of Interest Act.* Thus, it sought a volunteer. The township overlooked that it had authority as a council to request a judicial inquiry into the allegations of a councillor's misconduct pursuant to s. 274 (a) of the *Municipal Act, 2001.*

33 The reeve's status as a volunteer is problematic. It is apparent on the record that the council did not believe an elector would come forward to incur the costs of an application to the court. By the terms of the *Municipal Conflict of Interest Act*, the reeve has no standing to apply on behalf of the council. Council has no standing.

34 The reeve can apply for a declaration of conflict of interest in her personal capacity. However, notwithstanding s. 107(1), council has no authority to reimburse the reeve for her legal expenses when they are incurred outside the exercise of her office. See *Santa v. Thunder Bay (City)*, [2003] O.J. No. 3091 (Ont. S.C.J.), par. 28, affirmed by the Court of Appeal for Ontario (Ont. C.A.). This would be an improper use of municipal funds. For this reason, I find resolution #1138/06 is *ultra vires* and shall be struck.

35 The next issue is the reeve's status as a representative of the council. Should the application be struck on the grounds that it is being illegally maintained, as the term is understood in law, by the Shuniah council?

36 The law of champerty and maintenance is of medieval origin at common law. It lives on in Ontario as a result of the *Champerty Act* passed by the Legislature in 1897. A history of champerty and maintenance is set out by O'Connor, A.C.J.O. in *McIntyre Estate v. Ontario (Attorney General)* (2002), 61 O.R. (3d) 257 (Ont. C.A.) at par. 18. The concepts are defined at par 26:

> ...Maintenance is directed against those who, for an improper motive, often described as wanton or officious intermeddling, become involved in disputes (litigation) of others in which the maintainer has no interest whatsoever and where the assistance he or she renders to one or the other parties is without justification or excuse. Champerty is an egregious form of maintenance in which there is the added element that the maintainer shares in the profits of the litigation. Importantly, without maintenance there can be no champerty....

37 In *McIntyre*, the court observes that conduct considered to be champertous has evolved over time, but the purpose of the prohibition is to protect the administration of justice from abuse. The modern authorities confirm that an improper motive as being determinative of a finding of maintenance. The *McIntyre* case, at par. 33 adopts the observations of Griffiths, J.A. in *Buday v. Locator of Missing Heirs Inc.* (1993), 16 O.R. (3d) 257 (Ont. C.A.), that champerty includes the encouragement of litigation that parties would not otherwise initiate.

38 In these circumstances, it is not necessary to decide whether the township has engaged in unlawful maintenance by its resolution to pay the reeve's legal expenses, as its resolution has been struck on other grounds.

39 While I am satisfied that the court has jurisdiction to protect its process by striking actions that are an abuse, (see *Operation 1 Inc. v. Phillips*, [2004] O.J. No. 5290 (Ont. S.C.J.), the facts of this case do not warrant such an order. The

reeve is a qualified elector as defined by the *Municipal Conflict of Interest Act*. Her office does not make her ineligible to bring such an application. There is no evidence that she does so in bad faith. The application for a stay on the grounds of maintenance is dismissed.

Should A Stay be Ordered on the Grounds that the Application Lacks Particulars?

40 Mr. Fraser submits that the application, as amended, continues to lack particularity, such that he does not know the case he is to meet. He also submits that as the *Municipal Conflict of Interest Act* is a penal statute, with sanctions including removal from elected office, the application should be strictly pleaded so that he knows the case to be met. He asks that the application be stayed on the grounds that it fails to identify the impugned conduct.

41 The rules of pleading in civil matters grant latitude in amending pleadings, such that the issues may be fully and fairly canvassed at trial. There is no evidence at this preliminary stage that Councillor Fraser has been prejudiced by lack of particulars in the application against him.

42 Ms. Harding disputes there is any lack of particularity, but offers to amend the application if ordered to do so.

43 I agree that the application should contain particulars in order that the issues on examination and at trial may be narrowed and costs saved. A focussed pleading will also reduce the delay in bringing the matter to trial.

44 Ms. Harding is ordered to amend her application to particularize discussions or votes that give rise to complaint; to identify Councillor Fraser's alleged pecuniary interest at relevant times; and to plead what relationship Mr. Fraser had at relevant times to Mr. Drainville or his company, giving rise to a pecuniary interest.

45 The motion for a stay on the grounds that the application lacks particularity is dismissed.

Should Counsel be Removed as Solicitors for the Township and for the Reeve?

46 The firm, Buset and Partners are general counsel for the Township of Shuniah. They also represent Ms Harding, reeve of the township, against fellow Shuniah councillor, Mr. Fraser, in the conflict of interest application.

47 The thrust of Mr. Fraser's argument is that the Buset firm has breached the duty of loyalty it owes him by virtue of his membership on Shuniah council. He also relies on s. 2.04 of the *Rules of Professional Conduct* of the Law Society of Upper Canada, for their persuasive value, acknowledging that they do not bind the court. However, he does not allege the firm is privy to confidential information which may be used against him.

48 The Buset firm challenges this contention. It contends that it acts for a quorum of council, representing the municipal corporation, and not for individual councillors. It says that its client is the council as a whole. Mr. Fraser has never retained them.

49 Alternatively, the Buset firm submits that the court has jurisdiction to remove it from the record in respect of the case before it, but not to terminate a retainer that is not before the court.

50 In my view, the Buset firm has construed its duty to Mr. Fraser too narrowly.

51 The starting point for this conclusion is *R. v. Neil*, [2002] 3 S.C.R. 631 (S.C.C.). The facts of that case involve a lawyer associated with a firm acting against a current client of the firm, though in an unrelated matter where no confidential information was disclosed. At par. 19 of the judgment, Mr. Justice Binnie highlighted the lawyer's duty to his client beyond not disclosing confidential information. This duty is a duty of loyalty. Loyalty includes the obligation to avoid conflicting interests; commitment to the client's cause; and the necessity to be candid with the client on matters relevant to the retainer.

52 The court in *Neil* cited with approval, at par. 26, the conclusions of Wilson J.A. in *Davey v. Woolley, Hames, Dale & Dingwall* [1982 CarswellOnt 844 (Ont. C.A.)]:

> The underlying premise...is that, human nature being what it is, the solicitor cannot give his exclusive, undivided attention to the interests of his client if he is torn between his client's interests and his own or his client's interests and those of another client to whom he owes the self-same duty of loyalty, dedication and good faith.

The Supreme Court concluded, at par. 29, that generally:

> a lawyer may not represent one client whose interests are directly adverse to the immediate interests of another current client — *even if the two mandates are unrelated* — unless both clients consent after receiving full disclosure (and preferably independent legal advice) and the lawyer reasonably believes that he or she is able to represent each client without adversely affecting the other.

53 Rule 2.04(4) of the Law Society of Upper Canada's *Rules of Professional Conduct* prohibits a lawyer who has acted for a client in a matter from later acting against that client or against persons involved in or associated with the client in that matter, whether:

> a) in the same matter;
>
> b) in any related matter; or
>
> c) except as provided by subrule 2.04(5), in any new matter if the lawyer has obtained relevant confidential information from the previous retainer unless the client or those involved in or associated with the client consent.

54 The *Rules of Professional Conduct* are not law, but do constitute an important statement of public policy, as was noted by Sopinka J. in *MacDonald Estate v. Martin*, [1990] 3 S.C.R. 1235 (S.C.C.).

55 In *GMP Securities Ltd. v. Stikeman Elliott LLP*, [2004] O.J. No. 3276 (Ont. S.C.J.), Madam Justice Hoy found a law firm owed a limited duty of loyalty to the client of an investment banker, for whom the law firm acted in a proposed transaction. In her supplementary reasons, Hoy J. observed:

> ...on the issue of whether the Firm also owed a duty of loyalty to Wheaton, I concluded that in the specific fact situation, a limited duty of loyalty was owed. I was influenced in this conclusion by the fact that an investment banker and its counsel are often in essence part of a team which includes the investment banker's client and its counsel, working together with the common objective of effecting the particular transaction the client company seeks to complete. In this case, the Firm was part of such a team. It provided advice with respect to the Proposed Transaction, and not just with respect to GMP's role as investment banker.

56 The Buset firm relies on *RSJ Holdings Inc. v. London (City)*, [2004] O.J. No. 1982 (Ont. S.C.J.). The *ratio decidendi* of that case dealt with the propriety of releasing confidential information obtained at an *in camera* meeting. In *obiter*, at par. 21, the court noted there is no property in a witness; it held that counsel for the developer had not acted improperly in seeking evidence from city councillors to use on the developer's application against the city. The court held,"The City Solicitor does not represent or speak for these individuals unless with their consent."

57 Apart from the issue that *obiter* is not binding on the court, there is an important distinction between independent counsel seeking information *from* members of city council in order to move against the city, and the city solicitor moving *against* one of the members of his client group that comprise council.

58 The obligation of loyalty to a client, or one associated with the client, is directed at not acting against the interests of that client. It is the adversarial position that is destructive of the solicitor-client relationship.

59 In the case at bar, the Buset firm maintains that its client is the quorum of councillors, not any individual. This may be true in a technical sense; however, this position necessarily places the firm in an adversarial relationship with one out of five councillors who make up the quorum.

60 The record reflects that Mr. Fraser, through the agency of the chief administrative officer, sought legal advice from council's solicitors in connection with this matter. Subsequently, the solicitors accepted a retainer from the reeve to act against Mr. Fraser, at the resolution of council.

61 Mr. Fraser may not have retained the Buset firm personally, but as a member of the Shuniah Township council, he was entitled to expect that the township solicitors would not act against him on township business. The reeve is also a member of that client group. By accepting her retainer to act against a fellow councillor, the solicitors have preferred the interests of one member of the client group over those of another, notwithstanding all councillors have been elected to serve the township.

62 Mr. Fraser is part of the Township council team. He is potentially a part of the quorum that makes up the council for whom the solicitors act. As such, he is intimately connected with the business of the township. The lawyer's duty of loyalty to the client extends to the members of the client group. In these circumstances, it is improper of the Buset firm to act against him.

63 The Buset firm submits that there is no jurisdiction to terminate a retainer that is not before the court. I agree with this submission. The retainer that is objected to is that of solicitor for the township. This relationship is unrelated to the litigation once the Buset firm is removed as counsel for the reeve in her suit against Mr. Fraser. However, the reeve's application *is* before the court. There will be an order removing the Buset firm as counsel of record for Maria Harding in the application against John Peter Fraser.

Costs

64 If the parties cannot agree on costs, they may obtain an appointment from the trial coordinator to argue same.

Application granted.

TAB 4

1962 CarswellQue 27
Supreme Court of Canada

Gingras automobile Ltée, Re

1962 CarswellQue 27, [1962] S.C.R. 676, 34 D.L.R. (2d) 751, 4 C.B.R. (N.S.) 123

In re Gingras Automobile Ltee; Les Produits de Caoutchouc Marquis v. Trottier

Taschereau, Fauteux, Abbott, Judson and Ritchie JJ.

Judgment: June 11, 1962

Proceedings: affirmed *Gingras Automobiles Ltée, Re* ((1961)), 1961 CarswellQue 37, 3 C.B.R. (N.S.) 55, [1961] Que. Q.B. 827, [1961] B.R. 827 ((Que. Q.B.))

Counsel: *Arcadius Denis, Q.C.*, for the appellant.
P. E. Blain and *J. P. Bergeron, Q.C.*, for the respondent.

Subject: Corporate and Commercial; Insolvency
Related Abridgment Classifications
Bankruptcy and insolvency
X Priorities of claims
X.4 Claims by landlord
X.4.b Specific claims
X.4.b.iii Cost of repairs

Headnote
Bankruptcy --- Priorities of Claims — Claims by landlord — Specific claims — Cost of repairs
Constitutional law — Conflict between provincial and Federal law as to priority of landlord's claim for rent in bankruptcy — Federal bankruptcy legislation prevails.
Landlord and tenant — Claim for arrears of rent and costs of repairs — Landlord not a secured creditor — Landlord only a preferred creditor for amount set forth in s. 95(1)(f) of the Bankruptcy Act — Unsecured creditor for any balance.
Secured creditor — Landlord not a secured creditor — Claim for rent only entitled to priority given by the Bankruptcy Act.
The debtor company had a valid lease at the time of bankruptcy under which there were arrears of rent for the three months prior to bankruptcy of $1,800. During the period that the debtor had occupied the leasehold, he had caused damages to the premises amounting to $1,398. At the date of bankruptcy there were goods on the premises of sufficient realizable value to pay the full amount of the landlord's claim. The landlord claimed to be a preferred creditor for the full amount owing of $3,198.
Held, the landlord was only a preferred creditor for arrears of rent for the three months preceding the bankruptcy and for the balance of his claim was only an ordinary creditor.
A claim of the landlord for arrears of rent was not a secured claim. He had no lien on the property seized but had to give it up to the trustee. The value of the property seized was used as a gauge to fix the amount for which the landlord was allowed a preferred claim; *dicta* of Gordon J.A. in *Re Radioland Ltd.; Canadian Credit Men's Trust Ass'n. v. Carman Block Ltd.*, 36 C.B.R. 158 at p. 162, 22 W.W.R. 180, 8 D.L.R. (2d) 647, 1957 Can. Abr. 43, approved.

By virtue of s. 105 of the Bankruptcy Act, the nature and extent of the landlord's claim for rent or damages, and any other rights he may have had arising out of the contract of lease were determined by the law of the province in which the leased premises were situated. But in the event of bankruptcy, the right of the landlord to be collocated and paid by preference and the extent of that preference were clearly provided for in s. 95. Such preference ranked sixth in order of priority and was limited to three months arrears of rent prior to the bankruptcy and to accelerated rent for a period not exceeding three months following the bankruptcy. Any amount payable by preference was limited to the amount realized from the property on the leased premises, and any payment on account of accelerated rent had to be credited against any amount due by the trustee for occupation rent. The landlord was only entitled to rank as an unsecured creditor for any balance to which he may have been entitled by provincial law.
The exclusive authority given to Parliament by s. 91(21) of the B.N.A. Act to deal with all matters coming within the domain of bankruptcy and insolvency enables Parliament to determine the relative priorities of creditors under a bankruptcy. To the extent that such priorities may be in conflict with provincial law, the Federal statute must prevail. The fact that a different preferred position is given by provincial law is overruled by the provisions of the Bankruptcy Act.
Annotation

This case is a most important one on the subject of bankruptcy and the relationship of landlord and tenant. The Supreme Court of Canada has stated the law on this matter with clarity and a great deal of confusion has been cleared up by the Gingras judgment.

There are certain important consequences of this decision. These are as follows:

(a) The extent of the preferred claim of the landlord is limited to three months' arrears of rent prior to the bankruptcy and to accelerated rent for a period of three months following the bankruptcy. It is now clear that cases such as *In re Clayton's Ltd.; Ex parte Liggett Co.*, [1933] O.R. 492, 14 C.B.R. 361, [1933] 2 D.L.R. 767, 3 Can. Abr. 903, which indicated that the landlord might be able to claim for a longer period if the lease so provided, have no application under the present Bankruptcy Act.

(b) The nature and extent of the landlord's claim for rent and damages is determined by provincial law. The extent of the preferred claim of the landlord is, as has been pointed out in the judgment, determined by the Bankruptcy Act, but in deciding the balance of the preferred claim, the law of the province is to be used. Thus, in the province of Ontario, there will be no claim for damages for the unexpired portion of the lease; *In re Mussens Ltd.; Ex parte Petrie Ltd.*, [1933] O.W.N. 459, 14 C.B.R. 479, 3 Can. Abr. 874; *In re Ted Weale Ltd.*, [1952] O.W.N. 360, 32 C.B.R. 206, [1952] 3 D.L.R. 839, 1 Abr. Con. (2nd) 515.

(c) It is now established without doubt that a landlord in spite of the definition of "secured creditor" is not a secured creditor but only a preferred creditor in bankruptcy proceedings.

Appeal from [1961] Que. Q.B. 827, 3 C.B.R. (N.S.) 55.

The judgment of the Court was delivered by *Abbott J.*:

1 Appellant is a creditor of Gingras Automobile Ltée, a bankrupt, and respondent is the trustee of the estate of the said bankrupt. At the date of the receiving order a valid lease existed between the debtor and appellant covering premises occupied by the debtor and with respect to which three months' arrears of rent amounting to $1,800 were outstanding. In addition, appellant was entitled to claim from the debtor a sum of $1,398.22 representing the cost of certain repairs for which the debtor was liable under the terms of its lease. Appellant's total claim against the debtor amounted therefore to $3,198.22, for which it filed a claim with respondent, alleging that it was entitled to be paid its entire claim by preference.

2 It is conceded that at the date of the receiving order sufficient moveable property was located upon the leased premises to secure payment of the full amount claimed.

3 The trustee allowed the amount claimed for arrears of rent as a preferred claim but disallowed the balance. On appeal to the Superior Court that decision was reversed and appellant held entitled to rank by preference for the whole amount of its claim. On appeal to the Court of Queen's Bench, that judgment was reversed and the decision of the trustee restored. The present appeal, by leave, is from that judgment.

4 The facts are not in dispute and the sole questions in issue on this appeal are ones of law. Under the provincial law, appellant was entitled to be paid a sum of $3,198.22 and payment of that claim was secured by privilege on the moveable property located on the leased premises: articles 1619 *et seq.* and 2005 of the Civil Code. That privilege consisted in the right to seize and sell such moveable property and to be paid by preference out of the proceeds; Faribault, Traité de Droit civil, t. 2, p. 112. In the event of competing claims, under the law of Quebec the landlord's privilege ranks eighth in order of preference: article 1994 of the Civil Code.

5 The legal question in issue here is, to what extent if any the provincial law has been abrogated by the provisions of the Bankruptcy Act, R.S.C. 1952, c. 14.

6 In 1949 all existing bankruptcy legislation was repealed and a new Bankruptcy Act enacted, 13 George VI, c. 7 now R.S.C. 1952, c. 14. The previously existing statute was completely re-cast and many important changes made including changes in the preferential right of the landlord.

7 The present Act, like its predecessor Acts, provides that subject to the Act all debts proved in bankruptcy shall be paid *pari passu*. To that rule of absolute equality, certain exceptions are made including those provided for by s. 95. The exclusive authority given to Parliament by s. 91(21) of the British North America Act to deal with all matters arising within the domain of bankruptcy and insolvency, enables Parliament to determine the relative priorities of creditors under a bankruptcy: *Royal Bank v. Larue*, [1928] A.C. 187, 8 C.B.R. 579, [1928] 1 W.W.R. 534, [1928] 1 D.L.R. 945, 11 Can. Abr. 197. To the extent that such priorities may be in conflict with provincial law, the Federal statute must prevail. In his argument before us Mr. Denis did not of course challenge that proposition. He contended, however, that s. 95 of the Act dealt merely with the order in which a landlord was entitled to be collocated by preference, and that the extent of that preference under the provincial law was preserved by s. 105. With deference I am unable to agree with that submission. The relevant portions of s. 95 and s. 105 are as follows:

> 95. (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: ...
>
> (*f*) the landlord for arrears of rent for a period of three months next preceding the bankruptcy and accelerated rent for a period not exceeding three months following the bankruptcy if entitled thereto 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; ...
>
> (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.
>
> 105. Except as to priority of ranking as provided by section 95, and subject to the provisions of subsection (4) of section 42, the rights of landlords shall be determined according to the laws of the province in which the leased premises are situate.

8 "Secured creditor" is defined by s. 2(*r*) as follows:

> 'secured creditor' means a person holding a mortgage, hypothec, pledge, charge, lien or privilege on or against the property of the debtor or any part thereof as security for a debt due or accruing due to him from the debtor, or a

person whose claim is based upon, or secured by, a negotiable instrument held as collateral security and upon which the debtor is only indirectly or secondarily liable; ...

9 The interpretation and effect of these sections were considered by the Court of Appeal of Saskatchewan in *Re Radioland Ltd.; Canadian Credit Men's Trust Association Ltd. v. Carman Block Ltd.*, 36 C.B.R. 158, 22 W.W.R. 180, 8 D.L.R. (2d) 647, 1957 Can. Abr. 43.

10 In my respectful opinion, Gordon J.A. accurately stated the law when he said at p. 162:

With every deference I do not think a landlord with a claim for arrears of rent falls within the definition of a 'secured creditor'. He has no lien on the property seized but must give it up to the trustee and file his claim in the usual way. He has no security to value within the provisions of ss. 87-92 of *The Bankruptcy Act*. Further, I do not think that any such inference should be drawn in the face of the explicit directions contained in s. 95 of the Act. So far as I can see the Act deprives the landlord of his right of lien and merely uses the value of the property seized as a gauge to fix the amount for which he is allowed a preferred claim but does not make him a 'secured creditor'.

11 Subject to priority of ranking under s. 95 (and to s. 42(4) which has no relevance here) in virtue of s. 105 the nature and extent of the landlord's claim for rent or damages and any other rights he may have arising out of the contract of lease are determined by the law of the province in which the leased premises are situated.

12 In my opinion however, in the event of bankruptcy, the right of the landlord to be collocated and paid by preference, and the extent of that preference, are clearly provided for in s. 95. Shortly stated, such preference ranks sixth in order of priority. It is limited to three months' arrears of rent prior to the bankruptcy and to accelerated rent for a period not exceeding three months following the bankruptcy. Any amount payable by preference is limited to the amount realized from property on the leased premises, and any payment on account of accelerated rent must be credited against any amount due by the trustee for occupation rent.

13 I am further of opinion that by the combined effect of ss. 95, 100 and 105 of the Act the landlord is entitled to rank only as an unsecured creditor for any balance to which he may be entitled under provincial law.

14 The appeal should be dismissed with costs.

TAB 5

1938 CarswellOnt 44
Ontario Supreme Court [High Court of Justice]

Sidley, Re

1938 CarswellOnt 44, [1938] 4 D.L.R. 693, [1938] O.R. 649, [1938] O.W.N. 414, [1938] O.J. No. 451, 71 C.C.C. 32

Re Sidley

McTague J.

Heard: October 14, 1938
Judgment: October 14, 1938

Counsel: *D. L. McCarthy, K.C.*, *R. H. Sankey, K.C.*, and *B. V. Elliott*, for the executors of the will of Maybelle Sidley, deceased, applicants.
A. G. Slaght, K.C., *W. B. Common, K.C.*, and *D. D. Carrick*, for the Chief Coroner of Ontario and the Attorney-General for Ontario, respondents.

Subject: Criminal; Civil Practice and Procedure
Related Abridgment Classifications
Judges and courts
VIII Coroners
VIII.4 Coroner's inquest
VIII.4.b Procedural requirements
VIII.4.b.v Miscellaneous
Headnote
Judges and Courts --- Coroners — Coroner's inquest — Procedural requirements
Judges and Courts --- Coroners — Coroner's inquest — Procedural requirements — View
Coroners — Inquests — Power of Attorney-General to initiate proceedings by way of inquest — Powers of coroner — Body out of the jurisdiction — Inquest super visum corporis — The Coroners Act, R.S.O. 1937, ch. 138.
Under The Coroners Act, R.S.O. 1937, ch. 138, the Attorney-General of Ontario has no power to initiate an inquest; under secs. 7 to 10 of the Act the Attorney-General has the power to reverse a decision of a coroner who has deemed it unnecessary to hold an inquest, but this jurisdiction of the Attorney-General is limited to a situation where the preliminary steps outlined in secs. 7 to 10 have been taken by the coroner. Hence, in the present case, the proceedings by way of inquest, which were ordered by the Attorney-General for Ontario without the preliminary steps having been taken by a coroner, were wholly void, and an order of prohibition was made against the Chief Coroner of the Province of Ontario.
At common law the proceedings in a coroner's court were required to be super visum corporis, and, if otherwise held, were of no force and effect; the presence of the body was always deemed necessary to the valid holding of an inquest. Although sec. 27 of The Coroners Act permits the coroner to dispense with a view of the body by the jurors, it in no way permits the coroner to dispense with the presence of the body. Sec. 27 implies that the body should be available for view by the jurors, although the actual view of it may be dispensed with, and the form of oath administered to the foreman of the coroner's jury bears out this construction.

A motion by the executors of the will of Maybelle Sidley, deceased, for an order prohibiting the Chief Coroner of the Province of Ontario from carrying on proceedings by way of an inquest upon the body of the said Maybelle Sidley.

The motion was heard by McTague J. in Chambers at Toronto.

McTague J. **(oral judgment delivered at the conclusion of the argument):**

1 Maybelle Sidley died on the morning of July 6th, 1938. Prior to her death, on the 4th of July her son William Sidley had communicated certain suspicions to the coroner, who as a result communicated with the physicians in attendance. It is quite evident that the doctors in charge of the case had determined, before death took place at all, that there should be an autopsy.

2 Shortly after her death her body was removed to the Banting Institute and there an autopsy was had in charge of three independent doctors, Drs. Robinson, Lougheed and Lynell, in the presence of the three physicians who had attended the deceased during her illness and in the presence of Dr. Howland as well. The coroner knew that the autopsy was being held because, according to his evidence and that of Dr. Robinson, he telephoned Dr. Robinson and discussed the matter with him just prior to the autopsy. After the autopsy had been completed on the same day, July 6th, Dr. Farquharson issued a certificate of death and the body was released for burial and on instructions of William Sidley was shipped to Racine, Wisconsin. Certain of the vital parts were retained by the doctors who performed the autopsy and certain were sent for analysis to Professor Rogers, for the purpose of ascertaining if there was any evidence that death was caused by poison or by the introduction of some foreign substance. These vital parts are still retained in the jurisdiction, but the body proper is now out of it.

3 From July 6th to July 15th nothing was done towards holding any inquest by the coroner. On July 15th the coroner was called into a conference at the office of the Attorney-General and received verbal instructions, subsequently confirmed in writing, to proceed with the inquest. Accordingly he issued his warrant for the body and his warrant for the inquest. Apparently the Attorney-General was of opinion that his action in ordering the inquest in these circumstances was justified by section 10(2) of The Coroners Act, R.S.O. 1937, ch. 138. The coroner's jury was summoned for the 26th day of July, 1938, and in spite of objection to the jurisdiction by counsel for the applicants, the jury was sworn and some evidence taken, and the inquest adjourned to August 2nd. In the interim, or rather on the 26th day of July itself, these proceedings were launched for prohibition.

4 The law that is applicable is the common law of England, superimposed upon which is the statute, and where the statute conflicts with the common law, the statute must prevail, and where the statute is silent on any matter, the common law should prevail.

5 At common law there is no question that the proceedings of a coroner's court were required to be *super visum corporis*, and if otherwise held had no force and effect. In that respect reference may be made to *Rex v. Ferrand* (1819), 3 B. & Ald. 260. Other cases indicating that the presence of the body was deemed necessary to the valid holding of an inquest are *Reg. v. Price* (1884), 12 Q.B.D. 247, and *Reg. v. Stephenson* (1884), 13 Q.B.D. 331.

6 The requirements of The Coroners Act, R.S.O. 1937, ch. 138, with respect to initiating an inquest are to be found mostly in sections 7 to 10. These provide in the main the scheme to be followed, and at least substantial compliance with them is a condition precedent to giving the coroner's court jurisdiction. When the attention of the coroner is called to suspicious circumstances in connection with the death of a person, the Chief Coroner or any coroner deputed by him shall issue his warrant to take possession of the body, shall view the body and shall investigate to determine whether an inquest shall be held or not. The language of the sections is mandatory throughout.

7 If after the inquiry the coroner deems an inquest necessary, he is required to transmit a statutory declaration setting forth the grounds upon which he deems an inquest necessary. The statutory declaration is to be transmitted to the Crown Attorney. If, on the other hand, after viewing the body the coroner deems it unnecessary to hold an inquest, he issues his

warrant to bury the body and transmits to the Crown Attorney a statutory declaration setting forth the grounds upon which he has issued his warrant to bury the body. Then the statute goes on to provide that even if the coroner has decided an inquest is unnecessary, and has transmitted his statutory declaration to that effect, in that case and in that case only the Crown Attorney or the Attorney-General may reverse the coroner's decision and order the inquest to proceed under the direction of that coroner or some other coroner.

8 It was argued strenuously that the Attorney-General, under section 10(2), has the power to initiate an inquest himself, regardless of whether the necessary preliminary steps have been taken by the coroner or not. I am unable to subscribe to that view.

9 There is nothing in the statutes empowering the Attorney-General to initiate an inquest. It can only be initiated by the coroner, and for the coroner's court to obtain jurisdiction certain conditions precedent must be complied with. If they are not, then the proceedings are wholly void: *Rex v. Haslewood*, [1926] 2 K.B. 468.

10 On the evidence on the motion, no pretence whatever was made by the coroner towards compliance with the statutory requirements. Therefore the whole proceeding was void ab initio, and the order for prohibition must go, limited of course, to the particular proceedings in question.

11 With reference to the effect of section 27 of the Act, it in no way permits the coroner to dispense with the presence of the body, but only with the view of the body by the jurors. The section implies that the body should be available for view by the jurors, although the actual view of it may be dispensed with. The form of oath administered to the foreman bears out this construction as well.

12 Before parting with the matter, I wish to emphasize that I have dealt with the whole question on a purely legal basis and that I impute no malicious or extraneous motives to anyone concerned. The applicants are entitled to their costs against the respondents.

Order of prohibition made with costs.

TAB 6

2009 CarswellOnt 2849
Ontario Superior Court of Justice

Linens N Things Canada Corp., Re

2009 CarswellOnt 2849, 177 A.C.W.S. (3d) 493, 53 C.B.R. (5th) 232

In the Matter of the Bankruptcy of Linens 'N Things Canada Corp., of the City of Toronto, in the Province of Ontario

Reg. S.W. Nettie

Heard: May 7, 2009
Judgment: May 22, 2009
Docket: Estate No. 31-1121528

Counsel: James Klein for Appellant
Aubrey Kauffman, Graham Phoenix for Respondent / Trustee

Subject: Insolvency; Property

Related Abridgment Classifications

Bankruptcy and insolvency
IX Proving claim
IX.2 Disallowance of claim
IX.2.c Appeal from disallowance
IX.2.c.i General principles
Real property
V Landlord and tenant
V.13 Surrender
V.13.a Express surrender
V.13.a.ii Miscellaneous

Headnote

Bankruptcy and insolvency --- Proving claim — Disallowance of claim — Appeal from disallowance — General principles

Bankrupt was big box retailer of household linens and other items — Bankrupt made assignment into bankruptcy — At time of assignment, creditor was landlord of one of bankrupt's locations — Trustee occupied demised premises for approximately two months — Trustee disclaimed lease of premises — Creditor, in its proof of claim, claimed to be due from bankrupt amount, in aggregate, of $3,886,933.15 — Trustee disallowed amount of $3,693,984 claimed on account of costs of building structure, amounts provided under lease as tenant's allowance, and leasing commission — Creditor appealed — Appeal dismissed — Trustee properly disallowed those portions of creditor's proof of claim — Creditor characterized its disallowed claim as one for damages for breach of contract contained in lease — Only breach complained of by creditor was of covenant to pay rent — Effect of s. 39 of Commercial Tenancies Act ("CTA") was that effect of surrender or disclaimer by trustee was as if there was consensual surrender of lease — In other words, it was at end, and no claim for damages could possibly be founded from such cessation of obligations under lease — Neither CTA nor Bankruptcy and Insolvency Act provided for type of claim advanced.

Real property --- Landlord and tenant — Surrender — Express surrender — Miscellaneous

Bankrupt was big box retailer of household linens and other items — Bankrupt made assignment into bankruptcy — At time of assignment, creditor was landlord of one of bankrupt's locations — Trustee occupied demised premises for approximately two months — Trustee disclaimed lease of premises — Creditor, in its proof of claim, claimed to be due from bankrupt amount, in aggregate, of $3,886,933.15 — Trustee disallowed amount of $3,693,984 claimed on account

of costs of building structure, amounts provided under lease as tenant's allowance, and leasing commission — Creditor appealed — Appeal dismissed — Trustee properly disallowed those portions of creditor's proof of claim — Creditor characterized its disallowed claim as one for damages for breach of contract contained in lease — Only breach complained of by creditor was of covenant to pay rent — Effect of s. 39 of Commercial Tenancies Act ("CTA") was that effect of surrender or disclaimer by trustee was as if there was consensual surrender of lease — In other words, it was at end, and no claim for damages could possibly be founded from such cessation of obligations under lease — Neither CTA nor Bankruptcy and Insolvency Act provided for type of claim advanced.

Table of Authorities

Cases considered by *Reg. S.W. Nettie*:

Highway Properties Ltd. v. Kelly, Douglas & Co. (1971), 1971 CarswellBC 274, [1972] 2 W.W.R. 28, 17 D.L.R. (3d) 710, 1971 CarswellBC 239, [1971] S.C.R. 562 (S.C.C.) — distinguished

Mussens Ltd., Re (1933), 1933 CarswellOnt 52, 14 C.B.R. 479, [1933] O.W.N. 459 (Ont. S.C.) — followed

Statutes considered:

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

Generally — referred to

s. 73(4) — referred to

s. 135 — pursuant to

s. 136 — considered

s. 146 — referred to

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

s. 38 — considered

s. 39 — considered

APPEAL by creditor from partial disallowance of its proof of claim by trustee of bankrupt's estate.

***Reg. S.W. Nettie*:**

1 This was the appeal by Roundhouse Centre Windsor Inc. (the "Appellant") of the partial disallowance of its December 29, 2008, proof of claim by RSM Richter Inc., trustee of the Estate of Linens' N Things Canada Corp. (the "Trustee"), on or about February 20, 2009.

2 The appeal is pursuant to the provisions of s. 135 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("BIA").

Facts

3 Linens' N Things Canada Corp. (the "Bankrupt") was a big box retailer of household linens and other items. On October 31, 2008, it made an assignment into bankruptcy, pursuant to the provisions of the BIA. At the time of the assignment, the Appellant was the landlord of the Bankrupt's location at the Round House Centre, in Windsor, Ontario.

4 The Trustee occupied the demised premises until December 29, 2008. The Trustee disclaimed the lease of the premises, by way of notice dated January 16, 2009, effective that date.

5 The demised premises included a standalone structure, various landlord improvements to it, and a significant tenant's allowance. The Appellant also incurred in letting the premises certain leasing costs. All of these were as provided for in the lease.

6 The Appellant, in its proof of claim, claimed to be due from the Bankrupt the amount, in the aggregate, of $3,886,933.15. This included a claim in the amount of $3,693,984.00 for build cost of the structure, tenant allowance and

leasing commission. The proof of claim also included certain other amounts which were disallowed by the Trustee, but which amounts have now been agreed to as properly disallowed.

7 What remains in dispute is the propriety of the Trustee's disallowance of the $3,693,984.00 on account of the costs of building the structure; amounts provided under the lease as tenant's allowance; and the commission paid on the lease itself by the Appellant.

Analysis

8 Section 146 BIA provides that, subject to the priority of claims set out in s. 136 BIA, and the provisions of s. 73(4) BIA, the rights of landlords shall be determined according to the laws of the Province in which the demised premises are situated. In the case at bar, that is Ontario.

9 The law in Ontario as to the rights of a landlord is codified, and has been for many, many, years, in what are now sections 38 and 39 of the *Commercial Tenancies Act*, R.S.O. 1990, chapter L.7 (the "CTA"). While s. 38 CTA provides for a preferential claim which mirrors s. 136 BIA, it is s. 39 CTA which is of most concern on this appeal. That section provides as follows:

> 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...

10 The Trustee's position, in partially disallowing the proof of claim, is that it has allowed the claims provided for in s. 38 CTA and s. 136 BIA, being that of three months arrears of rent, and three months of accelerated rent (the lease having contained an acceleration clause), together with certain other entitlements by way of charge backs, outstanding at the time of the bankruptcy, as being rent under the lease, or, alternatively, as being actually due and quantified under the lease at the time of bankruptcy. The Trustee's position is that it is not required to allow the claim for damages which the Appellant alleges it is suffering as a result of the disclaimer of the lease.

11 What is the claim of the Appellant? Put succinctly, it is that it built an expensive purpose built building for the Bankrupt, in what to others is seen as a less than valuable location at its Round House Centre, and bargained to recover its costs of so doing, together with some element of profit, over a 10 year and 6 month period of demise under the lease. It advances the same argument with respect to the tenant allowance and the leasing commissions which it paid in letting the building to the Bankrupt. The Appellant claims that it cannot lease this building to anyone else -for a variety of reasons. Even if I accept this to be true, and that the costs of erecting, improving and leasing this building are a complete loss, the question is whether or not that is a claim provable in bankruptcy.

12 The Appellant has gone to great lengths at the hearing to characterize its disallowed claim as one for damages for breach of the contract contained in the lease. It has taken great pains not to claim that any part of the disputed amount is rent, as it accepts that it can only claim rent in accordance with s. 136 BIA and s. 38 CTA.

13 The Appellant relies upon the decision of the Supreme Court of Canada in *Highway Properties Ltd. v. Kelly, Douglas & Co.*, [1971] S.C.R. 562 (S.C.C.) for the proposition that a lease of real property is both a lease and a contract. Flowing from this is the finding in that decision that a landlord may have recourse not only to its rights as a landlord, but for contractual damages for breach of the contract which is the lease.

14 While I take no issue with the decision in *Highway Properties*, and it is clearly binding, it is also entirely distinguishable on the facts. The circumstances of the breach of the lease in *Highway Properties* were that the tenant therein repudiated the lease. There was no insolvency, and no applicability of s. 146 BIA or anything like sections 38 and 39 CTA.

15 Counsel spent considerable time on argument about whether the lease, which provides in its language a reservation to the Appellant of all of the Appellant's rights at law and equity for breach of the lease, was sufficient to contract out

of the provisions of sections 38 and 39 CTA, and whether or not a lease could provide for payback to a landlord, as damages, of an amount representing the unrealized costs of erecting a building for a tenant, or the like.

16 While such an argument is appealing, both the Dominion and Provincial Parliaments have spoken in determining that a trustee in bankruptcy may surrender or disclaim a lease. The effect of such is as if the parties had consensually ended the lease.

17 As pointed out in *Mussens Ltd., Re*, 1933 CarswellOnt 52 (Ont. S.C.), at paragraph 6, the language used in the predecessor of s. 39 CTA, which is for our purposes identical to the present day language in s. 39 CTA, means "that whether the lessor is or is not willing the [trustee] may surrender possession or disclaim the lease, and that if he does so surrender possession or disclaim the lease the tenant...shall be in the same position as if the lease had been surrendered with the consent of the lessor. Of course if the lease were surrendered with the consent of the lessor there could be no suggestion of any further liability on the part of the lessee to pay rent and no suggestion that by failing to pay rent the tenant was committing a breach of covenant and was rendering himself liable for liquidated or unliquidated damages."

18 As in *Mussens* the only breach complained of by the Appellant is of the covenant to pay rent. I concur with the learned Chief Justice in *Mussens* that the effect of what is now s. 39 CTA is, whether in liquidation, as in *Mussens*, or in bankruptcy, 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. As Chief Justice Rose said in paragraph 7 of *Mussens*, a trustee under this section is given a statutory right to commit a breach of the insolvent's obligations under the lease.

19 According to the Chief Justice, the then corresponding provisions of the similar United Kingdom statute provided that any person injured by the exercise of the surrender or disclaimer of a lease under that statute shall be deemed a creditor to the extent of such injury. If s. 39 CTA contained such deeming language, then it seems to me that the Appellant would have the claim which it seeks to advance.

20 The Ontario statute did not provide for such a damage claim and deemed creditor status 76 years ago, and it does not do so today. The Dominion Parliament, in exercising its jurisdiction over bankruptcy law in the Dominion, has wholly left it up to the Provinces to determine the rights of lessors in these circumstances, and the Provincial Parliament has not seen fit to provide for the type of damage claim advanced by the Appellant. One can imagine that this is so because the vast majority of landlords are either amply compensated by a reduced but preferred claim for unpaid rent and future loss of rent, capped at three months worth, or there is generally no issue as the estates of commercial tenants in bankruptcies most often have no funds to pay claims of any type, so it matters little as to the quantum of a landlord's claim. In this case, I am advised that there may be sufficient funds in the Estate to provide a dividend to ordinary unsecured creditors - making the outcome of the appeal significant to the Appellant.

21 Be that as it may, neither of the statutes which govern rights in these matters provides for the type of claim advanced. Even more, the CTA and its predecessors, has been found for the better part of a century to have the effect of a consensual ending of the lease, and the cases recognize that this is a statutorily permitted breach for which there is no damage remedy, beyond the s. 38 CTA and s. 136 BIA preferred claim.

22 Accordingly, I find that the Trustee has properly disallowed the portions of the Appellant's proof of claim which it did, and the within appeal is dismissed.

23 Counsel are to be thanked for their very helpful briefs.

24 As to costs, counsel have suggested brief written submissions following the release of these Reasons, not to exceed one page. I find this appropriate. Counsel should contact the Bankruptcy Office at Toronto to arrange for their submissions to be forwarded to me, within 45 days hereof.

Appeal dismissed.

End of Document

TAB 7

HMANALY G§140
Houlden & Morawetz Analysis G§140

Houlden and Morawetz Bankruptcy and Insolvency Analysis

THE BANKRUPTCY AND INSOLVENCY ACT

Part V (ss. 136-147)
L.W. Houlden and Geoffrey B. Morawetz

G§140 — Disclaimer and Surrender of Lease by the Trustee

G§140 — Disclaimer and Surrender of Lease by the Trustee

See ss. 136, 137, 138, 139, 140, 140.1, 141, 141, 143, 144, 145, 146, 147

(1) — *Generally*

For the effect of a disclaimer and surrender of a head lease by a trustee in bankruptcy on a sub-lease, see *ante* G§132 "Sub-Lessees".

For the right to disclaim or surrender a lease and the effect of a surrender or disclaimer, resort must be had to provincial law: s. 146. See also s. 30 of the *BIA*, which sets out the powers exercisable by the trustee with the permission of inspectors.

A party taking the position that a lease has been surrendered must specifically plead surrender: *Crystalline Investments Ltd. v. Domgroup Ltd.* (2004), 2004 CarswellOnt 219, 2004 CarswellOnt 220, [2004] S.C.J. No. 3, 2004 SCC 3, 184 O.A.C. 33, 46 C.B.R. (4th) 35, 316 N.R. 1, 234 D.L.R. (4th) 513, 16 R.P.R. (4th) 1 (S.C.C.).

For the form of a disclaimer under s. 38 of the *Commercial Tenancies Act* of Ontario, see Precedent 83 under Precedents in vol. 5.

The Ontario Court of Appeal gave direction on the legal effect of a notice of repudiation of lease given during a *CCAA* proceeding, for a debtor that subsequently became bankrupt. The court emphasized the distinction between a lease termination and a repudiation: *Re TNG Acquisition Inc.*, 2011 CarswellOnt 8039, 107 O.R. (3d) 304, 81 C.B.R. (5th) 151, 2011 ONCA 535 (Ont. C.A.). For a discussion of this judgment, see N§187 "Application to Leases".

The Alberta Court of Appeal dismissed the appeal of the landlord of a commercial lease. The lower court had concluded that a certain sum paid to the landlord by the bankrupt tenant was a security deposit, not prepaid rent. The security deposit became part of the estate of the bankrupt. An issue relating to set-off was returned to the lower court for determination: *York Realty Inc. v. Alignvest Private Debt Ltd.*, 2015 CarswellAlta 2108, 31 C.B.R. (6th) 98, 2015 ABCA 355 (Alta. C.A.). For a discussion of this judgment, see F§63(19) "Necessity for a Security Interest".

(2) — *Meaning of Disclaimer and Surrender*

A surrender and a disclaimer of a lease are different things. A disclaimer is a unilateral act on the part of the trustee terminating the lease. A surrender involves the giving up of the lease with the consent of the landlord; it is a consensual act: *Office Specialty Mfg. Co. v. Eastern Trust Co.* (1931), 13 C.B.R. 166, 3 M.P.R. 526 (N.B. C.A.); *Berkley Property Management Ltd. v. Garden City Plaza Ltd.* (1995), 32 C.B.R. (3d) 258, 29 Alta. L.R. (3d) 434, 171 A.R. 128, 1995 CarswellAlta 274 (Master); *Targa Holdings Ltd. v. Whyte*, 21 C.B.R. (N.S.) 54, [1974] 3 W.W.R. 632, 44 D.L.R. (3d) 209 (Alta. C.A.) The delivery of possession by the trustee to the landlord and the landlord's assumption of possession

effect a surrender of a lease by operation of law: *New Regina Trading Co. v. Canadian Credit Men's Trust Assn.*, [1934] S.C.R. 47, 15 C.B.R. 207, [1934] 1 D.L.R. 630.

(3) — *What constitutes a Surrender or Disclaimer*

The following acts have been held to constitute a surrender or disclaimer:

• giving a letter to a landlord that the trustee was surrendering possession of the leased premises and the landlord putting a new lock on the premises: *Office Specialty Mfg. Co. v. Eastern Trust Co.* (1931), 13 C.B.R. 166, 3 M.P.R. 526 (N.B. C.A.);

• the landlord demanding possession of the leased premises and the trustee in bankruptcy acquiescing and surrendering possession: *New Regina Trading Co. v. Canadian Credit Men's Trust Assn.*, [1934] S.C.R. 47, 15 C.B.R. 207, [1934] 1 D.L.R. 630.

(4) — *What Does Not Constitute a Surrender or Disclaimer*

The following acts have been held not to constitute a surrender or disclaimer of a lease:

• advertising assets for sale and stating in the advertisements that tenderers would have to make arrangements with the landlord for leasing and possession of the demised premises: *Whiteley v. Clarkson* (1933), 14 C.B.R. 306 (Ont. C.A.);

• handing over of keys to the leased premises by the trustee and the acceptance of the keys by the landlord without prejudice to the landlord's rights: *Re Panther Lead Co.*, [1896] 1 Ch. 978, 65 L.J. Ch. 499, 3 Mans 165, 44 W.R. 573.

(5) — *Time for Delivering Disclaimer or Making a Surrender*

Like the election to retain a lease, the right to disclaim or surrender a lease runs from the date of the filing of the assignment in bankruptcy or from the date of a bankruptcy order: *Targa Holdings Ltd. v. Whyte*, 21 C.B.R. (N.S.) 54, [1974] 3 W.W.R. 632, 44 D.L.R. (3d) 209 (Alta. C.A.). The disclaimer or surrender should be made within three months of the date of the filing of the assignment or the making of a bankruptcy order.

(6) — *Effect of the Trustee Entering into Possession*

Under s. 38 of the *Commercial Tenancies Act* of Ontario, the trustee has a right at any time before electing to retain the lease, by notice in writing, to surrender possession or disclaim the lease. The entry into possession of the leased premises and the occupation of them by the trustee are not under s. 38 deemed to be evidence of an intention on the part of the trustee to elect to retain the premises, and the trustee may give a disclaimer or surrender possession notwithstanding that the trustee has entered into possession of the leased premises.

(7) — *Approval of Inspectors*

A trustee may validly surrender or disclaim a lease without the consent of the inspectors: *Office Specialty Mfg. Co. v. Eastern Trust Co.* (1931), 13 C.B.R. 166, 3 M.P.R. 526 (N.B. C.A.). The better practice is to have the approval of the inspectors: s. 30(1)(k). If the approval is not obtained before surrendering or disclaiming the lease, the trustee should as soon as possible have the inspectors ratify its actions: *Office Specialty Mfg. Co. v. Eastern Trust Co., supra.*

If, because of conflict of interest, a majority of inspectors are unable to approve the activities of the trustee in disclaiming or surrendering a lease, the trustee can apply for directions under s. 34: *Re Salok Hotel Co.* (1967), 11 C.B.R. (N.S.) 95, 62 W.W.R. 268, 66 D.L.R. (2d) 5 (Man. Q.B.), affirmed (1967), 11 C.B.R. (N.S.) 158, 62 W.W.R. 705, 66 D.L.R. (2d) 14n (Man. C.A.).

(8) — *Effect of Surrender or Disclaimer*

The legal effect of a surrender or disclaimer is the same. When the trustee surrenders possession or gives a disclaimer of a lease, all the rights and obligations that vested in the trustee upon the making of the receiving order or the filing of

the assignment are terminated: *Cummer-Yonge Invt. Ltd. v. Fagot,* 8 C.B.R. (N.S.) 62, [1965] 2 O.R. 152, 50 D.L.R. (2d) 25 (H.C.), affirmed, [1965] 2 O.R. 157n, 8 C.B.R. (N.S.) 62n, 50 D.L.R. (2d) 30n (C.A.); *Re Vrablik* (1993), 17 C.B.R. (3d) 152, 1993 CarswellOnt 192 (Ont. Gen. Div.); *Re Salok Hotel Co.* (1967), 11 C.B.R. (N.S.) 95, 62 W.W.R. 268, 66 D.L.R. (2d) 5 (Man. Q.B.), affirmed (1967), 11 C.B.R. (N.S.) 158, 62 W.W.R. 705, 66 D.L.R. (2d) 14n (Man. C.A.). The liability of the trustee to pay occupation rent comes to an end: *Re Mussens Ltd.,* 14 C.B.R. 479, [1933] O.W.N. 459 (S.C.). After a disclaimer or surrender, there is no right in Ontario to claim damages for the unexpired portion of the lease: see *post* G§141 "Damages Claimed by Landlord for Unexpired Portion of Lease after Surrender or Disclaimer of Lease by Trustee".

If the trustee has surrendered or disclaimed the lease, the trustee has no rights subsequently to elect to retain the lease: *Re Niki's Palace Restaurant Ltd.* (1983), 48 C.B.R. (N.S.) 236 (Ont. S.C.).

The registrar upheld the disallowance of a landlord's proof of claim for damages suffered as a result of disclaimer of a lease. Section 146 of the *BIA* provides that, subject to the priority of claims set out in s. 136 and the provisions of s. 73(4), the rights of landlords shall be determined according to the laws of the province in which the premises are situated. Here, the rights of the landlord were codified in ss. 38 and 39 of the *Commercial Tenancies Act* (*CTA*). While s. 38 provides for a preferential claim that is similar to s. 136 of the *BIA,* s. 39 of the *CTA* specifies that the 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. The trustee allowed the claims provided for in s. 38 of the *CTA* and s. 136 of the *BIA*, specifically, three months arrears of rent and three months of accelerated rent, together with other entitlements as being rent under the lease. The trustee could disclaim the lease and if so, the tenant is in the same position as if the lease had been surrendered with the consent of the lessor, which means no further liability on the part of the lessee to pay rent and no suggestion that by failing to pay rent the tenant was committing a breach of covenant and liable for liquidated or unliquidated damages. Neither the *BIA* nor the *CTA* that govern rights in these matters provides for the type of claim advanced. The registrar concluded that the trustee had properly disallowed the portions of the landlord's proof of claim and the appeal was dismissed: *Re Linens N Things Canada Corp.* (2009), 2009 CarswellOnt 2849, 53 C.B.R. (5th) 232 (Ont. S.C.J.).

(9) — *Termination of a Lease by an Interim Receiver*

Although an interim receiving order gives the interim receiver of an assignee of a lease power to terminate existing agreements, the interim receiver has no power to terminate the obligations of the original lessee to the lessor. The relationship between the lessor and the original lessee has no connection with the insolvency of the assignee: *J.P. Morgan Canada v. Maxlink Canada Inc.* (2002), 31 C.B.R. (4th) 40, 2002 CarswellOnt 333, 155 O.A.C. 351 (Ont. C.A.).

HMANALY G§141
Houlden & Morawetz Analysis G§141

Houlden and Morawetz Bankruptcy and Insolvency Analysis

THE BANKRUPTCY AND INSOLVENCY ACT

Part V (ss. 136-147)
L.W. Houlden and Geoffrey B. Morawetz

G§141 — Damages Claimed by Landlord for Unexpired Portion
of Lease after Surrender or Disclaimer of Lease by Trustee

G§141 — Damages Claimed by Landlord for Unexpired Portion of Lease after Surrender or Disclaimer of Lease by Trustee

See ss. 136, 137, 138, 139, 140, 140.1, 141, 141, 143, 144, 145, 146, 147

By virtue of s. 146 of the *Bankruptcy and Insolvency Act*, the nature and extent of the landlord's claim for rent and damages for the unexpired portion of a lease are determined by the law of the province in which the leased premises are situated. The preferential claim of the landlord is determined by s. 136(1)(f) of the Act. If, by provincial law, after the trustee has surrendered or disclaimed a lease, there is a claim for rent or damages in addition to the preferred claim under s. 136(1)(f), the claim will only be an unsecured claim in the bankruptcy: *Re Gingras Automobile Ltée*, [1962] S.C.R. 676, 4 C.B.R. (N.S.) 123, 34 D.L.R. (2d) 751.

Under the *Commercial Tenancies Act* of Ontario when a trustee surrenders or disclaims a lease, a landlord has no claim for the rent for the remainder of the term of the lease. The surrender or disclaimer terminates all rights and obligations under the lease to pay rent: *Re Mussens Ltd.*, 14 C.B.R. 479, [1933] O.W.N. 459 (S.C.); *Re Smith* (1933), 14 C.B.R. 335 (Ont. S.C.); *Re Vrablik* (1993), 17 C.B.R. (3d) 152, 1993 CarswellOnt 192 (Ont. Gen. Div.); *Peat Marwick Thorne Inc. v. Natco Trading Corp.* (1995), 31 C.B.R. (3d) 119, 22 O.R. (3d) 727, 44 R.P.R. (2d) 207, 1995 CarswellOnt 55 (Ont. Gen. Div. [Commercial List]).

In *Re Ted Weale Ltd.*, 32 C.B.R. 206, [1952] O.W.N. 560, [1952] 3 D.L.R. 839 (S.C.), a landlord tried to file a claim as an unsecured creditor in respect of four promissory notes given by the tenant at the time of signing the lease, which were to cover the rent for the last four months of the lease. The trustee disclaimed the lease. The registrar found that this claim was an attempt to claim damages for the unexpired portion of the lease and disallowed the claim.

The provincial law is the same in Manitoba as in Ontario. The surrender or disclaimer of a lease by a trustee extinguishes all rights and obligations under the lease to pay rent, and a landlord cannot, after the surrender or disclaimer, claim damages for the rent for the balance of the term: *Re Salok Hotel Co.* (1967), 11 C.B.R. (N.S.) 95, 62 W.W.R. 268, 66 D.L.R. (2d) 5 (Man. Q.B.), affirmed (1967), 11 C.B.R. (N.S.) 158, 62 W.W.R. 705, 66 D.L.R. (2d) 14n (Man. C.A.).

The law in Alberta is the same as in Ontario. The surrender of disclaimer of a lease by a trustee extinguishes all rights and obligations under the lease to pay rent, and a landlord cannot, after the surrender or disclaimer, claim damages for the rent for the balance of the term: *Berkley Property Management Ltd. v. Garden City Plaza Ltd.* (1995), 32 C.B.R. (3d) 258, 29 Alta. L.R. (3d) 434, 171 A.R. 128, 1995 CarswellAlta 274 (Master); *Principal Plaza Leaseholds Ltd. v. Principal Group Ltd. (Trustee of)*, 41 Alta. L.R. (3d) 248, [1996] 9 W.W.R. 539, 188 A.R. 187, 1996 CarswellAlta 676 (Q.B.).

The law would appear to be the same in British Columbia as it is in Ontario, Manitoba and Alberta. See *KKBL No. 297 Ventures Ltd. v. Ikon Office Solutions Inc.* (2003), 47 C.B.R. (4th) 251, 2003 CarswellBC 2598, 2003 BCSC 1598, 16

R.P.R. (4th) 29, 21 B.C.L.R. (4th) 163 (B.C.S.C.); *West Shore Ventures Ltd. v. KPN Holdings Ltd.* (2001), 198 D.L.R. (4th) 520, [2001] 5 W.W.R. 209, 88 B.C.L.R. (3d) 95, 25 C.B.R. (4th) 139, 39 R.P.R. (3d) 155, 152 B.C.A.C. 55, 2001 CarswellBC 725, 250 W.A.C. 55, 2001 BCCA 279, [2001] B.C.W.L.D. 654, [2001] B.C.J. No. 713 (B.C.C.A.) and *Peat Marwick Thorne Inc. v. Natco Trading Corp., supra.*

Under Québec law, where a trustee abandons a lease, it is uncertain whether the landlord has a claim for damages for the remainder of the term after the abandonment. The length of the damage claim may depend on the economic situation and the particular circumstances of the property in which the leased premises are located, and would likely include a period sufficient to prepare the premises for a new tenant. Under earlier caselaw, if the landlord relet the premises, any such claim was wiped out and in ordinary cases, damages was not generally given for more than three months rent in advance, during which time it is expected that the lessor would find a new tenant: *Re Eftaxias* (1962), 3 C.B.R. (N.S.) 152 (Que. S.C.).

End of Document

TAB 8

2011 ABCA 145
Alberta Court of Appeal

Dancole Investments Ltd. v. House of Tools Co. (Trustee of)

2011 CarswellAlta 774, 2011 ABCA 145, [2011] 8 W.W.R. 499, [2011] A.W.L.D. 2319, [2011] A.W.L.D. 2320, 201 A.C.W.S. (3d) 807, 44 Alta. L.R. (5th) 64, 502 A.R. 360, 517 W.A.C. 360, 78 C.B.R. (5th) 81

Dancole Investments Ltd. (Appellant / Applicant) and Bill McCulloch & Associates Inc., Trustee of the Estate of House of Tools Company, a Bankrupt (Respondent / Respondent)

Elizabeth McFadyen, Jack Watson, Frans Slatter JJ.A.

Heard: February 1, 2011
Judgment: May 12, 2011
Docket: Edmonton Appeal 1003-0098-AC

Proceedings: reversing in part *Dancole Investments Ltd. v. House of Tools Co. (Trustee of)* (2010), 488 A.R. 320, 2010 ABQB 223, 2010 CarswellAlta 617 (Alta. Q.B.)

Counsel: D.H. Shell, Q.C., C. Lefebvre for Appellant
S.K. Dhir, L.E. Miller J.A. for Respondent

Subject: Insolvency; Property; Estates and Trusts
Related Abridgment Classifications
Bankruptcy and insolvency
X Priorities of claims
X.4 Claims by landlord
X.4.e Accelerated rent
X.4.e.i Entitlement to claim
Bankruptcy and insolvency
X Priorities of claims
X.4 Claims by landlord
X.4.e Accelerated rent
X.4.e.ii Amount claimable

Headnote
Bankruptcy and insolvency --- Priorities of claims — Claims by landlord — Accelerated rent — Entitlement to claim
Debtor company agreed to lease premises from landlord for ten years from January 1, 2008 — In April 2009, debtor failed to pay rent due under lease — Landlord served notice of default — In May 2009, debtor filed assignment in bankruptcy — Trustee was appointed — Receivership order was obtained appointing interim Receiver — Pursuant to agreement with landlord, Receiver occupied leased premises from May to July 2009 and paid rent to landlord — Section 136(1)(f) of Bankruptcy and Insolvency Act allows landlord preferred claim for three months arrears of rent and accelerated rent for up to three months following bankruptcy (if specified in lease), and provides that any payment made on account of accelerated rent shall be credited against amount "payable by the trustee" for occupation rent — Landlord submitted proof of claim to Trustee claiming three months accelerated rent as provided for in lease as preferred claim under s. 136(1)(f) — Trustee reduced claim by amount paid as occupation rent by Receiver — Chambers judge upheld Trustee's disallowance of claims — Landlord appealed — Appeal allowed in part — Chambers judge erred in his interpretation of s. 136(1)(f) and in his conclusion that rent paid by Receiver constituted "amount payable by the trustee for occupation rent" and permitted reduction in accelerated rent to which landlord was otherwise entitled — No amount was payable by

Trustee for occupation rent, therefore no deduction of accelerated rent was required — Phrase "payable by the trustee" does not include payments made by Receiver — Landlord is not required to establish that it actually sustained loss to establish entitlement to accelerated rent as preferred claim under s. 136(1)(f), it need only establish that it was entitled to accelerated rent under lease — Therefore it was not inconsistent for legislature to recognize right of landlord to claim both accelerated rent and occupation rent — Nothing done by landlord destroyed its entitlement to accelerated rent by operation of lease and statutes.

Bankruptcy and insolvency --- Priorities of claims — Claims by landlord — Accelerated rent — Amount claimable

Debtor company agreed to lease premises from landlord for ten years from January 1, 2008 — In April 2009 debtor failed to pay rent — Landlord served notice of default — In May 2009 debtor filed assignment in bankruptcy — Trustee was appointed — Receivership order was obtained appointing interim Receiver — Pursuant to agreement with landlord, Receiver occupied leased premises from May to July, 2009 and paid rent to landlord — Landlord submitted proof of claim to Trustee claiming three months accelerated rent as preferred claim under s. 136(1)(f) of Bankruptcy and Insolvency Act and sought legal costs it incurred as result of defaults under lease as part of preferred claim — Trustee disallowed landlord's claim for legal costs and reduced preferred claim by amount paid as rent by Receiver — Chambers judge upheld Trustee's disallowance of claims — Landlord appealed — Appeal allowed in part on other grounds — Chambers judge made no error in concluding that legal costs are not recoverable on priority basis under s. 136(1)(f) — Not all rent that is payable under lease is entitled to s. 136(1)(f) preference — In context of s. 136(1)(f), word "rent" is used in its ordinary sense and refers to payments of rent and expenses that accrue on monthly basis, but does not necessarily include all extraordinary expenses that may be added to monthly payment in accordance with terms of lease — Further, costs and expenses incurred after bankruptcy could not be included in deciding amount of monthly accelerated rent — Wording of lease, referring to "monthly rent", included expenses incurred on monthly basis but did not include extraordinary expenses that occurred after breach — Wording referred to obligations that accrue monthly on regular basis.

Table of Authorities

Cases considered:

A. Marquette & fils Inc. v. Mercure (1975), 1975 CarswellQue 51, 10 N.R. 239, 65 D.L.R. (3d) 136, [1977] 1 S.C.R. 547, 1975 CarswellQue 51F (S.C.C.) — referred to

Bank of Montreal v. Steel City Sales Ltd. (1983), 47 C.B.R. (N.S.) 15, 148 D.L.R. (3d) 585, 57 N.S.R. (2d) 396, 120 A.P.R. 396, 1983 CarswellNS 47, 28 R.P.R. 225 (N.S. T.D.) — referred to

Canadian Petcetera Ltd. Partnership v. 2876 R. Holdings Ltd. (2010), 295 B.C.A.C. 201, 501 W.A.C. 201, 2010 CarswellBC 2852, 2010 BCCA 469, [2010] 12 W.W.R. 189, 10 B.C.L.R. (5th) 235, 70 C.B.R. (5th) 180, 96 R.P.R. (4th) 157 (B.C. C.A.) — considered

Father & Son Investments Inc. v. Maverick Brewing Corp. (2007), 38 C.B.R. (5th) 272, 83 Alta. L.R. (4th) 287, [2008] 5 W.W.R. 518, 2007 CarswellAlta 1694, 2007 ABQB 752, 439 A.R. 247 (Alta. Q.B.) — referred to

Maple Homes Canada Ltd., Re (2000), 2000 BCSC 1443, 2000 CarswellBC 2017, 21 C.B.R. (4th) 87 (B.C. S.C.) — referred to

McCoubrey, Re (1924), 5 C.B.R. 248, [1924] 3 W.W.R. 587, [1924] 4 D.L.R. 1227, 1924 CarswellAlta 69 (Alta. T.D.) — referred to

Port Alice Specialty Cellulose Inc., Re (2005), 41 B.C.L.R. (4th) 259, 2005 BCCA 299, 2005 CarswellBC 1280, 254 D.L.R. (4th) 397, (sub nom. *Port Alice Specialty Cellulose Inc. (Bankrupt) v. ConocoPhillips Co.*) 212 B.C.A.C. 310, (sub nom. *Port Alice Specialty Cellulose Inc. (Bankrupt) v. ConocoPhillips Co.*) 350 W.A.C. 310, 11 C.B.R. (5th) 279 (B.C. C.A.) — followed

Sawridge Manor Ltd. v. Western Canada Beverage Corp. (1995), 33 C.B.R. (3d) 249, 61 B.C.A.C. 32, 100 W.A.C. 32, 1995 CarswellBC 169 (B.C. C.A.) — referred to

Shilco Industrial Sales Ltd., Re (1977), 23 C.B.R. (N.S.) 255, 1977 CarswellOnt 74 (Ont. Bktcy.) — followed

Shogun Holdings Ltd. v. Latitude 53 Realty Ltd. (1980), 37 C.B.R. (N.S.) 134, 1980 CarswellAlta 183 (Alta. Q.B.) — referred to

Soren Brothers Ltd., Re (1926), 1926 CarswellOnt 31, 30 O.W.N. 12, 7 C.B.R. 545 (Ont. S.C.) — referred to

1231640 Ontario Inc., Re (2007), 37 C.B.R. (5th) 185, 2007 ONCA 810, 2007 CarswellOnt 7595, 289 D.L.R. (4th) 684, 13 P.P.S.A.C. (3d) 57 (Ont. C.A.) — referred to

1231640 Ontario Inc., Re (2008), (sub nom. *Royal Bank of Canada v. 1231640 Ontario Inc. (Bankrupt)*) 386 N.R. 393 (note), (sub nom. *Royal Bank of Canada v. 1231640 Ontario Inc. (Bankrupt)*) 253 O.A.C. 396 (note), 2008 CarswellOnt 2897, 2008 CarswellOnt 2898 (S.C.C.) — referred to

Statutes considered:

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

Generally — referred to

s. 2(1) "trustee" or "licensed trustee" — referred to

s. 14.06 [en. 1992, c. 27, s. 9(1)] — referred to

s. 31(1) — referred to

s. 46 — referred to

s. 47 — referred to

s. 47(1) — referred to

s. 71 — considered

s. 73(4) — considered

s. 136(1)(f) — considered

s. 146 — considered

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36

Generally — referred to

Judicature Act, R.S.A. 2000, c. J-2

s. 13(2) — referred to

Landlord's Rights on Bankruptcy Act, R.S.A. 2000, c. L-5

Generally — referred to

s. 1 — considered

s. 2(a) — considered

s. 3 — considered

s. 3(b) — referred to

s. 4 — referred to

s. 5 — considered

s. 5(3) — considered

Words and phrases considered:

"payable by the trustee"

The primary question we must answer is whether the phrase "payable by the trustee" [in s. 136(1)(f) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3] includes payments made by the Receiver. We are of the view that it does not.

rent

In the context of [s.]136(1)(f) [of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3], the word "rent" is used in its ordinary sense and refers to payments of rent and expenses that accrue on a monthly basis, but does not necessarily include all extraordinary expenses that may be added to the monthly payment in accordance with the terms of the lease.

Further, costs and expenses incurred after bankruptcy cannot be included in deciding the amount of monthly accelerated rent.

APPEAL by landlord from judgment reported at *Dancole Investments Ltd. v. House of Tools Co. (Trustee of)* (2010), 488 A.R. 320, 2010 ABQB 223, 2010 CarswellAlta 617 (Alta. Q.B.), upholding Trustee's disallowance of landlord's claims.

***Per curiam*:**

Facts

1 The House of Tools Company agreed to lease premises from the appellant, Dancole Investments Ltd. for a period of ten years, commencing January 1, 2008. On April 1, 2009, House of Tools failed to pay the rent due under the lease and, on April 15, 2009, Dancole served a Notice of Default on House of Tools, specifying the default as the failure to pay Basic Rent, Operating Costs, Taxes and Goods and Services Tax in the amount of $48,059.37.

2 House of Tools failed to rectify its default, and on April 30, 2009, the bailiff, instructed by Dancole, attended the premises but was unable to effect seizure as no one was present. A Notice of Seizure was posted to the door of the premises at 3:21 p.m. on May 1, 2009. That same day, House of Tools obtained an order under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36.

3 On May 12, 2009, House of Tools filed an assignment into bankruptcy effective May 13. Bill McCulloch & Associates Inc. (the "Trustee") was appointed the trustee of its estate.

4 On May 13, 2009, the Bank of America successfully applied to set aside the CCAA Order and obtained a Receivership Order pursuant to s. 47(1) of the *Bankruptcy and Insolvency Act* ("*BIA*") and s. 13(2) of the *Judicature Act*, appointing RSM Richter Inc. ("Receiver") as interim receiver of House of Tools' assets.

5 Pursuant to an agreement with Dancole, the Receiver occupied the leased premises from May 13, 2009 to July 21, 2009, and paid rent to Dancole in the amount of $111,355.15. The Receiver delivered up the premises to Dancole on July 21, 2009. The Receiver's payments for occupation rent did not include interest or other costs, such as legal costs, incurred by Dancole as a result of the breaches of the terms of the lease. The Receiver transferred to the Trustee all funds remaining after payment of the secured claim and its expenses.

6 Before entering into the agreement with the Receiver, Dancole made inquiries of the Trustee, who indicated that it had no interest in the premises, and that issues relating to occupation rent were a matter for the Receiver and Dancole. The Trustee never assumed actual possession of the leased premises. The Trustee allowed the Receiver to make its own arrangements with Dancole and to use the leased premises to carry out its work under the Receivership Order.

7 Dancole submitted a Proof of Claim to the Trustee claiming three months accelerated rent as provided for in the Lease as a preferred claim under s. 136(1)(f) of the *BIA*. Dancole also sought its legal costs as part of its preferred claim.

8 The Trustee disallowed Dancole's claim for legal costs and reduced the preferred claim by the amount paid as occupation rent by the Receiver to Dancole.

9 In an action in the Court of Queen's Bench, Dancole sought the following declarations:

(1) the rent paid by the Receiver is not to be deducted for the amount of Dancole's preferred claim under s. 136(1)(f) of the *BIA*, and

(2) the legal costs incurred by Dancole arising from House of Tools' defaults form part of the rent payable under the Lease and are to be included in the calculation of Dancole's preferred claim.

10 The chambers judge upheld the Trustee's disallowance of Dancole's claims: *Dancole Investments Ltd. v. House of Tools Co. (Trustee of)*, 2010 ABQB 223, 488 A.R. 320 (Alta. Q.B.). He concluded that Dancole was not entitled to claim a preference for accelerated rent, as Dancole had already received occupation rent from House of Tools' assets. He concluded that pursuant to s. 136(1)(f) of the *BIA*, Dancole "will not be entitled to both acceleration rent and occupation rent for the same 3 months." While the chamber judge did not consider it necessary to address the claim for legal costs as part of rent, he opined that rent, for the purposes of s. 136(1)(f), did not include irregular costs that do not accrue day-to-day, such as the legal costs in this case.

Legislation

11 Dancole's claim to priority over other creditors is defined by s. 136(1)(f) of the *BIA*:

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:

...

(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;

12 Other relevant provisions of the *BIA* are as follows:

71 On a bankruptcy order being made or an assignment being filed with an official receiver, a bankrupt ceases to have any capacity to dispose of or otherwise deal with their property, which shall, subject to this Act and to the rights of secured creditors, immediately pass to and vest in the trustee named in the bankruptcy order or assignment, and in any case of change of trustee the property shall pass from trustee to trustee without any assignment or transfer.

...

73(4) Any property of a bankrupt under seizure for rent or taxes shall on production of a copy of the bankruptcy order or the assignment certified by the trustee as a true copy be delivered without delay to the trustee, but the costs of distress or, in the Province of Quebec, the costs of seizure are a security on the property ranking ahead of any other security on it, and, if the property or any part of it has been sold, the money realized from the sale less the costs of distress, or seizure, and sale shall be paid to the trustee.

...

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.

13 The *Landlord's Rights on Bankruptcy Act*, R.S.A. 2000, C. L-5 provides:

1 A lessee against or by whom a receiving order or assignment is made under the *Bankruptcy and Insolvency Act* (Canada) is deemed to have made an assignment of all the lessee's property for the general benefit of the lessee's creditors before the date of the receiving order or assignment.

2 As soon as the receiving order or assignment is made

(a) the landlord of the lessee is not afterwards entitled to distrain or realize the rent by distress, ...

3 The lessee is a debtor to the landlord

(a) for all surplus rent in excess of the 3 months' rent accrued due at the date of the receiving order or assignment, and

(b) for any accelerated rent to which the landlord may be entitled under the lease but not exceeding an amount equal to 3 months' rent.

4 Subject to section 3, the landlord has no right to claim as a debt any money due to the landlord from the lessee for any portion of the unexpired term of the lessee's lease.

5(1) The trustee is entitled to occupy and to continue in occupation of the leased premises for so long as the trustee requires the premises for the purposes of the trust estate vested in the trustee.

(2) The trustee shall pay to the landlord for the period during which the trustee actually occupies the leased premises from and after the date of the receiving order or assignment a rental calculated on the basis of the lease.

(3) A payment to be made to the landlord in respect of accelerated rent shall be credited against the amount payable by the trustee for the period of the trustee's occupation.

Issues

14 The appeal raises the following issues:

Did the chambers judge err by failing to distinguish between the Receiver and the Trustee in interpreting s. 136(1)(f) of the *BIA*? Are rent payments made by the Receiver to Dancole amounts "payable by the trustee for occupation rent" under s. 136(1)(f) of the *BIA*? Are Dancole's legal costs recoverable as part of its preferred claim for accelerated rent?

Standard of Review

15 The parties agree that the issues are subject to the correctness standard, as they involve questions of law regarding statutory interpretation. To the extent that the second issue involves an interpretation of the Lease, it also is reviewable on a correctness standard.

16 The general principles regarding the appropriate statutory interpretation of the *BIA* were referenced in *Port Alice Specialty Cellulose Inc., Re*, 2005 BCCA 299 (B.C. C.A.) at paras. 25 - 27, (2005), 41 B.C.L.R. (4th) 259 (B.C. C.A.) (and recently followed by the court in *Canadian Petcetera Ltd. Partnership v. 2876 R. Holdings Ltd.*, 2010 BCCA 469, 10 B.C.L.R. (5th) 235 (B.C. C.A.) at para. 18):

There is no dispute that the proper approach to the interpretation of s. 81.1 is that described in E.A. Driedger's *Construction of Statutes* (2nd ed. 1983), at p. 87:

> Today there is only one principle or approach, namely, the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament.

This approach has been approved by the Supreme Court of Canada in numerous cases. The Supreme Court has also said that this approach is confirmed by s. 12 of the ***Interpretation Act***, R.S.C. 1985, c. I-21, which provides that every enactment "is deemed remedial, and shall be given such fair, large and liberal construction and interpretation as best ensures the attainment of its objects": see *Barrie Public Utilities v. Canadian Cable Television Assn.*, [2003] 1 S.C.R. 476 at para. 20; ***Bell ExpressVu Limited Partnership v. Rex***, [2002] 2 S.C.R. 559 at para. 26.

17 In interpreting the *BIA*, courts have noted that it is a commercial statute used by business people and should not be given an overly narrow or legalistic approach: see *McCoubrey, Re*, [1924] 4 D.L.R. 1227 (Alta. T.D.), at 1231-32; *A. Marquette & fils Inc. v. Mercure* (1975), [1977] 1 S.C.R. 547 (S.C.C.), at 556; *Maple Homes Canada Ltd., Re*, 2000 BCSC 1443 (B.C. S.C.) at para. 21.

Are Rent Payments From the Receiver to Dancole Amounts "Payable by the Trustee for Occupation Rent" Under s. 136(1)(f) of the BIA?

18 Dancole submits that s. 136(1)(f) of the *BIA* provides that payments of occupation rent made by or payable by the trustee are to be set off against a landlord's preferred claim for accelerated rent. In enacting the *BIA*, Parliament has made clear distinctions between the trustee in bankruptcy, and a receiver or an interim receiver appointed under ss. 46 and 47. See, for instance, ss. 14.06 and 31(1). Accordingly, Dancole argues that Parliament would have used explicit language in s. 136(1)(f) if the intent was to include occupation rent payments made by the Receiver. Dancole acknowledges that the Receiver meets the general definition of "trustee" under s. 2, as the Receiver is licensed under the *BIA*, and was appointed as interim receiver under the *BIA*. However, Dancole submits that s. 136(1)(f) refers to "*the* trustee," which refers to the trustee appointed to administer the assets of the bankrupt in the case, as opposed to "a trustee," which defines who may act as a trustee or receiver for the purposes of the *BIA*.

19 The Trustee supports the decision of the chambers judge, submitting that the principal objective of the *BIA* is to ensure equality in the distribution of the assets of the bankrupt amongst the ordinary creditors. He submits that as the accelerated rent and the occupation rent are paid out of the assets of the bankrupt, the only reasonable interpretation that meets this objective of the *BIA* is that adopted by the chambers judge. He further submits that double payment of accelerated rent out of the estate of the bankrupt is contrary to the intent of the legislation.

20 In our view, Dancole's submissions are consistent with the appropriate principles of statutory interpretation and are correct. Section 136(1)(f) of the *BIA* allows the landlord a preferred claim for three months arrears of rent and accelerated rent for a period not exceeding three months following the bankruptcy (if specified in the lease), and provides that any payment made on account of accelerated rent shall be credited against the amount "payable by the trustee" for occupation rent.

21 The primary question we must answer is whether the phrase "payable by the trustee" includes payments made by the Receiver. We are of the view that it does not.

22 The *BIA* clearly distinguishes between the legal position, the rights, duties, and obligations of the trustee in bankruptcy and the receiver. Under s. 71 of the *BIA*, upon the issuance of a receiving order appointing the trustee in bankruptcy or upon making an assignment in bankruptcy, the bankrupt's right to deal with the property ends and all of its property is immediately vested in the trustee in bankruptcy. There is no similar vesting of the bankrupt's property in the receiver. The receiver's authority to take possession of or to deal with the property depends on the terms of the court order appointing the receiver.

23 Under s. 146, the landlord's rights on bankruptcy (subject to s. 136(1)(f) priority and s. 73(4)), and the trustee's powers and obligations regarding the bankrupt's leased property are determined by provincial law: *Sawridge Manor Ltd. v. Western Canada Beverage Corp.* (1995), 61 B.C.A.C. 32, 33 C.B.R. (3d) 249 (B.C. C.A.) at para. 5. In Alberta, the *Landlord's Rights on Bankruptcy Act*, assigns all of the lessee's property to the trustee in bankruptcy prior to the date of the receiving order or assignment. All rights previously held by a landlord to enforce payment of arrears of rent and other amounts, or otherwise enforce payment, are terminated. The landlord's claim for rent due under the unexpired portion of the lease is limited to three months. The trustee has the right to occupy the leased premises and if it does so, it must pay occupation rent: see Houlden and Morawetz, *Bankruptcy and Insolvency Law of Canada*, (4th ed.) loose-leaf (updated to Release 9, 2010)(Toronto: Thomson Reuters Canada Limited, 2009) at 5 - 247. Although the property is vested in the trustee, the trustee who does not occupy the premises is under no obligation to pay occupation rent.

24 There are no similar legislative provisions dealing with the rights and duties of an interim receiver in respect of leased property. No legislation vests the debtor's property in the interim receiver, nor governs its use and occupation of the property. No legislation requires the interim receiver to pay occupation rent for its use and possession of the leased property under the receivership order. The property does not vest in the interim receiver. The interim receiver's liability to pay occupation rent is based entirely on the contract, express or implied, between the interim receiver and landlord. In the absence of an agreement on the part of the interim receiver to pay rent during its occupancy, the court may impose an obligation to pay reasonable rent. See *Father & Son Investments Inc. v. Maverick Brewing Corp.*, 2007 ABQB 752, 439 A.R. 247 (Alta. Q.B.) and *Bank of Montreal v. Steel City Sales Ltd.* (1983), 148 D.L.R. (3d) 585, 57 N.S.R. (2d) 396 (N.S. T.D.). Absent an agreement, express or implied there is no obligation on the interim receiver to pay occupation rent. The debtor may remain in possession of the leased premises during a receivership (*Soren Brothers Ltd., Re* (1926), 7 C.B.R. 545 (Ont. S.C.) or a court-appointed receiver (*1231640 Ontario Inc., Re*, 2007 ONCA 810 (Ont. C.A.) at paras. 22 - 28, (2007), 289 D.L.R. (4th) 684 (Ont. C.A.) (*per* Feldman J.A.), leave to appeal to SCC granted: [2008] S.C.C.A. No. 34 (S.C.C.)). The interim receiver who enters into an agreement with a landlord or who is obliged to pay rent because of its occupancy of the leased property is personally liable to pay the rent owing.

25 Although the legislature saw fit to require the deduction of accelerated rent from any occupation rent payable by the trustee in bankruptcy, it did not provide for the deduction of accelerated rent from rent payable by the receiver.

26 The Trustee submits that Dancole's interpretation would result in a conflict between the *BIA* and the *Landlord's Rights on Bankruptcy Act*, essentially permitting payment of rent in excess of three months or double rent. We do not agree. The *BIA* and the *Landlord's Rights on Bankruptcy Act* both allow the trustee to take possession of the property and pay occupation rent. The amount paid by the trustee is to be deducted from accelerated rent to which the landlord is entitled.

27 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.

28 Accordingly, where a trustee disclaims or surrenders the lease shortly after bankruptcy, the landlord remains entitled to the preferred claim for accelerated rent, even though the landlord is able to rent the property to a third party immediately, or at an increased rental. This conclusion is supported by the construction of the statute. Section 136(1)(f) of the *BIA*, and s. 5(3) of the *Landlord's Rights on Bankruptcy Act* both provide that the landlord must give credit for "the amount payable by the trustee" for occupation rent. This specific set-off demonstrates that the statutes contemplate

that the landlord can (in some circumstances) be entitled to the three months of accelerated rent, as well as amounts recovered for actual occupation. If the statutes contemplated a general duty to mitigate, or an implied prohibition on "double recovery," this specific qualification would not be required. Giving credit for the amount payable by the trustee would be automatic.

29 The Trustee also submits that Dancole's interpretation of the lease conflicts with the intent of the *BIA* to treat all ordinary creditors equally. It submits that s. 136(1)(f) should be narrowly interpreted as it provides exceptions to this rule. Comparing the landlord's claims to that of other ordinary creditors is problematic. Generally, the landlord has rights that exceed those of an ordinary creditor, whether they arise by virtue of contract, statute or the common law. These include the right to distrain for arrears, the right to recover damages for the unexpired term of the lease, and to provide for accelerated rent to offset damages in the event of breach.

30 The *BIA* and the *Landlord's Rights on Bankruptcy Act* represent a balancing of the rights of the landlord against the rights of the other creditors. Under the statutory scheme, the landlord's right to claim for the value of the balance of the lease is cut off at the three-month point following termination of the lease, as is the related power of the landlord to distrain on goods found on the premises: *Landlord's Rights on Bankruptcy Act*, ss. 3(b) and 4. That limits the claim that the landlord might make as an unsecured creditor, and truncates its claim against the goods found on the premises. The *quid pro quo* is that the landlord is given a preferred claim for three months of accelerated rent. The preferred status of this three month claim is intended to compensate the landlord for the loss of the value of the lease past the three-month point, and is separate and apart from any compensation the landlord may be entitled to for actual occupation of the premises. The express proviso that credit must nevertheless be given for occupation rent payable by the trustee is simply a further refinement of the balancing of rights between the landlord and the other creditors of the estate.

31 Conceptually, the argument is that Dancole is achieving a "double recovery" that should not be allowed, or that Dancole must essentially "mitigate its losses" by accounting for the rent received from the Receiver. This argument fails to recognize that the landlord is recovering for two different bundles of rights, and there is no "double recovery" for any one loss. The landlord is not required to establish that it actually sustained a loss to establish its entitlement to accelerated rent as a preferred claim under s. 136(1)(f). It need only establish that it was entitled to accelerated rent under the lease. It is therefore not inconsistent for the legislature to recognize the right of the landlord to claim both accelerated rent and occupation rent.

32 The trustee's liability for occupation rent does not arise until the estate vests pursuant to s. 71 of the *BIA* and attaches only if the trustee elects to take possession of the leased premises: Houlden and Morawetz at 5 - 251. The receiver's authority to deal with the debtor's property derives entirely from the Receivership Order issued by the Court pursuant to s. 46 and 47 of the *BIA*. In this case, the Receivership Order granted extensive powers to the Receiver to deal with House of Tools' property, including the right to take possession of the property and the discretion to deal with it. Paragraph 3(q) of the Receivership Order specifically granted the Receiver authority to enter into agreements with the Trustee regarding the occupation for any property owned or leased by the House of Tools. This provision recognizes the vesting of the estate in the Trustee, and the Trustee's right to assume occupation of the leasehold premises and potentially incur the obligation to pay occupation rent.

33 However, the Trustee refused to take possession of the leased premises, disclaimed any interest in the premises and denied any responsibility to pay occupation rent. The Trustee advised Dancole that it took no position with regard to the payment of use and occupation rent from the date of the appointment of the Receiver, as that was a matter between the Receiver and Dancole. Further, the Trustee confirmed that the Receiver had been appointed to dispose of House of Tools' assets, impliedly denying responsibility for that phase of the proceedings. Throughout, the Receiver was obliged to pay occupation rent to Dancole, and as permitted by law, was entitled to recover the amount paid for rent as costs incurred in the receivership. The occupation rent was never payable by the Trustee or anyone other than the Receiver. Because the Receiver is entitled to recover its costs, the rent paid by it to Dancole under its agreement with Dancole did not come from the estate available for ordinary creditors, and was not an expense or amount payable by the Trustee as it was never paid out of the bankruptcy estate.

34 What is said to reduce the bankruptcy estate available for equal distribution to non-preferred creditors is the three month period of accelerated rent for which Parliament has given a priority to the landlord. Nothing done by Dancole destroyed its entitlement to accelerated rent by operation of the lease and the two statutes. The non-preferred creditors are not prejudiced as a result of Dancole's statutory preference remaining in place.

35 The Receiver's ability to recover its costs from the sale of the stock and merchandise pursuant to Bank of America's secured interest also had no unfair effect on other creditors. No one disputes that the Bank of America was entitled to act under its security. The Receiver found it efficient to engage Dancole in the recovery process, as opposed to moving the stock and merchandise somewhere else. The bankrupt estate was entitle to receive only the amounts that remained after the payment of the Bank of America claim. The fact that part of the Receiver's charges related to a payment made to Dancole did not change that situation. That payment did not unfairly advantage Dancole nor did it unfairly reduce the amount remaining for the bankruptcy estate.

36 We are of the view that the chambers judge erred in his interpretation of s. 136(1)(f) of the *BIA* and in his conclusion that the rent paid by the Receiver during its occupancy of the leased premises constitutes an "amount payable by the trustee for occupation rent" and permits the reduction in the accelerated rent to which Dancole was otherwise entitled. No amount was payable by the Trustee for occupation rent, and therefore no deduction of accelerated rent was required.

37 The appeal is allowed to that extent.

Are the Landlord's Legal Costs Recoverable as Part of Its Preferred Claim for Accelerated Rent?

38 On the final ground of appeal, we are asked to consider the meaning of "rent" and "accelerated rent" in s. 136(1)(f) of the *BIA*.

39 Dancole seeks priority payment under s. 136(1)(f) for the legal costs it incurred as a result of the defaults under the lease. Dancole retained its lawyers on April 1, 2009 and incurred legal fees prior to the registration of the assignment in bankruptcy in relation to the enforcement steps taken regarding arrears of rent, the CCAA proceedings, and in preparation for the Receivership application on May 13, 2009. Additional legal fees arose after the bankruptcy. These legal costs were not expenses that accrued on a monthly basis under the terms of the lease.

40 "Rent" is defined in Article 3 of the lease to include (a) monthly basic rent, (b) House of Tools' share of operating costs and taxes, payable monthly, (c) monthly payments in relation to an HVAC system, (d) GST payable on each of these items, and (e) all such other sums of money as may be required to be paid by House of Tools under the lease.

41 Dancole relies on Articles 11. 3 and 13.1 and says that these provisions, along with Article 3.1(e), required House of Tools to pay the legal expenses so incurred and that these expenses are other sums of money required to be paid as rent under the Lease.

42 The Trustee does not dispute that legal costs may be payable as rent under the lease although the amount is not admitted. Rather, the Trustee submits that Dancole is not entitled to add these costs to its preferred claim under s. 136(1)(f), on the basis that the provision permits the recovery, on a preferred basis, of rent and expenses that accrue on a regular monthly basis, but not the recovery of unusual or extraordinary expenses. The Trustee relies on the decision in *Shilco Industrial Sales Ltd., Re* (1977), 23 C.B.R. (N.S.) 255 (Ont. Bktcy.), where Registrar Ferron concluded that rent costs that do not accrue on a day-to-day basis in the three month period preceding the bankruptcy are not to be treated as preferred claims. Accelerated rent was not in issue in that case.

43 "Rent" is not defined in the *BIA* or the *Landlord's Rights on Bankruptcy Act*. Generally, whether an item is properly included as rent is largely a function of the terms of the lease. If it establishes certain prerequisites that are to be met before the item can be claimed as rent, then those prerequisites must be met before the item may be included as rent for the purposes of the lease: *Shogun Holdings Ltd. v. Latitude 53 Realty Ltd.* (1980), 37 C.B.R. (N.S.) 134 (Alta. Q.B.).

44 However that does not resolve the matter, because not all rent that is payable under the lease is entitled to s. 136(1)(f) preference. We agree with the view expressed in *Shilco*. In the context of 136(1)(f), the word "rent" is used in its ordinary sense and refers to payments of rent and expenses that accrue on a monthly basis, but does not necessarily include all extraordinary expenses that may be added to the monthly payment in accordance with the terms of the lease.

45 Further, costs and expenses incurred after bankruptcy cannot be included in deciding the amount of monthly accelerated rent. Dancole argues that expenses actually incurred after the bankruptcy can be included in the permitted accelerated rent. We do not agree. The accelerated rent provision is found in Article 14.2 and provides that in the event of a breach, "at the option of the Landlord, the full amount of the current month's and the next three (3) months' *monthly* rent shall immediately become due and payable," [emphasis added] and allows Dancole to exercise its right of distraint and to re-enter the property. The wording of the lease, referring as it does to the "monthly rent," includes expenses incurred on a monthly basis but does not include extraordinary expenses that occur after the breach. This wording refers to obligations that accrue monthly on a regular basis, such as the basic rent, the tenant's proportionate share of operating expenses and taxes, the HVAC system monthly payments, and the GST in respect of each of these items, all of which are defined in Article 3.1(a), (b), (c) and (d). The term "monthly rent" does not include payments referred to in (e).

46 Section 136(1)(f) adopts similar terminology, referring to "arrears of rent for three months," and "accelerated rent for a period not exceeding three months." The ordinary meaning of each of these terms refers to those obligations under the lease that accrue monthly and are ascertainable on that basis.

47 The chambers judge made no error in concluding that legal costs are not recoverable on a priority basis under s. 136(1)(f).

Appeal allowed in part.

End of Document

TAB 9

1971 CarswellBC 239
Supreme Court of Canada

Highway Properties Ltd. v. Kelly, Douglas & Co.

1971 CarswellBC 239, 1971 CarswellBC 274, [1971] S.C.R. 562, [1972] 2 W.W.R. 28, 17 D.L.R. (3d) 710

Highway Properties Limited v. Kelly, Douglas and Company Limited

Martland, Judson, Ritchie, Spence and Laskin JJ.

Judgment: February 1, 1971

Counsel: *W. B. Williston, Q.C.* and *W. C. Graham*, for appellant.
J. L. Farris, Q.C. and *I. G. Nathanson*, for respondent.

Subject: Property
Related Abridgment Classifications
Real property
V Landlord and tenant
V.13 Surrender
V.13.b Implied surrender
V.13.b.iii Miscellaneous

Headnote
Landlord and Tenant --- Surrender — Implied surrender
Landlord and tenant — Lease for term of years — Repudiation of lease by tenant — Landlord's actions leading to surrender by operation of law — Whether landlord can recover for loss of lease.
Appeal from the judgment of the Court of Appeal for British Columbia, 66 W.W.R. 705, 1 D.L.R. (3d) 626, dismissing an appeal from the judgment of Macdonald J., 60 W.W.R. 193. Appeal allowed.
Respondent had expressly repudiated its lease of premises in a shopping centre and appellant landlord had resumed possession, giving notice that it would hold respondent liable for damages suffered by reason of the repudiation. In the action damages were claimed not only for loss to the date of repudiation but also for prospective loss occasioned by respondent's failure to carry on a supermarket business for the term of the lease. In the lower Courts it was held, following *Goldhar v. Universal Sections & Mouldings Ltd.*, [1963] 1 O.R. 189, 36 D.L.R. (2d) 450 (C.A.), that the repudiation of the lease by the respondent and the taking of possession by the appellant amounted to a surrender, so that the lease ceased to exist, and that appellant was entitled to damages only up to the date of surrender.
Held that the appeal must be allowed; repudiation by the tenant gave the landlord an option whether to hold the tenant to the terms of the lease, or whether to terminate it, but on repudiation a right of action for damages arose, and it was open to the landlord to terminate the lease, giving at the same time notice to the tenant that damages would be claimed in respect of the unexpired term. It was no longer sensible to pretend that a commercial lease, such as the one in the case at bar, was simply a conveyance, and not also a contract. It was equally untenable to deny resort to the full armoury of remedies ordinarily available to redress repudiation of covenants, merely because such covenants might be associated in land: *Goldhar v. Universal Sections & Mouldings Ltd.*, supra, overruled; *Buchanan v. Byrnes* (1906), 3 C.L.R. 704 applied.

The judgment of the Court was delivered by *Laskin J.*:

1 The issue in this appeal arises out of the repudiation of an unexpired lease by the major tenant in a shopping centre and the resumption of possession by the landlord, with notice to the defaulting tenant that it would be held liable for damages suffered by the landlord as a result of the admittedly wrongful repudiation. This issue raises squarely the correctness of the decision of the Ontario Court of Appeal in *Goldhar v. Universal Sections & Mouldings Ltd.*, [1963] 1 O.R. 189, 36 D.L.R. (2d) 450, which was followed by the majority of the British Columbia Court of Appeal in the present case.

2 The substantial question emerging from the facts is the measure and range of damages which the landlord, the appellant before this Court, may claim by reason of the repudiation by the tenant, the respondent herein, of its lease of certain premises, and its consequent abandonment of those premises, where the landlord took possession with a contemporaneous assertion of its right to full damages according to the loss calculable over the unexpired term of the lease. It will be necessary, in dealing with this question, to consider the situations where, upon the tenant's repudiation and abandonment, the landlord does not resume possession but insists on enforcing the lease, or takes possession on his own or on the tenant's account. A common characterization of the problem in this appeal is whether it is to be resolved according to the law of property or according to the law of contract; but, in my opinion, this is an over-simplification.

3 The dispute between the parties stems from a lease of 19th August 1960 under which the landlord demised certain premises in its shopping centre to the tenant "to be used for grocery store and super market". A term of 15 years from 1st October 1960 was specified at a prescribed annual rent, payable monthly in advance, plus an additional rent based on a certain formula which need not be reproduced here. The tenant covenanted, inter alia, to pay rent, certain taxes and maintenance costs; not to do or suffer anything to be done on the demised premises without the landlord's consent whereby insurance policies thereon might become void or voidable or the premiums increased; and to pay into a promotion fund to be used for the benefit of the shopping centre. There were covenants for repair and provisions for renewal but their terms are not germane to the disposition of this appeal. There was also a covenant by the landlord for quiet enjoyment. Clause 5(a), so far as relevant here, provided that if the rent or any part thereof be in arrears for 15 days or if any covenant by the tenant should be unfulfilled, and the failure to pay rent or fulfill the covenant should continue 15 days after notice thereof to the tenant, then the current month's rent and three months' additional rent should immediately become due and the landlord might forthwith re-enter, and thereupon the demise should absolutely determine, but without prejudice to any right of action in respect of any antecedent breach of the tenant's covenants.

4 Clause 9, which was central to the landlord's claim for damages, was as follows:

> The tenant further covenants and agrees that it will commence to carry on its business within thirty (30) days from the completion of the demised premises and will carry on its business on the said premises continuously. The demised premises shall not be used for any other purpose than as to conduct the Tenant's business in the said premises during such hours as the Landlord may from time to time require on all business days during the term hereby created and in such manner that the Landlord may at all times receive the maximum amount of income from the operation of such business in and upon the demised premises. The Tenant shall install and maintain at all times in the demised premises first class trade fixtures and furniture adequate and appropriate for the business of the Tenant thereon. The Tenant further agrees to conduct its business as aforesaid in the said premises during such evenings and for such hours thereof during the term hereby created as permitted by the By-laws of the Corporation of the District of North Vancouver, B.C. and consistent with the practices generally acceptable by retail outlets in the area.

5 The shopping centre built by the appellant consisted of 11 stores, including the supermarket premises let to the respondent. Before buying the land on which the shopping centre was later built, the appellant obtained the commitment of the respondent to lease space therein for a food supermarket to be constructed according to its specifications. This commitment was evidenced by a lease dated blank day of May 1960, whose terms were carried into the document of 19th August 1960. The respondent went into possession through a subtenant (with the appellant's consent) on or about 20th October 1960. By February 1961 only five other stores in the shopping centre had been let, and the venture did not prosper. The supermarket subtenant indicated its intention to close the business down on 24th March 1962, and did so. The appellant drew the respondent's attention to cl. 9 of the lease and received an assurance in a letter from the

respondent of 26th March 1962 that it was standing by the lease and was endeavouring to sublet its leasehold. Nothing came of its endeavours.

6 The closing down of the supermarket adversely affected the other tenants in the shopping centre, and by 22nd November 1963 (a date whose relevance will appear later) three of those tenants had moved out. The shopping centre began to take on a "ghost-town" appearance and suffered from petty vandalism. On 13th April 1962, following the closing down of the supermarket, the appellant's solicitors wrote to the respondent, again drawing attention to cl. 9 of the lease, complaining that the appellant was suffering damage and advising that they would seek compliance to have the business reopened or would claim damages. The appellant learned in July 1962 that the respondent was removing fixtures, and its solicitors wrote in objection on 11th July 1962, relying on cl. 9 and on the covenant in cl. 10(a) permitting removal if the tenant is not in default. The letter threatened resort to an injunction unless the removal was halted.

7 The action, out of which this appeal arises, was commenced on 16th July 1962, and an interlocutory injunction was sought but refused. Rent was paid by the respondent to June 1963. The statement of claim, which was delivered on 31st May 1963, asked for a declaration that the lease was binding upon the respondent, asked for a decree of specific performance and for a mandatory order and an injunction, and also sought damages. The respondent delivered a defence and counter-claim on 12th September 1963. Paragraph 8 of the counter-claim said flatly: "The Defendant hereby repudiates the said agreement dated August 19, 1960". As a result of this repudiation, the appellant's solicitors wrote to the respondent's solicitors on 22nd November 1963 (a date mentioned earlier in these reasons) in these terms:

> Dear Sirs:
>
> *Re: Highway Properties Limited and Kelly Douglas & Co. Ltd.*
>
> This is to advise you that in view of your pleadings, our client takes the position that your client has repudiated the lease in question.
>
> Our client, therefore, intends to take possession of the premises and will attempt to lease these upon the same terms and conditions as set out in the lease of the 19th of August, 1960.
>
> We would further advise you that our client intends to hold your client responsible for any damages suffered by them as a result of your client's breach and wrongful repudiation of the said lease.

8 Following this letter the appellant took possession of the supermarket premises and attempted, without success, to relet them for the unexpired term of the lease of the respondent. Subsequently, the appellant subdivided the premises into three stores which were eventually rented, two under a lease of 1st March 1965, and the third under a lease of 1st November 1965. At the opening of trial on 29th November 1966 the appellant obtained leave to amend its statement of claim. The amendment referred to the respondent's rescission of the agreement thereunder in accordance with the letter of 22nd November 1963 and claimed damages not only for loss suffered to the date of the so-called rescission but also, and mainly, for prospective loss resulting from the respondent's failure to carry on a supermarket business in the shopping centre for the full term of the lease.

9 The theory upon which the appellant claimed damages was rejected by the trial Judge, Macdonald J., 60 W.W.R. 193, and by the majority of the Court of Appeal, 66 W.W.R. 705, 1 D.L.R. (3d) 626, Davey C.J.B.C. dissenting. The holding both at trial and on appeal was that there had been a surrender of the lease by reason of the repudiation and the taking of possession by the appellant; that the principles enunciated in the *Goldhar* case were applicable; that the lease and its covenants ceased to exist with the surrender; and that the appellant could recover only for breaches occurring to the date of surrender. The damages on this footing totalled $14,256.38, composed of five months' rent; the decline in rental income in 1962 and in 1963 to the date of surrender by reason of the closing of other stores; a portion of the taxes payable for 1963; a sum for increased insurance premiums for 1963; and a portion of maintenance costs for 1963 to the date of surrender.

10 It is common ground, as appears from the reasons of Davey C.J.B.C. in the Court of Appeal, that if it should be determined that damages must be assessed on the basis claimed by the appellant, the assessment should be remitted to the trial Judge to be made on the evidence adduced before him.

11 I approach the legal issue involved in this appeal by acknowledging the continuity of common-law principle that a lease of land for a term of years under which possession is taken creates an estate in the land, and also the relation of landlord and tenant, to which the common law attaches various incidents despite the silence of the document thereon. For the purposes of the present case, no distinction need be drawn between a written lease and a written agreement for a lease. Although by covenants or by contractual terms, the parties may add to, or modify, or subtract from the common-law incidents, and, indeed, may overwhelm them as well as the leasehold estate by commercial or business considerations which represent the dominant features of the transaction, the "estate" element has resisted displacement as the pivotal factor under the common law, at least as understood and administered in this country.

12 There has, however, been some questioning of this persistent ascendancy of a concept that antedated the development of the law of contracts in English law and has been transformed in its social and economic aspects by urban living conditions and by commercial practice. The judgments in the House of Lords in *Cricklewood Property & Investment Trust Ltd. v. Leighton's Investment Trust Ltd.*, [1945] A.C. 221, [1945] 1 All E.R. 252, are illustrative. Changes in various states of the United States have been quite pronounced, as is evident from 1 American Law of Property, 1952, para. 3.11.

13 In the various common-law provinces, standard contractual terms (reflected, for example, in Short Forms of Leases Acts) and, to a degree, legislation, have superseded the common law of landlord and tenant; for example, in prescribing for payment of rent in advance; in providing for re-entry for non-payment of rent or breaches of other covenants exacted from the tenant; in modifying the absoluteness of covenants not to assign or sublet without leave; and in blunting peremptory rights of termination or forfeiture. The contractual emphasis, even when reinforced by commercial clauses testifying to the paramount business considerations in a lease of land, has hitherto stopped short of full recognition of its remedial concomitants, as, for example, the principle of anticipatory breach and the principle governing relief upon repudiation. I note that this Court had no hesitation in applying the doctrine of anticipatory breach to a contract for the sale of land, even to the point of allowing an immediate suit for specific performance (but, of course, at the time fixed for completion): see *Kloepfer Wholesale Hardware & Automotive Co. v. Roy*, [1952] 2 S.C.R. 465, [1952] 3 D.L.R. 705. I think it is equally open to consider its application to a contractual lease, although the lease is partly executed. Its anticipatory feature lies, of course, in the fact that instalments of rent are payable for future periods, and repudiation of the lease raises the question whether an immediate remedy covering the loss of such rent and of other advantages extending over the unexpired term of the lease may be pursued notwithstanding that the estate in the land may have been terminated.

14 The developed case law has recognized three mutually exclusive courses that a landlord may take where a tenant is in fundamental breach of the lease or has repudiated it entirely, as was the case here. He may do nothing to alter the relationship of landlord and tenant, but simply insist on performance of the terms and sue for rent or damages on the footing that the lease remains in force. Second, he may elect to terminate the lease, retaining of course the right to sue for rent accrued due, or for damages to the date of termination for previous breaches of covenant. Third, he may advise the tenant that he proposes to re-let the property on the tenant's account and enter into possession on that basis. Counsel for the appellant, in effect, suggests a fourth alternative, namely, that the landlord may elect to terminate the lease but with notice to the defaulting tenant that damages will be claimed on the footing of a present recovery of damages for losing the benefit of the lease over its unexpired term. One element of such damages would be, of course, the present value of the unpaid future rent for the unexpired period of the lease less the actual rental value of the premises for that period. Another element would be the loss, so far as provable, resulting from the repudiation of cl. 9. I say no more about the elements of damages here in view of what has been agreed to in that connection by the parties.

15 There is no need to discuss either the first or second of the alternatives mentioned above other than to say, in respect of the second, that it assumes a situation where no prospective damages could be proved to warrant any claim for them,

or even to warrant taking the third alternative. I wish, however, to examine the underpinnings and implications of the third course because they have a decided bearing on whether the additional step proposed by counsel for the appellant should be taken in this case.

16 Where repudiation occurs in respect of a business contract (not involving any estate in land), the innocent party has an election to terminate the contract which, if exercised, results in its discharge pro tanto when the election is made and communicated to the wrongdoer. (I agree with the opinion of such text writers as Cheshire and Fifoot, The Law of Contract, 7th ed., 1969, p. 535, that it is misleading to speak of the result as rescission when there is no retrospective cancellation ab initio involved.) Termination in such circumstances does not preclude a right to damages for prospective loss as well as for accrued loss.

17 A parallel situation of repudiation in the case of a lease has generally been considered in the language of and under the principles of surrender, specifically of surrender by operation of law or implied surrender. It is said to result when, upon the material breach or repudiation of a lease, the innocent party does an act inconsistent with the continued existence of that lease. The *Goldhar* case applied the doctrine where, upon a tenant's repudiation of a lease, the landlord re-let the premises. The further consequence of this was said to be not only the termination of the estate in the land but also the obliteration of all the terms in the document of lease, at least so far as it was sought to support a claim thereon for prospective loss.

18 The rule of surrender by operation of law, and the consequences of the rule for a claim of prospective loss, are said to rise above any intention of the party whose act results in the surrender, so long as the act unequivocally makes it inconsistent for the lease to survive. Even if this be a correct statement of the law, I do not think it would apply to a case where both parties evidenced their intention in the lease itself to recognize a right of action for prospective loss upon a repudiation of the lease, although it be followed by termination of the estate. There are cases in other jurisdictions which have recognized the validity of covenants to this effect: see 11 Williston on Contracts (Jaeger) 3rd ed., 1968, para. 1403. One of the terms of the lease in *Bel-Boys Buildings Ltd. et al. v. Clark* (1967), 59 W.W.R. 641, 62 D.L.R. (2d) 233, was in the nature of such a covenant applicable to a guarantor, and the dissenting judgment of Allen J.A. of the Alberta Appellate Division recognized the enforceability of the guarantee notwithstanding the termination of the obligation to pay rent. I should add that the reasons proceeded on the ground that the guarantee obligation arose before there had been an effective surrender.

19 English and Canadian case law has given standing to a limitation on the operation of surrender, although there is repudiation and repossession, if the landlord, before repossessing, notifies the defaulting tenant that he is doing so with a view to re-letting on the tenant's account. No such notice was given in the *Goldhar* case; and although it was argued in the present case that the letter of 22nd November 1963 asserted that position, neither the trial Judge nor the Court of Appeal accepted the argument. I agree that the letter is not sufficiently explicit to that end, but I would think that the recognition of such a modifying principle would suggest a readiness to imply that a re-letting was on the repudiating tenant's behalf, thus protecting the landlord's rights under the lease and at the same time mitigating the liability for unpaid rent. Some of the views expressed in *Oastler v. Henderson* (1877), 2 Q.B.D. 575, point to a disposition to such an implication; and there is authority in the United States to that effect: see 11 Williston on Contracts, supra. I know that under the present case law the landlord is not under a duty of mitigation, but mitigation is in fact involved where there is a re-letting on the tenant's account.

20 Since the limiting principle under discussion is based on a unilateral assertion of unauthorized agency, I find it difficult to reconcile with the dogmatic application of surrender irrespective of intention. One of the earliest of the cases in England which gave expression to this limiting principle was *Walls v. Atcheson* (1826), 3 Bing. 462, 130 E.R. 591. I read it as indicating that a landlord upon an abandonment or repudiation of a lease by his tenant may qualify his re-entry to make it clear that he is not foregoing his right to insist on continuation of the tenant's obligation to pay rent. Since rent was regarded, at common law, as issuing out of the land, it would be logical to conclude that it ceased if the estate in the land ceased. But I do not think that it must follow that an election to terminate the estate as a result of

the repudiation of a lease should inevitably mean an end to all covenants therein to the point of denying prospective remedial relief in damages.

21 I appreciate, however, that this principle of denial has been carried into modern doctrine from the older cases that were founded on the relation of surrender to a continuing claim for rent. Woodfall on Landlord and Tenant, 1968, vol. 1, 27th ed., p. 869 cites only the *Goldhar* case for the proposition, but it is evident from other English cases such as *Richmond v. Savill*, [1926] 2 K.B. 530, that the English law is to the same effect. I have the impression from a reading of the cases that the glide into this principle was assisted by translating repudiation or abandonment into an "offer" of surrender and by compounding this legal solecism by a further lapse into the language of rescission.

22 Nothing that was decided by this Court in *Attorney General of Saskatchewan v. Whiteshore Salt & Chemical Co. Ltd. et al.*, [1955] S.C.R. 43, [1955] 1 D.L.R. 241, bears on the issues now before it. That case was concerned with whether certain unexpired mining leases of Saskatchewan land, granted under federal authority before the 1930 transfer to Saskatchewan of its natural resources by Canada, must be taken to have been surrendered when in 1931 the leases were replaced by others granted by the province, these being in turn replaced in 1937. On the answer to this question depended the liability of the lessees to increased royalties prescribed under provincial law. If there was no surrender, the lessees were protected by a provision of the Natural Resources Agreement of 1930. Kellock J., who spoke for the majority, was not addressing himself to any issue of damages such as is involved here when he referred generally to the proposition that on a surrender "the lease is gone and the rent is also gone" (a proposition which brooks no disagreement); or when he referred to *Richmond v. Savill*, supra, as standing for the principle that the lessee remains liable for rent accrued due or breaches of covenant committed prior to surrender. These observations were unnecessary for the determination of the question before him, and I do not regard them in any event as controlling for the present case.

23 As long ago as 1906, the High Court of Australia in *Buchanan v. Byrnes* (1906), 3 C.L.R. 704, held that upon an abandonment by a tenant, in breach of covenant, of the hotel property which he had leased, the landlord was entitled to claim damages over the unexpired term of the lease notwithstanding a surrender. It is coincidence that the lease in that case was for 15 years and that it also included a covenant by the tenant, similar to the covenant here, to carry on the business fo which the lease was given, for the full term of the tenancy. I quote two passages from the various reasons for judgment, one from those of Griffith C.J. and the second from those of Barton J., as follows (found, respectively, at pp. 714 and 719):

> In this case he covenanted to carry on [the business] for fifteen years, and on 30th June he not only left the place, but he did so under such circumstances that he could not carry it on, and he sold the funiture. That was as complete a breach of the covenant to carry on the business as it was possible for him to commit, and under these circumstances the plaintiff had at once a complete cause of action against him. He was entitled to bring an action forthwith for the breach of that covenant, and he was entitled to such damages as would properly flow from such a breach of covenant. The surrender, therefore, if accepted at all, took place after breach, and the defence is not proved ...
>
> It must not be forgotten that a right of action had arisen on the termination of the correspondence on the 28th June, as the defendant had given distinct notice of his intention not to perform his covenant. There was at that time a renunciation which, at the plaintiff's option, amounted to a breach of the covenants that throughout the term he would carry on a licensed victualler's business upon the premises and keep them open and in use as an inn, &c., and of the covenant not to do anything which might entail forfeiture of the licence (*Licensing Act* 1885, sec. 101), as well as of the subsidiary covenants. The plaintiff was then entitled to claim in an immediate action, prospectively, such damages as would be caused by a breach at the appointed time, subject to any circumstances which might operate in mitigation of damages: *Leake on Contracts*, 4th ed., 617-618, and cases there cited, especially *Hochester v. Delatour* (1853), 2 E. & B. 678, 118 E.R. 922, and *Johnstone v. Milling* (1886), 16 Q.B.D. 460. But it is said that the conduct of the plaintiff in resuming possession under the circumstances estops him from suing upon the covenants. I must not be taken to hold that it has that effect as to the covenant to pay rent. But, however that may be, can it estop him as to the other covenants which relate to the keeping the premises as an inn throughout the term, and the doing of the other things necessary for that purpose? Conduct, to constitute an estoppel, must have caused another to believe in

> the existence of a certain state of things, and have induced him to act on that belief so as to alter his own position. How can that be said to be the effect of the plaintiff's conduct, when the act of the defendant, so far from having been induced by it, has preceded it? In my judgment the doctrine of estoppel cannot be applied against the plaintiff, and I am driven to the conclusion that the learned Judge who tried the case, and who held that the plaintiff was bound by estoppel, has based his judgment on facts which do not entitle a Court to apply that doctrine.

24 I note that *Buchanan v. Byrnes* was applied a few years ago by the Supreme Court of Western Australia in *Hughes v. N.L.S. Pty. Ltd.*, [1966] W.A.R. 100.

25 The approach of the High Court of Australia commends itself to me, cutting through, as it does, artificial barriers to relief that have resulted from overextension of the doctrine of surrender in its relation to rent. Although it is correct to say that repudiation by the tenant gives the landlord at that time a choice between holding the tenant to the lease or terminating it, yet at the same time a right of action for damages then arises; and the election to insist on the lease or to refuse further performance (and thus bring it to an end) goes simply to the measure and range of damages. I see no logic in a conclusion that, by electing to terminate, the landlord has limited the damages that he may then claim to the same scale that would result if he had elected to keep the lease alive.

26 What is apparently the majority American view is to the same effect as the view taken in Australia and that I would take: see 4 Corbin on Contracts, 1951, para. 986, p. 955. The American Law of Property, 1952, vol. 1, pp. 203-4, states that "If the lessee abandons the premises and refuses to pay rent, the cases quite generally hold, in accordance with the doctrine of anticipatory breach, that the lessor may sue for complete damages without waiting until the end of the term"; and I may add that, under the case law, this is so at least where the suit is for damages and not for rent as such.

27 There are some general considerations that support the view that I would take. It is no longer sensible to pretend that a commercial lease, such as the one before this Court, is simply a conveyance and not also a contract. It is equally untenable to persist in denying resort to the full armoury of remedies ordinarily available to redress repudiation of covenants, merely because the covenants may be associated with an estate in land. Finally, there is merit here as in other situations in avoiding multiplicity of actions that may otherwise be a concomitant of insistence that a landlord engage in instalment litigation against a repudiating tenant.

28 Lest there be any doubt on the point, cl. 5(a) of the lease (previously referred to in these reasons) does not preclude the claim made herein for prospective damages. The landlord did not invoke the clause, and hence no question arises of an irrevocable election to rely on it.

29 I would, accordingly, allow his appeal, with costs to the appellant throughout, and remit the case to the trial Judge for assessment of damages. It follows that I would overrule the *Goldhar* case.

End of Document

TAB 10

Most Negative Treatment: Reversed
Most Recent Reversed: Crystalline Investments Ltd. v. Domgroup Ltd. | 2002 CarswellOnt 705, 27 B.L.R. (3d) 102, 49 R.P.R. (3d) 171, 31 C.B.R. (4th) 225, 112 A.C.W.S. (3d) 355, 156 O.A.C. 392, 58 O.R. (3d) 549, 210 D.L.R. (4th) 659, [2002] O.J. No. 883 | (Ont. C.A., Mar 6, 2002)

2001 CarswellOnt 601
Ontario Superior Court of Justice

Crystalline Investments Ltd. v. Domgroup Ltd.

2001 CarswellOnt 601, [2001] O.J. No. 736, [2001] O.T.C. 142,
103 A.C.W.S. (3d) 904, 31 C.B.R. (4th) 216, 39 R.P.R. (3d) 49

Crystalline Investments Limited, Plaintiff/ Respondent and Domgroup Ltd., Defendant/Applicant

Burnac Leaseholds Limited, Plaintiff/Respondent and Domgroup Ltd., Defendant/Applicant

Trafford J.

Heard: March 1, 2001
Judgment: March 5, 2001 *
Docket: 97-CU-117965, 97-CU-117966

Counsel: *Sharon Addison*, for Plaintiffs/Respondents
Harold S. Springer, *David Stevens*, for Defendant/Applicant

Subject: Property; Insolvency
Related Abridgment Classifications
Bankruptcy and insolvency
X Priorities of claims
X.4 Claims by landlord
X.4.h Assignment of lease
Real property
V Landlord and tenant
V.11 Assignment of lease
V.11.a Nature and effect of assignment
Headnote
Bankruptcy --- Priorities of claims — Claims by landlord — Assignment of lease
Defendant tenant leased premises from plaintiff landlords — Leases each included clause stipulating that tenant was to continue to be bound by lease notwithstanding assignment — Tenant assigned leases to third party — Third party became insolvent and filed proposals under Bankruptcy and Insolvency Act — Proposals were approved by court order — Under proposals, leases were terminated and landlords were paid statutory compensation for damages — Landlords brought actions against tenant for arrears of rent and other damages owing under leases — Tenant brought motions for summary judgment to dismiss actions — Motions granted and actions dismissed — Court-approved termination of leases ended all obligations of all parties to leases — Termination of leases by court rendered assignment clause inoperative — Landlords were informed of trustee's intention to terminate leases and received legal advice — Landlords chose not to exercise right to apply under s. 65.2(2) of Act for declaration that s. 65.2(1) did not apply to leases — Section 65.2(2) of Act provided court with jurisdiction to remove leases as asset of bankrupt estate — Effect of proposal was to fully and

completely terminate leases — Notices of repudiation sought termination of leases and not termination of assignments — Entire lease including assignment clause was terminated by court order in each case — Landlords accepted payments made as total compensation for all damages to which they were entitled under leases — Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, ss. 65.2(1), 65.2(2).

Landlord and tenant --- Assignment of lease — Nature and effect of assignment

Defendant tenant leased premises from plaintiff landlords — Leases each included clause stipulating that tenant was to continue to be bound by lease notwithstanding assignment — Tenant assigned leases to third party — Third party became insolvent and filed proposals under Bankruptcy and Insolvency Act — Proposals were approved by court order — Under proposals, leases were terminated and landlords were paid statutory compensation for damages — Landlords brought actions against tenant for arrears of rent and other damages owing under leases — Tenant brought motions for summary judgment to dismiss actions — Motions granted and actions dismissed — Court-approved termination of leases ended all obligations of all parties to leases — Termination of leases by court rendered assignment clause inoperative — Landlords were informed of trustee's intention to terminate leases and received legal advice — Landlords chose not to exercise right to apply under s. 65.2(2) of Act for declaration that s. 65.2(1) did not apply to leases — Section 65.2(2) of Act provided court with jurisdiction to remove leases as asset of bankrupt estate — Effect of proposal was to fully and completely terminate leases — Notices of repudiation sought termination of leases and not termination of assignments — Entire lease including assignment clause was terminated by court order in each case — Landlords accepted payments made as total compensation for all damages to which they were entitled under leases — Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, ss. 65.2(1), 65.2(2).

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Cosgrove-Moore Bindery Services Ltd., Re, 2000 CarswellOnt 1561, 48 O.R. (3d) 540, 17 C.B.R. (4th) 205 (Ont. S.C.J. [Commercial List]) — referred to

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Down, Re, 2000 BCSC 1148, 80 B.C.L.R. (3d) 28, 189 D.L.R. (4th) 709, 19 C.B.R. (4th) 46 (B.C. S.C.) — referred to

EdperBrascan Corp. v. 117373 Canada Ltd. (2000), 50 O.R. (3d) 425, 9 B.L.R. (3d) 234, 37 R.P.R. (3d) 188 (Ont. S.C.J.) — referred to

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Highway Properties Ltd. v. Kelly, Douglas & Co., [1971] S.C.R. 562, [1972] 2 W.W.R. 28, 17 D.L.R. (3d) 710 (S.C.C.) — referred to

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

Pt. III — referred to

s. 62(3) — considered

s. 65.2 [en. 1992, c. 27, s. 30] — considered

s. 65.2(1) [en. 1992, c. 27, s. 30] — considered

s. 65.2(2) [en. 1992, c. 27, s. 30] — considered

s. 65.2(3) [en. 1992, c. 27, s. 30] — considered

s. 65.2(4) [en. 1992, c. 27, s. 30] — referred to

s. 179 — considered

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MOTIONS by tenant for summary judgment to dismiss landlords' actions for rent arrears and other damages.

***Trafford J.*:**

Introduction

1 This is a motion for summary judgment by Domgroup Limited ("Domgroup") in two actions by Crystalline Investments Limited ("Crystalline") and Burnac Leaseholds Limited ("Burnac"). In these actions the plaintiffs claim arrears of rent and other damages alleged to be owing under two shopping centre leases. The leases were entered into by a predecessor of Domgroup and were assigned by it to a third party. The assignee became insolvent and filed a proposal under the *Bankruptcy and Insolvency Act*, R.S. 1992, c. 27 (the "1992 Act"). The proposal was approved by an order of the Court of Queen's Bench of New Brunswick. Under the proposal the leases were terminated and the plaintiffs were paid statutory compensation for their damages. In this motion, Domgroup takes the position that the actions cannot succeed as a matter of law.

2 Although there are no material facts in dispute between the parties, it is helpful to elaborate upon them before giving the ruling of the Court.

The Circumstances of the Case

3 By a lease dated April 30, 1979 Dominion Stores Limited, the predecessor of Domgroup, leased from Crystalline premises located in the Northumberland Square Shopping Centre in Douglastown, New Brunswick. The term of the lease was for 25 years ending on March 31, 2004. The lease contained the following provision:

> Notwithstanding any assignment or sublease the lessee shall remain fully liable under this lease and shall not be released from performing any of its covenants, obligations or agreements in this lease and shall continue to be bound by this lease.

By an assignment dated May 25, 1995 Dominion Stores Limited assigned the lease to Coastal Foods Limited. It subsequently amalgamated with The Food Group Inc. On or about February 11, 1994 The Food Group Limited filed

a Notice of Intention to make a proposal pursuant to Part III of the 1992 Act. On February 18, 1994 Peat Marwick Thorne Inc., acting as the proposal trustee of The Food Group Inc., delivered a Notice of Repudiation of the lease to Crystalline pursuant to s. 65.2 of the 1992 Act. The Notice of Repudiation stated, in part, as follows:

> a) The repudiation of the lease will become effective on the 31 st day of March, 1994 at 11:59 PM local time.
>
> b) Before the repudiation becomes effective, you may apply to the court, within 15 days after the day this notice is received, for a declaration that subsection 65.2(1) of the *Bankruptcy and Insolvency Act* does not apply in respect of the lease mentioned above.
>
> c) By virtue of subsection 65.2(3) of the *Bankruptcy and Insolvency Act*, a proposal filed by the undersigned commercial tenant must provide for payment to you immediately after court approval of the proposal, of compensation equal to the lesser of
>
> > a) an amount equal to six months rent under the lease, and
> >
> > b) the rent for the remainder of the lease, from the date on which the repudiation takes effect.
>
> d) As detailed in the proposal, The Food Group Inc. or the Trustee intends to continue to occupy the premises for the period from the date of the notice of intention until a date not later than March 31, 1994, and the payment provided for under Part 6 of this notice shall be considered compensation for all damages and occupation rent and the landlord shall not have any right to vote a claim in respect of accelerated rent, damages arising out of the repudiation or the compensation provided for herein (section 65.2(4)).

Crystalline did not apply to the Court to challenge the repudiation of the lease as it was entitled to under the 1992 Act. By a letter dated March 16, 1994 Peat Marwick Thorne Inc. undertook to pay Crystalline the amount to which it was entitled under the 1992 Act subject to confirmation that Crystalline would not object to the application for approval of the proposal by the Court. Crystalline returned a signed copy of the letter and confirmed, in accordance with the terms of the letter, that it would not take any action to object to the application for approval of the proposal. This was confirmed by counsel for Crystalline. The proposal stated that a number of leases, including the one with Crystalline, would be terminated in accordance with s. 65.2 of the 1992 Act with effect on March 31, 1994. This proposal was approved by the Court of Queen's Bench for New Brunswick in Bankruptcy by order dated March 18, 1994. Pursuant to that order Crystalline received and accepted payment in the amount of $131,154.54 in respect of the compensation payable under s. 65.2(3) of the 1992 Act for the termination of the lease. The lease was terminated effective March 31, 1994. However, on January 20, 1995 Crystalline sent to Domgroup a letter in which it referred to the assignment clause and alleged that Domgroup was in default of payment of rent due under the lease. The letter expressed an intention to seek relief through the Courts if Domgroup did not remedy the alleged default. The letter did not acknowledge the termination of the lease as of March 31, 1994.

4 The circumstances surrounding the lease with Burnac are more or less similar. Let me elaborate on them. By lease dated April 24, 1980 Dominion Stores Limited leased from Burnac premises located in the Chaleur Centre in Bathurst, New Brunswick. This lease had a term of 25 years ending on March 14, 2005. It also contained the assignment clause. By an agreement dated March 25, 1985 Dominion Stores Limited assigned this lease to Coastal Foods Limited. It, as I indicated earlier, subsequently amalgamated with The Food Group Inc. On February 11, 1994 The Food Group Inc. filed a proposal for bankruptcy. On February 18, 1994 Peat Marwick Thorne Inc. delivered a Notice of Repudiation of this lease to Burnac pursuant to s. 65.2 of the 1992 Act. The Notice of Repudiation stated, in part, as follows:

> a) The repudiation of the lease will become effective on the 31 st day of March, 1994 at 11:59 PM local time.

b) Before the repudiation becomes effective, you may apply to the court, within 15 days after the day this notice is received, for a declaration that subsection 65.2(1) of the *Bankruptcy and Insolvency Act* does not apply in respect of the lease mentioned above.

c) By virtue of subsection 65.2(3) of the *Bankruptcy and Insolvency Act*, a proposal filed by the undersigned commercial tenant must provide for payment to you immediately after court approval of the proposal, of compensation equal to the lesser of

a) an amount equal to six months rent under the lease, and

b) the rent for the remainder of the lease, from the date on which the repudiation takes effect.

d) As detailed in the proposal, The Food Group Inc. or the Trustee intends to continue to occupy the premises for the period from the date of the notice of intention until a date not later than March 31, 1994, and the payment provided for under Part 6 of this notice shall be considered compensation for all damages and occupation rent and the landlord shall not have any right to vote a claim in respect of accelerated rent, damages arising out of the repudiation or the compensation provided for herein (section 65.2(4)).

Burnac also did not apply to the Court to challenge the repudiation of this lease as it was entitled to under the 1992 Act. It executed and returned the trustee's letter of March 16, 1994 confirming its agreement, in accordance with the terms of the letter, not to take any action to object to the application for approval of the proposal. It, too, was represented by counsel in making this decision. The proposal provided for termination of the lease in accordance with s. 65.2 of the 1992 Act effective March 31, 1994. It was approved by the Court. On March 24, 1994 Burnac received payment in the amount of $173,704.39 as compensation under s. 65.2(3) of the 1992 Act for the termination of the lease. The lease was terminated effective March 31, 1994. Again, on January 20, 1995 Domgroup received a letter from Burnac referring to the assignment clause and claiming that Domgroup was in default of payment of rent under the lease. It further provided that should Domgroup fail to remedy the alleged default relief would be sought in Court. The letter did not acknowledge the termination of the lease as of March 31, 1994.

The Legal Issue to be Determined by the Court

5 Counsel before this Court agree that the legal issue to be determined in the circumstances of these cases may be stated as follows:

> Is a landlord, following the Court-approved termination of a commercial lease under s. 65.2 of the 1992 Act and following acceptance of the compensation provided for by the statutory code, entitled to arrears of rent, or for damages, in respect of the unexpired term of the terminated lease as against the pre-proposal assignor of the lease?

6 They also agree that the legal principles governing a motion for summary judgment have been concisely stated by the Supreme Court of Canada in *Guarantee Co. of North America v. Gordon Capital Corp.* (1999), 178 D.L.R. (4th) 1 (S.C.C.), at pp. 10-11:

> The appropriate test to be applied on a motion for summary judgment is satisfied when the applicant has shown that there is no genuine issue of material fact requiring trial, and therefore summary judgment is a proper question for consideration by the court.... Once the moving party has made this showing, the responding party must then establish his claim as being one with a real chance of success.

Summary judgment may be available in cases involving the interpretation of contracts and of statutes, as long as there is no dispute as to the material facts of the case. See Rule 20, *EdperBrascan Corp. v. 117373 Canada Ltd.* (2000), 50 O.R. (3d) 425 (Ont. S.C.J.) and *Aguonie v. Galion Solid Waste Material Inc.* (1998), 38 O.R. (3d) 161 (Ont. C.A.).

The History of the Pertinent Provisions of the Bankruptcy Legislation in Canada

7 The determination of this question requires me to make a brief reference to the historical context of a number of the pertinent provisions of the 1992 Act.

8 Section 65.2 of the 1992 Act contained a statutory code for the repudiation of commercial leases by an insolvent person. Subsection 1 of this provision stated that, subject to subsection 2, an insolvent person who was a commercial tenant could repudiate the lease on giving 30 days notice to the landlord in a prescribed manner. Under subsection 2 the landlord was given the right to challenge the repudiation of the lease. It provided that, within 15 days of being given Notice of Repudiation, the landlord could apply to the Court for a declaration that subsection 1 did not apply to the lease. The landlord's right to challenge the repudiation of a lease was a significant one. Upon application, subsection 2 required the Court to make the declaration that subsection 1 did not apply to the lease unless the insolvent person could meet the test specified in subsection 2. The test focused on the viability of the proposal without the repudiation of the lease. Section 65.2 of the 1992 Act went on to establish compensation for a repudiation of a lease. Subsection 3 provided that when a lease was repudiated, a proposal filed by the insolvent person must provide for payment to the landlord of compensation equal to the lesser of six months rent under the lease or the rent for the remainder of the lease.

9 The provisions of the 1992 Act are significantly different than the present legislation. The primary difference is that the present legislation, s. 65.2(1), permits an insolvent person to disclaim a commercial lease as opposed to repudiate a commercial lease under the 1992 Act. The legal effect of the disclaimer of a lease by a trustee in bankruptcy is that all of the rights and obligations inherited by the trustee from the bankrupt tenant are wholly at an end. See *Cummer-Yonge Investments Ltd. v. Fagot*, [1965] 2 O.R. 152 (Ont. H.C.) for an interpretation of the notion of disclaimer in a different context. However, a disclaimer by the trustee of a bankrupt assignee does not terminate an assigned lease. Where a lease has been assigned, the legal effect of a disclaimer of that lease is that the unexpired term of the disclaimed lease reverts to the assignor of the lease. See *Transco Mills Ltd. v. Percan Enterprises Ltd.* (1993), 29 R.P.R. (2d) 235 (B.C. C.A.), at pp. 243-245. The legal significance of the change from "repudiation" to "disclaimer" is, in effect, the issue to be determined by this Court.

The Position of the Respondents

10 The position of the respondents is that where a lessee assigns his term, the assignment destroys the privity of estate between him and the lessor but not the privity of contract so that the lessee remains liable upon the express covenants in the lease. Reference was made to *Barmond Builders Ltd. v. Mark 3 Investment Corp.* (1993), 32 R.P.R. (2d) 149 (Ont. Gen. Div.), at 158. The trustee in bankruptcy of the assignee of the lease cannot affect the contractual rights between the landlord and the assignor. Reference was made to *Daniel Ignat Kaneff Holdings Ltd. v. National Trust Co.* (1988), 68 C.B.R. (N.S.) 134 (Ont. S.C.). In the submission of the respondents, the fact of bankruptcy only affects the rights and obligations of parties *vis a vis* the bankrupt person. It does not affect the rights and obligations of parties arising out of a contract to which the bankrupt is not privy. Reference was made to *Transco Mills Ltd. v. Percan Enterprises Ltd.*, *supra*, at p. 320 and *Glenview Corp. v. Lavolpicella* (1997), 12 R.P.R. (3d) 74 (Ont. Gen. Div.), at 77. These submissions were made in the context of a further reference to s. 62(3) of the 1985 Act which provided that the acceptance of a proposal by a creditor did not release any person who would not be released under the Act by the discharge of the debtor. A further contextual reference was made to s. 179 of the 1985 Act which provides that an order of discharge does not release a person who at the date of bankruptcy was a partner or co-trustee with the bankrupt or was jointly bound or had made a joint contract with the bankrupt or a person who was surety or in the nature of a surety for the bankrupt. Those provisions, it was said by counsel on behalf of the respondents, are still in the bankruptcy legislation and were in the 1992 Act. In other words, if a liability is joint and several, the release of one party through the operation of law from his/her personal obligation to pay does not discharge the debt. The remaining party continues to be liable on the basis of contract. These, then, were the submissions of the respondents.

The Analysis of the Court

11 At common law, when a repudiation of a contract, including a lease, is accepted by another party, that party may be entitled to sue for damages notwithstanding that the contract, or lease, itself has come to an end. See *Highway Properties Ltd. v. Kelly, Douglas & Co.* (1971), 17 D.L.R. (3d) 710 (S.C.C.), at pp. 720-721. However, in my opinion, this principle does not apply in the context of the 1992 Act. See *Vrablik, Re* (1993), 17 C.B.R. (3d) 152 (Ont. Bktcy.), at pp. 158-159 and *Peat Marwick Thorne Inc. v. Natco Trading Corp.* (1995), 22 O.R. (3d) 727 (Ont. Gen. Div. [Commercial List]) at p. 732. The payments received by the plaintiffs from the trustee following the repudiation of the leases amounted to the entire compensation to which they were entitled from any party, including the defendant, under the leases. In other words, the Court-approved termination of the leases ended all obligations of all parties to the leases. The termination of the leases by the Court rendered the assignment clause in them inoperative. This conclusion does not mean that the plaintiffs-respondents have been unfairly dealt with in the circumstances of these cases. They had the right, after receiving the Notice of Repudiation, to challenge the repudiation of the leases and the proposal. The Notice of Repudiation clearly brought to their attention, especially with the assistance of their counsel, an intention on the part of the trustee to terminate the leases. They chose not to invoke the jurisdiction of the Court. The jurisdiction of the Court under s. 65.2(2) of the 1992 Act in my opinion changes the legal significance of the sections and the authorities relied upon by the respondents in these motions. Parliament provided to the Court a jurisdiction to, in effect, remove the leases as an asset of the bankrupt estate. It was open to the plaintiffs-respondents to seek to preserve the liability of Domgroup Limited under the leases. They could have applied for a declaration under s. 65.2(2) of the 1992 Act that subsection 1 did not apply to these leases. Had they made such an application, the onus would have been on the trustee to satisfy the Court that the proposal would not have been viable without the repudiation of the leases and the related ones. If the application had been successful, the leases would not have been terminated and the plaintiffs would have preserved their right to look to Domgroup Limited under the assignment clause in each lease. In such circumstances, they would not have been entitled to the compensation prescribed by the remaining parts of s. 65.2 of the 1992 Act.

12 The fact that the Court-approved termination ended all obligations under the lease is not an unusual circumstance in the bankruptcy context. In *Cummer-Yonge Investments Ltd. v. Fagot, supra*, Gale, C.J.H.C. held that, when the trustee in bankruptcy disclaimed the interest of the tenant in the lease, all of the rights and obligations which the trustee inherited from the tenant were wholly at end. Therefore, the action by a commercial landlord against the guarantors of the bankrupt tenant for arrears of rents did not succeed. The Court held that because there were no longer any covenants which required the tenant to perform, the guarantee became inoperative. See also *Titan Warehouse Club Inc. (Trustee of) v. Glenview Corp.* (1988), 67 C.B.R. (N.S.) 204 (Ont. H.C.) as affirmed by the Court of Appeal at (1989), 75 C.B.R. (N.S.) 206 (Ont. C.A.) and *Peat Marwick Thorne Inc. v. Natco Trading Corp., supra*, at pp. 728-730. Although it is possible for a landlord to avoid the effect of this jurisprudence through appropriate drafting of a clause in the lease, the clause in this case in my opinion does not succeed. The effect of the proposal, as accepted by the Court, was to fully and completely terminate the leases. The Notice of Repudiation did not seek termination of the assignment of the lease. It sought termination of the lease. There is nothing on the face of the provision of the 1992 Act which would limit the Notice of Repudiation as advocated by counsel for the respondents in this motion.

13 Accordingly, in each case, the entire lease including the assignment clause was terminated by the Court order. There is no basis in law for the claims made against Domgroup Limited. The respondents-plaintiffs accepted the payments made as the total compensation for all damages to which they were entitled under the leases. The scheme of the bankruptcy legislation is to provide a complete and comprehensive code for all matters related to a bankrupt person. See *Cosgrove-Moore Bindery Services Ltd., Re* (2000), 48 O.R. (3d) 540 (Ont. S.C.J. [Commercial List]) and *Down, Re* (2000), 189 D.L.R. (4th) 709 (B.C. S.C.), at 723. This complete code may affect third parties. See *Cummer-Yonge Investments Ltd. v. Fagot, supra* and *Titan Warehouse Club Inc. (Trustee of) v. Glenview Corp., supra.*

Conclusion

14 The motions for summary judgment succeed. The actions by Crystalline and Burnac against Domgroup Limited are dismissed. Costs to Domgroup Limited on a solicitor-client scale.

Motions granted.

Footnotes

* Reversed 2002 CarswellOnt 705, 31 C.B.R. (4th) 225 (Ont. C.A.).

Most Negative Treatment: Leave to appeal allowed
Most Recent Leave to appeal allowed: Crystalline Investments Ltd. v. Domgroup Ltd. | 2002 CarswellOnt 4282, 2002 CarswellOnt 4283, 307 N.R. 195 (note), 178 O.A.C. 199 (note) | (S.C.C., Dec 12, 2002)

2002 CarswellOnt 705
Ontario Court of Appeal

Crystalline Investments Ltd. v. Domgroup Ltd.

2002 CarswellOnt 705, [2002] O.J. No. 883, 112 A.C.W.S. (3d) 355, 156 O.A.C. 392, 210 D.L.R. (4th) 659, 27 B.L.R. (3d) 102, 31 C.B.R. (4th) 225, 49 R.P.R. (3d) 171, 58 O.R. (3d) 549

Crystalline Investments Limited (Plaintiff / Appellant) and Domgroup Ltd. (Defendant / Respondent)

Burnac Leaseholds Limited (Plaintiff / Appellant) and Domgroup Ltd. (Defendant / Respondent)

Carthy, Weiler, Cronk JJ.A.

Heard: January 10, 2002
Judgment: March 6, 2002
Docket: CA C36097

Proceedings: reversing (2001), 39 R.P.R. (3d) 49 (Ont. S.C.J.)

Counsel: *Peter-Paul E. DuVernet*, for Appellants
Harold S. Springer, *David Stevens*, for Respondent

Subject: Property; Insolvency
Related Abridgment Classifications
Bankruptcy and insolvency
X Priorities of claims
X.4 Claims by landlord
X.4.h Assignment of lease
Real property
V Landlord and tenant
V.11 Assignment of lease
V.11.a Nature and effect of assignment
Headnote
Bankruptcy --- Priorities of claims — Claims by landlord — Assignment of lease
Landlord and tenant entered into long-term lease agreements — Tenant assigned leases to sub-lessee, which subsequently became insolvent, made proposal under Bankruptcy and Insolvency Act, and repudiated leases under s. 65.2 of Act — Landlord was paid compensation equal to six months' rent as set out in Act — Landlord brought actions against tenant for amounts owing under leases — Tenant brought motions for summary judgment to dismiss actions — Motions granted — Landlord appealed — Appeal allowed — Rights as between landlord and original tenant were unaffected by proceedings taken by insolvent sub-lessee under s. 65.2 of Act — To consider that original lease was terminated by repudiation of leases by sub-lessee was counter-intuitive as no benefit was conferred on sub-lessee, and purpose of legislation, which is to provide insolvent party with opportunity to rid itself of lease obligations in order to make viable proposal under Act, was not served — Repudiation under s. 65.2(2) of Act was not equivalent of termination at common law — Hearing as to viability of sublessee's proposal was totally unrelated to rights of landlord against other parties

— Compensation for landlord under s. 65.2 of Act was nominal compared to income stream from long-term lease with solvent original tenant — Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, ss. 65.2, 65.2(2).
Landlord and tenant --- Assignment of lease — Nature and effect of assignment
Landlord and tenant entered into long-term lease agreements — Tenant assigned leases to sub-lessee which subsequently became insolvent, made proposal under Bankruptcy and Insolvency Act, and repudiated leases under s. 65.2 of Act --- Landlord was paid compensation equal to six months' rent as set out in Act — Landlord brought actions against tenant for amounts owing under leases — Tenant brought motions for summary judgment to dismiss actions — Motions granted — Landlord appealed — Appeal allowed — Rights as between landlord and original tenant were unaffected by proceedings taken by insolvent sub-lessee under s. 65.2 of Act — To consider that original lease was terminated by repudiation of leases by sub-lessee was counter-intuitive as no benefit was conferred on sub-lessee, and purpose of legislation, which is to provide insolvent party with opportunity to rid itself of lease obligations in order to make viable proposal under Act, was not served — Repudiation under s. 65.2(2) of Act was not equivalent of termination at common law — Hearing as to viability of sublessee's proposal was totally unrelated to rights of landlord against other parties — Compensation for landlord under s. 65.2 of Act was nominal compared to income stream from long-term lease with solvent original tenant — Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, ss. 65.2, 65.2(2).

Annotation

The trial decision reported at *Crystalline Investments Ltd. v. Domgroup Ltd.*, 2001 CarswellOnt 601, 39 R.P.R. (3d) 49, 31 C.B.R. (4th) 216 (Ont. S.C.J.) caused quite a stir in leasing circles when its reasons were first released. At trial, the Ontario Superior Court released the original tenant cum assignor from its obligations under the lease upon the repudiation of the lease by the tenant under a bankruptcy proposal. To the considerable relief of the leasing community, a unanimous Court of Appeal panel reversed the trial decision in *Crystalline*. Paraphrasing Mr. Justice Carthy, the insolvency of the assignee did not affect and was totally unrelated to the rights of the landlord as against other parties (including the assignor).

Application has already been filed for leave to appeal the Ontario Court of Appeal's decision in Crystalline to the Supreme Court of Canada. This might not be such a bad thing, since it would be a terrific opportunity for the Supreme Court of Canada to provide some long overdue guidance regarding the application of the rule in *Cummer-Yonge Investments Ltd. v. Fagot*, [1965] 2 O.R. 152, 8 C.B.R. (N.S.) 62, 50 D.L.R. (2d) 25, 1965 CarswellOnt 40 (Ont. H.C.), the decision that is at the root of *Crystalline*. There can be no doubt that the rule in *Cummer-Yonge* is complicated, inconsistently applied and often misunderstood. In this regard, *Crystalline* might actually be the perfect appeal platform whence the Supreme Court could take a fresh, "from the bottom up" review of the role of *Cummer-Yonge* in modern Canadian insolvency law.

The rule in *Cummer-Yonge*, distilled to its most basic formulation, provides that a guarantor of the lease obligations of a tenant is excused from all further liability under such guarantee in the event of a bankruptcy of the guaranteed tenant (although most practitioners equate *Cummer-Yonge* with a subsequent disclaimer of the lease by the trustee in bankruptcy, there may be some theory and case law to suggest that the release of the guarantor is actually triggered upon the bankruptcy itself, irrespective of any subsequent disclaimer of the lease - see, generally J. Lem and S. Proniuk, "Goodbye *Cummer-Yonge*: A Review of Modern Developments in the Law Relating to the Liability of Guarantors of Bankrupt Tenants", 1 *Digest of Real Property Law* (December, 1993) at page 432).

For the landlord bar, it was incredible enough that *Cummer-Yonge* seemed to prevent recourse against guarantors for the unpaid rent of bankrupt tenants, but for many landlords, it was simply impossible to suggest that the rule in *Cummer-Yonge* could somehow be extrapolated to release the original, still solvent, tenant (one that happened to have since transferred the leasehold to an assignee) from liability under the lease, when the assignee (not the assignor) subsequently goes bankrupt. This is, however, exactly what the Ontario Superior Court concluded in the trial decision in *Crystalline* (this annotator admits to using the reference to "trial" too liberally since the lower court decision in *Crystalline* was in fact a motion, but it is a useful descriptor to separate the Superior Court decision from that of the Court of Appeal). At trial, the original tenant *cum* assignor was freed of its original covenant precisely because the bankruptcy of the assignee *cum* tenant-in-possession terminated all of the obligations under the lease a là *Cummer-Yonge*, including the obligations of the original tenant under the lease, and notwithstanding that the original tenant was not itself bankrupt.

A great deal of the case law that followed *Cummer-Yonge* focussed, perhaps wrongly, upon the dichotomy between the primary obligor and secondary obligor in respect of lease obligations, such that primary obligors (for instance, indemnifiers) would not be excused from liability under their obligations, but secondary obligators (for instance, guarantors) would be released from liability under their obligations. As a result, much of solicitors' drafting efforts post-*Cummer-Yonge* have emphasized the primary (as opposed to secondary) nature of the intended surety's covenant. Against this backdrop, one can understand how stunning the trial reasons in *Crystalline* were to the real estate leasing bar. If the *Cummer-Yonge* paradigm contemplates liability for sureties with primary liability, how can an assigning tenant, being the original covenantor, be released from liability under *Cummer-Yonge*? After all, the assigning tenant, being the original tenant named on the lease, still has direct privity of contract with the landlord and, one might have thought that if any party would have had primary liability to the landlord, it would have been the original tenant under the lease (readers are reminded that, in *Crystalline*, it was the assignee (not the assignor) that was seeking bankruptcy protection and that there had been no contractual release of the assignor on the assignment).

That said, there is, admittedly, an intuitive attractiveness to the argument that a tenant post-assignment is nothing more than a guarantor of the assignee's obligations under the lease. After all, at least from a lay perspective, an assignor post-assignment does appear, for all intents and purposes, to be just a guarantor. The assignor is not called upon as a tenant on a day-to-day basis, is rarely invoiced on the rent, and merely stands ready to pay the rent if the assignee fails to do so; in effect, like a "guarantor". The Ontario courts have considered the nature of *de facto* guaranties in *Montreal Trust Co. of Canada v. Birmingham Lodge Ltd.*, 46 R.P.R. (2d) 153, 125 D.L.R. (4th) 193, 24 O.R. (3d) 97, 82 O.A.C. 25, 21 B.L.R. (2d) 165, 1995 CarswellOnt 541 (Ont. C.A.) (not quite in the context of *Cummer-Yonge* but certainly in an analogous analysis) and concluded that substance governs over form in considering the nature of such surety obligations. In *Birmingham Lodge*, Mr. Justice Laskin considered the true nature of a surety contract which, on its face, expressly purported to make certain debtors primary obligors:

...The mere inclusion of a phrase such as "the guarantors shall be considered as primarily liable" is not determinative. The court should examine the entire document to ascertain the parties' intention. If the court is uncertain about the correct interpretation, it may resort to extrinsic evidence to assist it. In this case, I would not give effect to the respondent's submission that the appellants are liable as principal debtors. In my view, the parties intended that the appellants would be liable only as guarantors . . .

On the facts in *Crystalline*, the parties arguably did, in fact, treat the assignor as if it were but a guarantor of the lease obligation and, at least on a *Birmingham Lodge* analysis, it certainly would not have been a stretch for the court to find the assignor a guarantor in substance, if not in form.

This "substance over form" argument was applied in *Alberta Financial Consultants Ltd. v. Cuthbert*, 55 A.R. 147, 1984 CarswellAlta 353 (Alta. Q.B.) (albeit again not in the context of *Cummer-Yonge*). In *Alberta Financial*, the issue before the court was whether or not an assignment of lease had to comply with certain statutory form requirements applicable to Alberta guarantees. The Alberta Queen's Bench in *Alberta Financial* concluded that an assignment of lease created a guarantee relationship of sorts, making the assignor of the lease a *de facto* guarantor. Indeed, for some considerable time prior to the trial decision in *Crystalline*, it was common for insolvency practitioners to "manufacture" a legal construct similar to the trial decision in *Crystalline* by invoking, first, *Birmingham Lodge*, then *Alberta Financial*, and immediately thereafter applying *Cummer-Yonge*.

Although the *de facto* guarantor argument developed in *Alberta Financial* is a fascinating theory in its own right, considering *Crystalline* on the narrow issue of whether or not the original covenantor *cum* assignor is but a *de facto* guarantor of the assignee in bankruptcy protection would be entirely to miss the point. Indeed, it is arguable that this very narrow legal issue has already been determined, at least in Ontario. In *Glenview Corp. v. Lavolpicella*, 12 R.P.R. (3d) 74, 1997 CarswellOnt 1137, 28 O.T.C. 234 (Ont. Gen. Div.), the Ontario Court of Justice (General Division) decided that an assignor is *not* a guarantor for the purposes of a *Cummer-Yonge* defence. If the Supreme Court decides to hear the appeal in *Crystalline*, and then limits its disposition of the case to a mere revisitation of *Glenview Corp.*, the Supreme

Court would not only have missed out on the opportunity to deal with *Cummer-Yonge* once and for all, but it is submitted that it would also ultimately be an incomplete analysis of the true issue in *Crystalline*. The *Crystalline* case is arguably the ultimate appeal vehicle for a determination of the rule in *Cummer-Yonge* precisely because the disposition of the "assignor as *de facto* guarantor" issue is not sufficient to settle the matter of the assignor's ultimate liability under *Cummer-Yonge*. That is, even if the Supreme Court upholds *Glenview Corp.* in finding that an assignor is not, in fact, a guarantor, the Supreme Court really still has to determine whether or not the assignor/original covenantor should, *qua* assignor/original covenantor (*i.e.*, in its own right), attract the relief afforded by *Cummer-Yonge*.

For many years, this annotator was firmly ensconced in the ranks of those who considered the rule in *Cummer-Yonge* contrary to commercial reality. Alas, too much exposure to the insolvency bar over the years and a certain discernment that comes with age has brought about, if not an about face, then certainly a serious reconsideration of the proper role of *Cummer-Yonge* in Canadian insolvency law. This reconsideration has been an evolutionary process, fuelled in large part by jurisprudence, up to and including the trial decision in *Crystalline* and the British Columbia Court of Appeal's recent decision in *West Shore Ventures Ltd. v. K.P.N. Holding Ltd.*, 2001 BCCA 279, 2001 CarswellBC 725, 88 B.C.L.R. (3d) 95, 39 R.P.R. (3d) 155, [2001] 5 W.W.R. 209, 198 D.L.R. (4th) 520, 25 C.B.R. (4th) 139, 152 B.C.A.C. 55, 250 W.A.C. 55 (B.C. C.A.), that seemed to persistently stymie drafting attempts to ensure that a landlord could recover all that it contracted for on the insolvency of its tenants.

Developing a consistent theory to explain and guide the application of *Cummer-Yonge* is difficult. First of all, nothing useful can be gained by revisiting the exact reasoning of *Cummer-Yonge* itself. The "obligations" argument adopted by Chief Justice Gale in *Cummer-Yonge* was probably wrong and has received almost universal scholarly and judicial condemnation (for a general discussion of the "obligations" analysis, see Lem and Proniuk, at p. 433), but the result itself (*i.e.* that a guarantor of a tenant is relieved from liability upon the bankruptcy of the tenant) has been repeatedly applied by Canadian courts now for over thirty years. Understanding the judicial longevity of *Cummer-Yonge* requires the reader to look beyond the decision itself.

The Alberta Court of Appeal in *Targa Holdings Ltd. v. Whyte*, [1974] 3 W.W.R. 632, 44 D.L.R. (3d) 209, 21 C.B.R. (N.S.) 54, 1974 CarswellAlta 7 (Alta. C.A.) provides an alternative and "corrected" rationale explaining the result in *Cummer-Yonge*. In *Targa*, Mr. Justice Clement, for the majority, concludes that subsection 14(1)(k) of the federal *Bankruptcy Act*, R.S.C. 1952, c. 14 (*i.e.*, the landlord's preferred claim), when combined with the provisions of the *Landlord's Rights on Bankruptcy Act*, R.S.A. 1970, c. 201 (*i.e.*, the Alberta statute limiting a landlord's provable damage claim in bankruptcy to preferred claim afforded by the federal bankruptcy legislation), together form a complete code governing the maximum extent of landlord recoverability in the event of the bankruptcy of the tenant. Although Ontario does not have a statutory equivalent to Alberta's *Landlord's Rights on Bankruptcy Act*, Mr. Justice Maloney's decision in *Vrablik, Re*, 17 C.B.R. (3d) 152, 1993 CarswellOnt 192 (Ont. Bktcy.) has effectively placed Ontario in a similar regime.

Nor is it particularly productive to criticize the outcome in *Cummer-Yonge* as being somehow inconsistent with the true intent of the parties at the time of the transaction. That is, it is trite to argue that the guarantor, the tenant and the landlord in *Cummer-Yonge* all expected and fully intended that the guarantor would be responsible for payment to the landlord of amounts owing under the lease in the event of non-payment of rent or non-performance of other covenants by the tenant, howsoever caused (including, without limitation and, indeed, especially in the case of, the bankruptcy of the tenant!). A constant critique of *Cummer-Yonge* is that it has always run counter to commercial reality and the true intent of the parties, but, as in many things bankruptcy related, it may just be that the mutual intention of the parties is not a relevant principle in understanding *Cummer-Yonge*. If *Cummer-Yonge* applies because it is a correct application of the federal bankruptcy legislation, then any attempt to "contract-out" of the distribution scheme contemplated by the *Bankruptcy and Insolvency Act*, no matter how mutually agreed upon or how otherwise commercially reasonable the "contracting-out" scheme might be, should arguably be inherently unenforceable as being against public policy. Indeed, in the extreme, many "*ipso facto*" default arrangements designed to shuffle in alternative ownership or liability schemes on the eve of bankruptcy have met with judicial displeasure as "frauds on the bankruptcy law" (see, e.g., *Canadian Imperial Bank of Commerce v. Bramalea Inc.*, 1998 CarswellOnt 1143, 3 C.B.R. (4th) 106 (Ont. Gen. Div. [Commercial List])).

This annotator is not convinced that landlords' attempts to structure their affairs so as to protect their recoveries in the event of tenant bankruptcy quite fall within the category of fiscal arrangements constituting a "fraud on the bankruptcy laws", but nonetheless simply notes that all anti-*Cummer-Yonge* structures, whether they be guaranties, indemnities, letters of credit or otherwise, have the ultimate effect of providing landlords greater recoveries in bankruptcy than the available recoveries prescribed by the *Bankruptcy and Insolvency Act*.

From the insolvency practitioners' perspective, the landlord's right to a reasonable recovery for the economic loss of the tenant and the general sanctity of freedom to contract are wholly subsumed by the integrity of the bankruptcy distribution scheme. On that thinking, the result in *Cummer-Yonge* begins to almost make sense. The Court of Appeal's reasons in the appeal version of *Crystalline* hint at this insolvency practitioner's perspective. The Court of Appeal recognized, firstly, that the *Bankruptcy and Insolvency Act* provides a fixed "statutory scheme" for insolvent persons, then concludes that it is "counterintuitive" to consider the assignor released as a result of the assignee's repudiation of the lease in bankruptcy. The Court of Appeal goes on to explain that, to release the assignor from its obligations under the lease, "confers no benefit on the insolvent [and] . . . does nothing to serve the purpose of the legislation ...". The point being made by the Court of Appeal, consistent with the *ratios* in *Targa* and *Vrablik*, is that the landlord in *Crystalline* had already been paid the full compensation allocable to it under the *Bankruptcy and Insolvency Act*, and the compensation scheme in the statute formed a complete code governing the landlord's entitlement in the event of the bankruptcy protection of a tenant, to the absolute exclusion of any and all other remedies (see, generally, Lem, "*Cummer-Yonge* Revisited: *Subnom*: Spawn of *Cummer-Yonge*", *Six-Minute Real Estate Lawyer*, 2002, Law Society of Upper Canada)(of course, whether the entitlements afforded to landlords under the federal legislation are anywhere approaching economically adequate is an altogether different policy issue for Parliament).

Therein also lies what this annotator believes may be the Achilles' Heel in the Court of Appeal's reasons in *Crystalline*. Although the Court of Appeal correctly identifies the litmus test of whether or not the *Bankruptcy and Insolvency Act* distribution scheme is honoured, it is submitted that the Court of Appeal may have been perhaps premature in concluding that releasing the assignor from its covenant "confers no benefit on the insolvent" or, by implication, that the release of the assignor would not itself be a violation of the sanctity of the *Bankruptcy and Insolvency Act* distribution scheme. True, the point is far from intuitive; at first instance, the assignee does not appear to benefit at all from any release of the assignor and, since the assignor is not itself the insolvent party, its liability to the landlord for the lease obligations would not seem to contravene the statutory recovery scheme in place against the bankrupt assignee. However, explicit in any typical assignment scheme (and, in any event, implied at common-law), the assignor would have a subrogated or indemnity claim against the bankrupt estate equal to the payout by the assignor to the landlord. So, whether as a *de facto* guarantor or in its own right or as an original covenantor under the lease, any liability on the part of the assignor to the landlord not terminated contemporaneously with the assignee's own liability under the lease would mean a corresponding subrogated or indemnity claim by the assignor against the bankrupt assignee's estate, and this subrogated or indemnity claim would not necessarily be confined to the limited recoveries afforded under the *Bankruptcy and Insolvency Act*.

Although *Cummer-Yonge* type arguments have not generally met with much success in the U.S. courts (see, *e.g. Cromwell Field Associates LLP v. The May Department Stores* Company, 2001 U.S. APP. Lexus 3127), ironically the American judiciary may very well be coming around to adopting *Cummer-Yonge*-like reasoning in those cases dealing with the limited recourse recoveries available to U.S. landlords under the damage cap provisions of section 502 (b)(6) of the U.S. *Bankruptcy Code* (the "max cap"). Susan Fowler, in her article, "Letters of Credit in Lease Transactions, Part 1: Advantages to Landlord and Landlord's Lender", *Probate & Property*, Volume 16, No. 4, p. 28 at 30, criticizes the tendency of U.S. courts not to apply the max cap to claims by landlords against guarantors of tenants:

The rationale of not applying the Section 502(b)(6) cap to claims against a guarantor is that the guarantor's assets are not property of the bankrupt tenant's estate. Courts that take this position, however, do not address the guarantor's subrogation rights and indemnity claims, which may cause the tenant's estate to be depleted by the amount of the landlord's entire claim paid by the guarantor, including the portion that exceeds the Section 502(b)(6) cap.

Fowler cites *Levit v. Ingersoll Rand Financial Corp.* (*In re Deprizio Construction Co.*) 874 F.2d 1186 (7th Cir. 1989) as authority for the adoption in the United States of a more *Cummer-Yonge*-like approach to limiting recourse against guarantors. In *Deprizio*, the issue before the United States Court of Appeals for the Seventh Circuit involved the preference-recovery provisions of the *Bankruptcy Code* (roughly equivalent to the "reviewable transactions" provisions of the *Bankruptcy and Insolvency Act*), but in deciding the issue, the Court concludes:

A guarantor has a contingent right to payment from the debtor: if Lender collects from Guarantor, Guarantor succeeds to Lender's entitlements and can collect from Firm. So, Guarantor is a "creditor" in Firm's bankruptcy.

The Court of Appeal in *Crystalline* arguably falls into the same trap as the U.S. courts criticized by Fowler, by seemingly to ignore the subrogation and indemnification rights of the assignor that would inevitably be activated if the assignor is compelled to observe its covenant under the lease, and the resulting "back door" claim in bankruptcy that would arise when the assignor proves this claim in the bankruptcy. In the end, the lease is gone, the landlord is paid in full from the assignor, and the assignor proves a claim in bankruptcy against the assignee under its right of indemnity, with the result that the tenant in possession's estate faces a claim on account of the lost lease well in excess of the recovery allowed therefore under the *Bankruptcy and Insolvency Act.*

The theory that the *Bankruptcy and Insolvency Act* distribution scheme ought to be inviolate, and that schemes to avoid the maximum recoveries imposed thereunder are, accordingly, unenforceable, actually goes well beyond guarantees and assignments to possibly vitiate any number of credit enhancement arrangements that heretofore have been considered "*Cummer-Yonge*-proof" (including, possibly, indemnities, pre-paid rents, letters of credit, and the like). Brought to its ultimate logical conclusion, the theory may conclude that it is actually impossible to devise a scheme that will give a landlord the protection in bankruptcy that it really wants!

Of course, the Supreme Court of Canada, when (not if) it ultimately tackles *Cummer-Yonge* (this annotator believes that, whether or not leave to appeal *Crystalline* is granted, the Supreme Court of Canada will eventually have to rationalize the ever growing body of conflicting *Cummer-Yonge* case law), will have to reconcile the persistent comments of the country's lower courts to the effect that, even if any given surety covenant is released upon the release of the tenant, such secondary release may, in each such case, have been avoided by careful drafting. But can this urge to draft around *Cummer-Yonge* actually be reconciled with a theory of *Cummer-Yonge* that categorically rejects any scheme that yields recovery to a landlord above the statutorily prescribed limit? The answer is a definite "maybe". This annotator still represents as many landlords as he does trustees in bankruptcy and the landlord side of the practice continues to agonize over how best to protect itself against aggressive monitors and trustees invoking *Cummer-Yonge* at the drop of a hat. While sleeping with the enemy certainly has made this annotator more sympathetic to the insolvency bar's perspective on *Cummer-Yonge*, until and unless the Supreme Court of Canada drives a stake through the issue once and for all, this annotator (and others) will continue to try and structure our landlord clients' affairs so as to survive a *Cummer-Yonge* attack. In this regard, this annotator still feels he has a few "tricks" up his sleeve and continues not to give up hope (although supporting opinions as to enforceability have been abandoned some time ago!).

One fascinating aspect of the appellate decision in *Crystalline* that may go unnoticed by many practitioners is the Court of Appeal's almost out-of-hand rejection of the "repudiation" *versus* "disclaimer" reasoning that was prominent at trial and dispositive of the identical issue in *Transco Mills Ltd. v. Percan Enterprises Ltd.*, 76 B.C.L.R. (2d) 129, 100 D.L.R. (4th) 359, 29 R.P.R. (2d) 235, 23 B.C.A.C. 181, 39 W.A.C. 181, 1993 CarswellBC 19 (B.C. C.A.). By the *Transco Mills* argument, where the legislation entitles a tenant to "repudiate" its lease, then the lease is totally at an end (including any derivative liability such as the liability that may have attached to the original tenant *cum* assignor). If, on the other hand, a tenant is only entitled to "disclaim" its interest under the lease, then, while the tenancy may be at an end vis-à-vis the tenant-in-possession *cum* assignee, the rights of the landlord as against any others (including the original tenant *cum* assignor) that may have arisen under or through the lease *might* still remain intact and be enforceable (or at least would then be a justicable issue).

The principle in *Transco Mills* actually formed the crux of the trial decision in *Crystalline*. Since the facts in *Crystalline* occurred during the currency of the pre-1995 *Bankruptcy and Insolvency Act* (which used the "repudiation" language), the trial judge felt constrained to release the assignor from the obligations under the then "repudiated" lease, noting *in obiter*, however, that he would not have been so constrained on post-1995 facts (the *Bankruptcy and Insolvency Act* having been amended in 1995 to replace the "repudiation" privilege with a right to "disclaim" a lease of real property).

Prior to the release of the appeal in *Crystalline*, this annotator was quite concerned with the apparent catastrophic practice implications presented by *Crystalline*. Prior to the trial decision in *Crystalline*, a landlord would have found itself in a better position, covenant-wise, after an assignment of the lease by the tenant (since the common law does not release an assignor from obligations upon assignment, and since the assignor is seldom contractually released on assignment, the landlord usually ended-up with the joint and several covenants of both the assignor and the assignee — in effect, a "doubling-up" of the covenant comfort). After the trial but before the appeal in *Crystalline*, this annotator was quite agitated by the fact that all future consent to assignments of lease would have to be scrutinized on a true credit worthiness basis, lest the assignee's bankruptcy also release the assignor from liability, leaving the landlord with not two covenants, but rather, no covenants. Of course, while consents to assignments of the lease should probably always be scrutinized on a credit-worthiness basis, it was only after the trial decision in *Crystalline* that the legal implications of not doing so became ominous. Consider, for example, allowing a tenant to assign to a wholly owned subsidiary (even if it remains a subsidiary). Although routinely available prior to the trial in *Crystalline*, it would have been fraught with credit risk after *Crystalline* because the original tenant *cum* assignor could then escape its covenant merely by bankrupting its own subsidiary (the scenario becomes all too "real world" when one envisages a U.S. corporate parent assigning to its wholly owned Canadian subsidiary, then deciding that the Canadian market is not quite to their liking).

Critics (and there were, as usual, many) pointed out, however, that the fear that the *Crystalline* trial decision would prove a long-term deterrent to "normal" assignment practices was overblown. Because *Crystalline* was decided on the basis of *Transco Mills*, (which in turn was decided on the basis of the "repudiation" right available under the *Bankruptcy and Insolvency Act* prior to 1995 and not thereafter), the holding in *Crystalline* would actually continue to apply to only a miniscule (and ever depleting) handful of pre-1995 tenant bankruptcies still lingering before the courts, and not to assignments going forward from 1995. As a result, this annotator's fears of catastrophic assignment risk might have been reduced to "Chicken Little"-esque cries of impeding sky-falling. While this annotator has always been suspicious of the sophistry of *Transco Mills*, the ferocity with which it has been argued against this annotator, and the unequivocal endorsement thereof by the trial judge in *Crystalline*, left this annotator quite alone in his fear of the implications of the trial decision in *Crystalline*.

Mr. Justice Carthy's treatment of the *Transco Mills* theory in appeal was "nasty, brutish and short", but effective and, it is submitted, entirely correct. He concludes:

Much was made in argument of the fact that by a 1995 amendment the English version of ss. 65.2(1), (2), (3) and (4) was amended to change the word "repudiate" to "disclaim". This was a significant pillar in the trial judge's reasoning... The argument is that a repudiation destroys the lease while a disclaimer may not have that effect. I cannot accept that proposition... No one knows why the change was made and the appellant was probably right in suggesting that it was simply to be consistent with other uses of "disclaim" in the Act... [there] is not room to argue that the meaning was changed.

This annotator is divided about this aspect of the appeal decision. There is no doubt that Mr. Justice Carthy got the analysis dead on correct, and there is always some degree of personal satisfaction in having been vindicated by the Court of Appeal. That said, it is not a "convenient" conclusion for the leasing bar. In fact, even for that side of the bar that applauds the overturning of the trial decision in *Crystalline*, there was a conspiratorial undercurrent that wished that the Court of Appeal would leave well enough alone, safe in the understanding that since the trial decision in *Crystalline*, as heretical as it may have seemed, was nonetheless safely cauterized to pre-1995 facts and could not be a practical menace going forward.

Another fascinating aspect of *Crystalline* litigation seemingly overlooked by both the trial and appellate courts (but telling in their absence of criticism), is that the rule in *Cummer-Yonge* was argued in the context of a pre-bankruptcy proposal disclaimer under section 65 of the *Bankruptcy and Insolvency Act*. Historically, *Cummer-Yonge* has only been argued after the tenant was bankrupt, but *Crystalline* now seems authority for the proposition that *Cummer-Yonge* can also be argued in the context of leases disclaimed prior to bankruptcy under a *Bankruptcy and Insolvency Act* proposal. This is, of course, not a startling conclusion, but it does provide some insight into *Cummer-Yonge* case law: nothing really turns on the mechanics by which the lease is ultimately dealt with; everything turns on whether the landlord should be entitled to recovery in excess of the prescribed landlord maximums, whether that recovery be the proposal disclaimer consideration pre-bankruptcy or the preferred claim post-bankruptcy.

Courts looking at *Cummer-Yonge* scenarios from the perspective of solicitor negligence generally should not be quick to find any negligence on the part of counsel. Almost ten years ago, this annotator lamented the state of the *Cummer-Yonge* jurisprudence then to date but concluded, perhaps, in retrospect, with the naïve optimism that comes with youth, that the *Cummer-Yonge* cases were beginning to reduce in frequency and reconcile into a consistent pattern. The *Cummer-Yonge* cases, far from reducing in number or reconciling in theory, have only increased in frequency and disparity in the last decade. The *Crystalline* litigation is a perfect example of the difficulty in credibly predicting the judicial outcome of any given *Cummer-Yonge* gambit, but it is certainly not the only recent example. Although *West Shore* remains the law in British Columbia upholding *Cummer-Yonge* in the letter of credit context, the appeal to the Ontario Court of Appeal in *Lava Systems Inc. (Receiver and Manager of) v. Clarica Life Insurance Co.* [2002] O.J. No. 2526 (soon to be reported in *R.P.R.*) reverses the Ontario Superior Court holding in *Lava* and once again pits British Columbia against Ontario in their respective interpretations of *Cummer-Yonge* letters of credit. Likewise, a motion for leave to appeal is also currently before the Supreme Court of Canada in respect of the Ontario Court of Appeal decision in *J.P. Morgan Canada v. Maxlink Canada Inc.*, 2002 CarswellOnt 333, 31 C.B.R. (4th) 40, 155 O.A.C. 351, 58 O.R. (3d) 205 (Ont. C.A.), which dealt with facts very similar to those in *Crystalline*, but found, by an absolutely tortured analysis, that the disclaimer by the assignee's receiver operated only as a disclaimer of the assignment of lease and not of the lease itself (all this notwithstanding the fact that the receiver of the assignee never once purported to disclaim the assignment of lease!) Indeed, it would be rare to find experienced counsel now who would opine with any degree of certainty on any given *Cummer-Yonge* structure. Conversely, in all but a few situations, it would be difficult to find a landlord's counsel negligent for having implemented a pro-landlord *Cummer-Yonge* avoidance structure that did not ultimately succeed (or, for that matter, a trustee's counsel for having failed to prosecute a landlord for a recovery which, in retrospect, may have been limited by an aggressive application of *Cummer-Yonge*).

While time and space considerations make this annotation less than an ideal vehicle for a sweeping review of *Cummer-Yonge*, this annotator feels compelled to do so at the earliest opportunity. The bar would be better served if the Supreme Court of Canada did so instead.

Jeffrey W. Lem [1]

Table of Authorities

Cases considered by *Carthy J.A.*:

Andy & Phil Investments Ltd. v. Craig, 5 O.R. (3d) 656, 9 C.B.R. (3d) 52, 1991 CarswellOnt 223 (Ont. Gen. Div.) — considered

Cosgrove-Moore Bindery Services Ltd., Re, 2000 CarswellOnt 1561, 48 O.R. (3d) 540, 17 C.B.R. (4th) 205 (Ont. S.C.J. [Commercial List]) — referred to

Cummer-Yonge Investments Ltd. v. Fagot, [1965] 2 O.R. 152, 8 C.B.R. (N.S.) 62, 50 D.L.R. (2d) 25, 1965 CarswellOnt 40 (Ont. H.C.) — considered

Cummer-Yonge Investments Ltd. v. Fagot, [1965] 2 O.R. 157n, 8 C.B.R. (N.S.) 62n, 50 D.L.R. (2d) 30n (Ont. C.A.) — referred to

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Transco Mills Ltd. v. Percan Enterprises Ltd., 76 B.C.L.R. (2d) 129, 100 D.L.R. (4th) 359, 29 R.P.R. (2d) 235, 23 B.C.A.C. 181, 39 W.A.C. 181, 1993 CarswellBC 19 (B.C. C.A.) — considered
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Statutes considered:

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3
s. 65.1 [en. 1992, c. 27, s. 30] — considered

s. 65.2 [en. 1992, c. 27, s. 30] — considered

s. 65.2(1) [en. 1992, c. 27, s. 30] — referred to

s. 65.2(2) [en. 1992, c. 27, s. 30] — considered

s. 65.2(3) [en. 1992, c. 27, s. 30] — considered

s. 65.2(4) [en. 1992, c. 27, s. 30] — referred to

APPEAL by landlord from judgment reported at 2001 CarswellOnt 601, 39 R.P.R. (3d) 49, 31 C.B.R. (4th) 216 (Ont. S.C.J.), dismissing landlord's claims against tenant for amounts owing under leases.

Carthy J.A.:

1 This appeal concerns two actions, each arising from similar circumstances. In each, summary judgment has been awarded dismissing the claim of the landlord of commercial real estate seeking lease payment damages against the tenant Domgroup Ltd. The circumstances are similar to those in the recent decision of this court in *J.P. Morgan Canada v. Maxlink Canada Inc.* (2002), 31 C.B.R. (4th) 40 (Ont. C.A.), released February 7, 2002, but the legal backdrop is very different. All three cases involve a long-term lease to a lessee, an assignment to a sub-lessee, and the insolvency of the sub-lessee. All concern the legal impact upon the relationship between the landlord and the original tenant. In *J.P. Morgan Canada*, the result flowed from the interpretation of a court order. In the instant appeal, the decision flows from an interpretation of s. 65.2 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, as amended to 1994.

2 Do the provisions of that section terminate a lease for all purposes or do they only affect the obligations of the insolvent? The motions judge found that the notices of repudiation given under that section terminated the leases for all purposes. He also held that the compensation paid to the landlord pursuant to s. 65.2 constituted the landlord's full entitlement under each lease. Thus, the actions against the original lessees were dismissed.

3 I cannot agree with those dispositions for the reasons that follow.

4 The motions judge succinctly outlines the facts of each case and they are so similar that, for purposes of this appeal, a quotation of the reasons concerning *Crystalline* will suffice:

> By a lease dated April 30, 1979 Dominion Stores Limited, the predecessor of Domgroup, leased from Crystalline premises located in the Northumberland Square Shopping Centre in Douglastown, New Brunswick. The term of the lease was for 25 years ending on March 31, 2004. The lease contained the following provision:
>
> > Notwithstanding any assignment or sublease the lessee shall remain fully liable under this lease and shall not be released from performing any of its covenants, obligations or agreements in this lease and shall continue to be bound by this lease.
>
> By an assignment dated May 25, 1995 Dominion Stores Limited assigned the lease to Coastal Foods Limited. It subsequently amalgamated with The Food Group Inc. On or about February 11, 1994 The Food Group Limited filed a Notice of Intention to make a proposal pursuant to Part III of the 1992 Act. On February 18, 1994 Peat

Marwick Thorne Inc., acting as the proposal trustee of The Food Group Inc., delivered a Notice of Repudiation of the lease to Crystalline pursuant to s. 65.2 of the 1992 Act. The Notice of Repudiation stated, in part, as follows:

> 3. The repudiation of the lease will become effective on the 31 st day of March, 1994 at 11:59 PM local time.
>
> 4. Before the repudiation becomes effective, you may apply to the court, within 15 days after the day of which this notice is received, for a declaration that subsection 65.2(1) of the *Bankruptcy and Insolvency Act* does not apply in respect of the lease mentioned above . . .
>
> 6. By virtue of subsection 65.2(3) of the *Bankruptcy and Insolvency Act*, a proposal filed by the undersigned commercial tenant must provide for payment to you, immediately after court approval of the proposal, of compensation equal to the lesser of
>
> (a) an amount equal to six months rent under the lease, and
>
> (b) the rent for the remainder of the lease, from the date on which the repudiation takes effect.
>
> 7. As detailed in the proposal, The Food Group Inc. or the Trustee intends to continue to occupy the premises for the period from the date of the notice of intention until a date not later than March 31, 1994, and the payment provided for under Part 6 of this notice shall be considered compensation for all damages and occupation rent and the landlord shall not have any right to vote a claim in respect of accelerated rent, damages arising out of the repudiation or the compensation provided for herein (section 65.2(4)).

Crystalline did not apply to the Court to challenge the repudiation of the lease as it was entitled to under the 1992 Act. By a letter dated March 16, 1994 Peat Marwick Thorne Inc. undertook to pay Crystalline the amount to which it was entitled under the 1992 Act subject to confirmation that Crystalline would not object to the application for approval of the proposal by the Court. Crystalline returned a signed copy of the letter and confirmed, in accordance with the terms of the letter, that it would not take any action to object to the application for approval of the proposal. This was confirmed by counsel for Crystalline. The proposal stated that a number of leases, including the one with Crystalline, would be terminated in accordance with s. 65.2 of the 1992 Act with effect on March 31, 1994. This proposal was approved by the Court of Queen's Bench for New Brunswick in Bankruptcy by order dated March 18, 1994. Pursuant to that order Crystalline received and accepted payment in the amount of $131,154.54 in respect of the compensation payable under s. 65.2(3) of the 1992 Act for the termination of the lease. The lease was terminated effective March 31, 1994. However, on January 20, 1995 Crystalline sent to Domgroup a letter in which it referred to the assignment clause and alleged that Domgroup was in default of payment of rent due under the lease. The letter expressed an intention to seek relief through the Courts if Domgroup did not remedy the alleged default. The letter did not acknowledge the termination of the lease as of March 31, 1994.

5 Section 65.2 of the *Bankruptcy and Insolvency Act* was introduced in 1992 along with other sections dealing with proposals by insolvent persons. That section reads:

> **65.2** (1) At any time between the filing of a notice of intention and the filing of a proposal, or on the filing of a proposal, in respect of an insolvent person who is a commercial tenant under a lease of real property, the insolvent person may repudiate the lease on giving thirty days notice to the landlord in the prescribed manner, subject to subsection (2).
>
> (2) Within fifteen days after being given notice of the repudiation of a lease under subsection (1), the landlord may apply to the court for a declaration that subsection (1) does not apply in respect of that lease, and the court, on notice to such parties as it may direct, shall make such a declaration unless the insolvent person satisfies the court that the insolvent person would not be able to make a viable proposal, or that the proposal the insolvent person has made would not be viable, without the repudiation of that lease and all other leases that the tenant has repudiated under subsection (1).

(3) Where a lease is repudiated pursuant to subsection (1), a proposal filed by the insolvent person must provide for payment to the landlord, immediately after court approval of the proposal, of compensation equal to the lesser of

(*a*) an amount equal to six months rent under the lease, and

(*b*) the rent for the remainder of the lease, from the date on which the repudiation takes effect.

(4) For the purpose of voting on any question relating to a proposal referred to in subsection (3), the landlord does not have any claim in respect of accelerated rent, damages arising out of the repudiation, or the compensation referred to in subsection (3).

(5) Nothing in subsections (1) to (4) affects the operation of section 146 in the event of bankruptcy.

(6) Where an insolvent person who has made a proposal referred to in subsection (3) becomes bankrupt

(*a*) after court approval of the proposal and before the proposal is fully performed, and

(*b*) after compensation referred to in subsection (3) has been paid,

the landlord has no claim against the estate of the bankrupt for accelerated rent.

6 This section must be read in context with s. 65.1, which provides that where a notice of intention or a proposal is filed by an insolvent, no person may terminate an agreement or claim an accelerated payment by reason only of the insolvency or the failure to pay rent. Thus, the landlord's rights against the insolvent tenant are suspended subject to the right to collect rent on a day-to-day basis following the date of the notice or proposal. For a discussion of this section, see *Cosgrove-Moore Bindery Services Ltd., Re* (2000), 48 O.R. (3d) 540 (Ont. S.C.J. [Commercial List]).

7 Section 65.2 then follows, providing the insolvent tenant an opportunity to rid itself of lease obligations in order to make its proposal viable. In that event, the landlord recovers a maximum of 6 months rent after repudiation.

8 This statutory scheme is clearly designed to permit commercial businesses to avoid being dismantled in a bankruptcy and to survive in the hope of future viability. The question before this court is whether the insolvent assignee's repudiation of the lease pursuant to the scheme affects the agreement between the landlord and the original lessee. I note at the outset that it seems counter-intuitive to consider that the original lease is affected and indeed terminated by the repudiation. This result confers no benefit on the insolvent and does nothing to serve the purpose of the legislation.

9 Much was made in argument of the fact that by a 1995 amendment the English version of ss. 65.2(1), (2), (3) and (4) was amended to change the word "repudiate" to "disclaim". This was also a significant pillar in the trial judge's reasoning. Curiously, no change was made to the French version, which employs the word "résilier". The argument is that a repudiation destroys the lease while a disclaimer may not have that effect. I cannot accept that proposition. A canvas of dictionaries including a French to French dictionary shows only a modest difference, mostly of usage in a particular context, between "repudiate", and "disclaim" and "résilier". No one knows why the change was made and the appellant is probably right in suggesting it was simply to be consistent with other uses of "disclaim" in the Act. In any event, the French version has equal authority to the English version, leaving no room to argue that the meaning has changed.

10 Of far more significance is the fact that s. 65.1 uses the term "termination" when a final act is contemplated. A landlord may respond, in ordinary circumstances, to a failure to pay rent by terminating the lease - an act in response to a failure to meet a condition of the lease. Section 65.1 prevents that termination if a proposal has been filed. A disclaimer or a repudiation is a statement of position by one party. It creates legal rights in the other party which are triggered by a response but does not, in ordinary circumstances, effect a termination without a response and election. The result under s. 65.2 of the repudiation by the insolvent is that the landlord's rights against the insolvent are as set out in the section. It may come forward to have the insolvent satisfy the court that the viability of the proposal depends upon the repudiation.

If not, it may claim six months rent and has no further claim on the insolvent. Those are the statutory consequences visited upon the landlord and there is no mention in the statute of termination or consequences affecting others who may have liability to the landlord.

11 Trafford J. was of the opinion that the repudiation terminated the lease. The sole entitlements of the landlord were to appear pursuant to s. 65.2(2) and contest the repudiation and, if unsuccessful, to recover the six months' rent provided for in s. 65.2(3). I have expressed my view that repudiation under s.65.2(2) is not the equivalent of termination at common law. I would only add that the hearing as to the viability of the proposal without the repudiation is totally unrelated to the rights of the landlord against other third parties and the compensation provided for in s. 65.2(3) is nominal compared to the income stream from a twenty-five-year lease with a credit-worthy original lessee. It should be noted that the lease may have real value to that original lessee. Consequently, the original lessee's rights cannot be abrogated in its absence.

12 My conclusion that the rights as between the landlord and the original tenant are unaffected by these proceedings under s. 65.2 is supported by every authority brought to my attention, albeit none deal with this section of the Act.

13 In *Cummer-Yonge Investments Ltd. v. Fagot*, [1965] 2 O.R. 152 (Ont. H.C.) aff'd [1965] 2 O.R. 157n (Ont. C.A.), Gale C.J.H.C. found that when a lease is disclaimed by a trustee in bankruptcy, the bankrupt's covenants to perform are dissolved. Since the guarantors' obligation is to assure performance of those covenants, their obligations disappear with the covenants.

14 The distinction between the position of a guarantor and one who has primary obligations was identified by Austin J. in *Andy & Phil Investments Ltd. v. Craig* (1991), 5 O.R. (3d) 656 (Ont. Gen. Div.) at 658, where he states:

> In *Cummer-Yonge* the guarantor guaranteed "the due performance by the Lessee of all its covenants in this lease". Gale C.J.H.C. decided that this was a "secondary obligation" (p. 154 O.R., p. 64 C.B.R.) which ended when the primary obligations passed to the trustee on the bankruptcy of the lessee.
>
> The obligation of Craig in the present case is not secondary. It is clear from the language of clause 16.15 that Craig signed "as principal and not as surety". Clause 16.15, set out above, makes Craig a tenant to all intents and purposes. Craig not having gone bankrupt, there has been no suspension of the landlord's rights to proceed against Craig as tenant or principal.

15 Similarly, in *Glenview Corp. v. Lavolpicella* (1997), 12 R.P.R. (3d) 74 (Ont. Gen. Div.), Chadwick J. found an assignor lessee liable under the lease when the assignee's trustee in bankruptcy disclaimed the lease. They were assignors and not guarantors and, thus, liable.

16 In *Transco Mills Ltd. v. Percan Enterprises Ltd.* (1993), 100 D.L.R. (4th) 359 (B.C. C.A.), the British Columbia Court of Appeal dealt with identical facts to those on this appeal, although not under s. 65.2 and applied the word "disclaim" rather than "repudiate". Taylor J.A. dealt at length with the history in England of the right of a trustee to disclaim a lease, seeking to resolve the same debate as is now presented to this court but in the context of a British Columbia statute empowering the trustee to "disclaim any lease". As an aside, I note that this long history of use of "disclaim" may explain the 1995 *Bankruptcy and Insolvency Act* amendment. In *Transco Mills Ltd.*, Taylor J.A. quoted, at p. 366, from Vice-Chancellor Megarry in *Warnford Investments Ltd. v. Duckworth* (1977), [1978] 2 All E.R. 517 (Eng. Ch. Div.):

> On the other hand, where the lease has been assigned, and the bankruptcy is that of the assignee in whom the lease is vested, and not of the original lessee, the position of the original lessee is very different. *The disclaimer does not destroy the lease, but leaves it in existence, though without an owner until a vesting order is made.* The original lessee is a person who as principal, undertook towards the lessor, the obligations of the lease for the whole term; and there is nothing in the process of assignment which replaced this liability by the mere collateral liability of a surety who must pay the rent only if the assignee does not. The bankruptcy of the assignee has for the time being destroyed the original lessee's right against the assignee to require him to discharge the obligations of the lease, and it has impaired the lessee's right of indemnity against him when he has to discharge the obligations himself; but it has not affected

> his primary liability towards the lessor, which continues unaffected. At no time does an original lessee become a mere guarantor to the lessor of the liability of any assignee of the lease. [Emphasis is that of Taylor J.A.]

17 Although there is no procedure in British Columbia for a vesting order, Taylor J.A. concluded at p.367:

> There appears to me to be very good reason for our taking the same approach to determination of the consequences of disclaimer by a trustee in bankruptcy under the *Commercial Tenancy Act* [R.S.B.C. 1979, c. 54] as the English courts have adopted under the English legislation - that is to say, so as to accomplish the purpose of the bankruptcy scheme only, and so far as possible not adversely to affect the position of those outside the bankruptcy.

18 This reasoning is as convincing with the word "repudiation" as with "disclaim". Both are unilateral expressions of a refusal to be bound by the lease in the future and the consequences of one or the other should be restricted to those set out in s. 65.2 and directed to the purposes of insolvency proceedings.

19 For these reasons, I would allow the appeal and set aside the summary judgments with costs to the appellants here and below. Under the new rules effective January 1, 2002 this court must assess the costs. The appellants shall submit a bill of costs with appropriate details, based upon the partial indemnity scale, and the respondent shall have 10 days thereafter to respond.

Appeal allowed.

Footnotes

* Corrigenda issued by the court have been incorporated herein.

1 Davies Ward Phillips & Vineberg, LLP

2004 SCC 3, 2004 CSC 3
Supreme Court of Canada

Crystalline Investments Ltd. v. Domgroup Ltd.

2004 CarswellOnt 219, 2004 CarswellOnt 220, 2004 SCC 3, 2004 CSC 3, [2004] 1 S.C.R. 60, [2004] S.C.J. No. 3, 128 A.C.W.S. (3d) 380, 16 R.P.R. (4th) 1, 184 O.A.C. 33, 234 D.L.R. (4th) 513, 316 N.R. 1, 43 B.L.R. (3d) 1, 46 C.B.R. (4th) 35, 70 O.R. (3d) 254 (note), 70 O.R. (3d) 254, J.E. 2004-335, REJB 2004-53098

Domgroup Ltd., Appellant v. Crystalline Investments Ltd. and Burnac Leaseholds Ltd., Respondents

McLachlin C.J.C., Iacobucci, Major, Binnie, LeBel, Deschamps, Fish JJ.

Heard: November 7, 2003
Judgment: January 29, 2004
Docket: 29196

Proceedings: affirming (2002), 2002 CarswellOnt 705, 31 C.B.R. (4th) 225, 210 D.L.R. (4th) 659, 156 O.A.C. 392, 58 O.R. (3d) 549, 49 R.P.R. (3d) 171, 27 B.L.R. (3d) 102, [2002] O.J. No. 883 (Ont. C.A.); reversing (2001), 2001 CarswellOnt 601, 39 R.P.R. (3d) 49, 31 C.B.R. (4th) 216 (Ont. S.C.J.)

Counsel: Fred D. Cass, Lawrence J. Crozier, David Stevens, for Appellant
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Subject: Insolvency; Property; Civil Practice and Procedure

Related Abridgment Classifications

Bankruptcy and insolvency
X Priorities of claims
X.4 Claims by landlord
X.4.h Assignment of lease
Real property
V Landlord and tenant
V.11 Assignment of lease
V.11.a Nature and effect of assignment

Headnote

Bankruptcy and insolvency --- Priorities of claims — Claims by landlord — Assignment of lease
Repudiation of leases by assignee under s. 65.2 of Bankruptcy and Insolvency Act does not relieve original tenant of its obligations under leases as original lessee — Post-disclaimer, assignors and guarantors should be treated in same manner with respect to liability.
Landlord and tenant --- Assignment of lease — Nature and effect of assignment
Rights as between landlord and original tenant unaffected by proceedings taken by insolvent sub-lessee under s. 65.2 of Bankruptcy and Insolvency Act — Post-disclaimer, assignors and guarantors should be treated in same manner with respect to liability.
Faillite et insolvabilité --- Priorités des réclamations — Réclamations du locateur — Cession de bail
Résiliation d'un bail par le cessionnaire en vertu de l'art. 65.2 de la Loi sur la faillite et l'insolvabilité ne libère pas le locataire initial de ses obligations en vertu du bail à titre de locataire initial — Après la résiliation d'un bail, les cédants et les garants devraient être assujettis à la même responsabilité.
Locateur et locataire --- Cession de bail — Nature et effet de la cession

Procédures engagées en vertu de l'art. 65.2 par un sous-locataire insolvable n'ont aucune incidence sur les droits du locateur et du locataire initial — Après la résiliation d'un bail, les cédants et les garants devraient être assujettis à la même responsabilité.

Landlords and tenant entered into long-term lease agreements. The tenant later assigned the leases to a sub-lessee which subsequently became insolvent, made a proposal under the Bankruptcy and Insolvency Act, and repudiated the leases under s. 65.2 of the Act. The landlords were paid compensation equal to six months' rent as set out in the Act, and they then brought actions against the tenant for the amounts owing under the leases. The tenant's motion for summary judgment dismissing the landlords' actions was granted, the motions judge holding that the court-approved termination of the leases ended all obligations of all parties under the leases.

The landlords' appeal was allowed, the appeal court determining that the rights as between the landlords and the original tenant were unaffected by the proceedings taken by the insolvent sub-lessee under s. 65.2 of the Act.

The tenant appealed to the Supreme Court of Canada.

Held: The appeal was dismissed.

Section 65.2 of the Act should be read narrowly. The plain purposes of the section are to free an insolvent from the obligations under a commercial lease that have become too onerous, to compensate the landlord for the early termination of the lease, and to allow the insolvent to resume viable operations as best it can. Nothing in s. 65.2, or any part of the Act, protects third parties such as assignors from the consequences of an insolvent's repudiation of a commercial lease.

The tenant as principal undertook towards the landlords the obligations of the lease for the whole term and there was nothing in the process of assignment which replaced this liability by the mere collateral liability of a surety who had to pay the rent only if the assignee did not. The bankruptcy of the assignee destroyed for the time being the tenant's right against the assignee to require it to discharge the obligations of the lease, and also impaired the tenant's right of indemnity against the assignee when the tenant had to discharge the obligations itself. However, it did not affect the tenant's primary liability towards the landlords, which continued unaffected. At no time did the tenant become a mere guarantor to the landlords of the liability of the assignee of the lease.

The mere possibility that the tenant might have a right of indemnity against its insolvent assignee and be able to make a claim to participate in the proposal proceedings as an unsecured creditor was not inconsistent with the Act. On the contrary, it was consistent with the circumstances applicable to other alternative convenantors and did not affect or alter the nature of the tenant's contractual relationship and obligations. More importantly, it did not require that the tenant be discharged from liability.

The distinction between guarantors as having secondary obligations that disappear when a lease is disclaimed by a trustee in bankruptcy, and assignors as having primary obligations that survive a disclaimer, thrives in Canadian case law, but the cases so holding should be overruled. 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.

Les locatrices ont conclu des baux à long terme avec la locataire. Celle-ci a cédé ultérieurement ses baux à une sous-locataire qui, par la suite, est devenue insolvable, a fait une proposition en vertu de la Loi sur la faillite et l'insolvabilité et a résilié les baux en vertu de l'art. 65.2 de la Loi. À titre de compensation, les locatrices ont reçu six mois de loyer, comme le prévoit la Loi; elles ont ensuite intenté des procédures contre la locataire afin d'obtenir les montants dus en vertu des baux. La requête pour jugement sommaire présentée par la locataire a été accueillie par le juge au motif que les obligations de toutes les parties en vertu des baux avaient été complètement éteintes par la décision du tribunal approuvant la résiliation des baux.

Le pourvoi des locatrices a été accueilli par la Cour d'appel, qui a conclu que les droits des locatrices et de la locataire initiale n'étaient pas touchés par les procédures engagées par la sous-locataire en vertu de l'art. 65.2 de la Loi.

La locataire a interjeté appel à la Cour suprême du Canada.

Arrêt: Le pourvoi a été rejeté.

L'article 65.2 de la Loi devrait recevoir une interprétation restrictive. Les objectifs manifestes de cet article sont de libérer une personne insolvable des obligations découlant d'un bail commercial qui sont devenues trop lourdes, d'indemniser le locateur pour la fin prématurée du bail et de permettre à la personne insolvable de reprendre autant que possible des activités viables. Ni l'article 65.2 ni quelque autre partie de la Loi ne protègent les tiers, dont les cédants, des conséquences de la résiliation d'un bail commercial par une personne insolvable.

À titre de débitrice principale, la locataire s'est engagée envers les locatrices à assumer les obligations du bail pour toute la durée de celui-ci; le processus de cession n'a pas pour effet de substituer à cette obligation la simple obligation subsidiaire qu'a la caution de payer le loyer uniquement en cas de défaut du cessionnaire. La faillite de la cessionnaire a éteint pour le moment le droit de la locataire d'exiger de la cessionnaire l'exécution des obligations prévues par le bail et a affaibli le droit de la locataire d'être indemnisée par cette dernière lorsqu'elle doit les exécuter elle-même. La faillite n'a cependant pas eu d'incidence sur l'obligation fondamentale de la locataire envers la locatrice, obligation qui, elle, reste intacte. La locataire n'est devenue, en aucune circonstance, simple garante envers les locatrices des obligations de la cessionnaire du bail.
La simple possibilité que la locataire dispose d'un droit d'indemnisation opposable à sa cessionnaire insolvable et qu'elle puisse présenter une réclamation afin de participer aux procédures de proposition en tant que créancière non garantie n'était pas incompatible avec la Loi. Au contraire, cette possibilité demeurait pertinente dans les circonstances applicables aux autres contractants subsidiaires et ne modifiait en rien la nature des obligations et relations contractuelles de la locataire. Facteur plus important, cette possibilité ne commandait pas que la locataire soit libérée de ses obligations.
La distinction voulant que les garants soient tenus à une obligation secondaire qui disparaît en cas de résiliation du bail par le syndic de faillite et que les cédants soient tenus à une obligation principale qui survit à cette résiliation demeure bien vivante dans la jurisprudence canadienne; les décisions qui arrivent à une telle conclusion devraient être infirmées. Après la résiliation d'un bail, cédants et garants devraient être assujettis à la même responsabilité. Le seul fait de la résiliation ne devrait libérer ni les uns ni les autres de leurs obligations contractuelles.

Annotation

At the risk of hyperbole, these annotators submit that the decision of the Supreme Court of Canada in *Crystalline Investments Limited v. Domgroup Ltd.* is, bar none, the single most important Canadian landlord and tenant law decision since *Highway Properties Ltd. v. Kelly Douglas & Co. Ltd.*, [1971] S.C.R. 562.

While landlord and tenant law has always generally favoured commercial landlords by providing them with substantial remedial powers as of right, landlords have nonetheless always obsessed about the financial strength and enforceability of tenant covenants. While commercial landlords had traditionally sought third party guarantees to enhance the credit-worthiness of their tenants, the Ontario High Court decision in *Cummer-Yonge Investments Ltd. v. Fagot* (1965), 2 O.R. 152 (Ont. H.C.), aff'd (1965), 2 O.R. 157 (Ont. C.A.) effected a total sea change in the way landlords went about protecting their covenant recourse in times of tenant bankruptcy.

In *Cummer-Yonge*, a tenant made a voluntary assignment in bankruptcy and the trustee-in-bankruptcy subsequently disclaimed the lease, leaving the landlord with up to six months' worth of rent as its preferred claim in the bankruptcy. Although it has been nearly forty years since *Cummer-Yonge*, the general scheme of bankruptcy recovery for landlords has remained largely unchanged to date. The landlord in *Cummer-Yonge*, not fully compensated by the preferred claim in bankruptcy, turned to a third party surety under guarantee that it had procured to secure "the due performance by the lessee of all of its covenants . . . including the covenant to pay rent". The guarantee proved to be of little practical value to the landlord in *Cummer-Yonge*. According to the High Court (with affirmation from the Court of Appeal but without reasons), since the lease had been validly disclaimed in the bankruptcy proceeding, and since the tenant no longer had any obligations under the lease as a result of such disclaimer, there could be no obligations for the guarantor to guarantee. As a result of this simple analysis, the guarantor in *Cummer-Yonge* was fully released from its covenant under the guarantee.

A significant body of jurisprudence has developed over the past four decades dealing with *Cummer-Yonge*-based defences (for an excellent cataloguing of the jurisprudence to date, see, D. Rogers, "Revisiting Letters of Credit, Guarantees and Indemnities in a Fragile Economy", *The Six Minute Commercial Leasing Lawyer*, The Law Society of Upper Canada, October 1, 2001). These cases, which hail from jurisdictions across Canada, have, for the most part, ebbed and flowed in their support of the rule in *Cummer-Yonge*, with some cases wholeheartedly supporting the rule, and others distinguishing the facts then at bar sufficient to avoid the operation of the rule (but, curiously, without a single court ever purporting to actually overrule *Cummer-Yonge* itself). Recently, the jurisprudence has seen an unusually high rate of successful *Cummer-Yonge* defences against landlord recoveries. In the past decade alone, as a result of the application of the rule in *Cummer-Yonge*, commercial leasing practice has seen the emasculation of general security agreements (*Peat Marwick*

Thorne Inc. v. Natco Trading Corp. (1995), 44 R.P.R. (2d) 207), letters of credit (*West Shore Ventures Limited v. K.P.N. Holding Ltd.*, [2001] B.C.C.A. 279 (C.A.), but see also *Lava Systems Inc. (Receiver & Manager of) v. Clarica Life Insurance Co.* (2002), 1 R.P.R. (4th) 50 (Ont. C.A.) for a slightly different take on letters of credit) and, most recently, even indemnities (*KKBL No. 297 Ventures Ltd. v. Ikon Office Solutions, Inc.*, (2003), 16 R.P.R. (4th) 29 (B.C. S.C.)).

The *Crystalline* case was on the forefront of this wave of recent destabilizing *Cummer-Yonge* cases, and was perhaps the most conceptually extreme example of the rule. In *Crystalline*, a grocery store tenant assigned its lease to an assignee who subsequently became insolvent and filed a proposal under Section 65.2 of the pre-1995 version of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3. As part of the proposal, the assigned lease was repudiated. As a result of such repudiation, the landlord received compensation approximately equivalent to the six months' worth of rent that the landlord would have received had the tenant gone bankrupt and the lease had been disclaimed by the trustee in bankruptcy. Since the six months' worth of rent did not fully compensate the landlord for its losses on the repudiation, the landlord then sued the original tenant *cum* assignor under the lease for the balance of the landlord's damages. The lease did not provide that, as a matter of contract, the assignor would be released upon the assignment. Indeed, quite the opposite was in fact the case: the lease expressly confirmed that the original tenant would remain fully liable under the lease notwithstanding any assignment.

The original tenant in *Crystalline*, now faced with a significant damage award arising as a consequence of the repudiation of the lease by its assignee, argued that it actually fell within the rule in *Cummer-Yonge*. That is, since it was no longer in possession of the leased premises, it became, in effect, analogous with any third party surety of the assignee. Significantly paraphrased, the assignor's argument was simply that, upon the insolvency of the tenant-in-possession (i.e. the assignee) and the resulting termination of the lease in that assignee's insolvency process, there simply was no more lease to covenant in respect of, so the original tenant *cum* assignor should also be released from all liability under the now repudiated lease: in effect, just like the guarantor in *Cummer-Yonge*. According to the argument, the landlord, having recovered the equivalent of the preferred claim in bankruptcy, had received all that the legislature ever intended that it should receive.

At trial ((2001), 39 R.P.R. (3d) 49), Mr. Justice Trafford of the Ontario Superior Court of Justice accepted the assignor's *Cummer-Yonge* gambit, fully releasing the original tenant *cum* assignor from any further obligations relating to the then repudiated lease. On appeal ((2002) 49 R.P.R. (3d) 171), the Ontario Court of Appeal reversed the trial court decision, restoring the general rule that an assignor, unless contractually released by the landlord, remains liable on the covenant, and adding that this regime should govern notwithstanding the insolvency of the assignee and notwithstanding any end to the lease by repudiation or disclaimer as a result of insolvency proceedings. The Court of Appeal reasons gave rise to a multitude of fascinating issues, a number of which were canvassed in a case annotation in the *Real Property Reports* version of the appeal reasons (see, J. Lem, "Annotation", at 49 R.P.R. (3d) 171). The original tenant *cum* assignor then appealed the case to the Supreme Court of Canada, where a good number of the "interesting" issues set forth in the aforesaid annotation were addressed by the Supreme Court of Canada, in reasons delivered by Mr. Justice Major.

What has been greatly unappreciated by the practising bar is that, had the assignor's arguments in *Crystalline* carried the day at the Supreme Court of Canada, there would have been a profound impact on the day-to-day activities of Canadian landlords and tenants, far more so than with any of the other *Cummer-Yonge* cases. Indeed, given the unique status of the leasehold assignor in landlord and tenant law, we submit that any extension of the *Cummer-Yonge* doctrine to assignors might have opened up a veritable Pandora's Box of issues not present in other *Cummer-Yonge* situations.

For instance, as the law stood immediately before *Crystalline* (and now after *Crystalline* as well), a landlord could consent to any assignment of any lease to any assignee, relatively safe in the legal presumption that, absent a contractual release from the landlord, the original tenant *cum* assignor would remain liable on the original covenant notwithstanding having transferred the benefit of the lease (note that the presumption is reversed in Quebec). There are, of course, some arguably legitimate non-covenant reasons for insisting upon some discretion over the identity of future tenants-in-possession, but technically, from a purely financial perspective, a landlord can never be worse off with an assignee, regardless of the credit-worthiness of that assignee's covenant, because the landlord always has recourse to the continuing covenant of the original tenant *cum* assignor, which is all of the covenant comfort that the landlord ever had in the first place. To

the extent that the landlord gets covenant comfort from the assignee, such recourse is in addition to, rather than in lieu of, the comfort granted by the original covenantor. Had the assignor succeeded in establishing a *Cummer-Yonge* defence at the Supreme Court of Canada, any assignment of any lease to any assignee would constitute, in every such instance, a contingent release of the assignor. What's worse, the contingency giving rise to the release (i.e. petitioning the assignee into bankruptcy) could be unilaterally invoked by the assignee as a "scorched earth" tactic denying the landlord the benefit of the assignor's covenant, or by the assignor itself as a purely strategic self-exculpating manoeuvre, or by a collusion between the two or even by a creditor competing against the landlord. As if to add insult to injury, such a regime would also effectively deny landlords from ever themselves petitioning the tenant-in-possession into bankruptcy (although much of the discussion around *Cummer-Yonge* pre-supposes that landlords would be adverse to a tenant bankruptcy, it has to be remembered that a landlord is also a creditor and may itself have reasons to bankrupt its own tenant where choice of remedy permits). As a consequence of the foregoing, a landlord would never be able to consent to any assignment (except possibly to a materially better covenant), and leasing practice in Canada would quickly grind to a halt as the legal regime converts itself into a leasehold-transfers-by-sublease only jurisdiction.

The Supreme Court of Canada released its reasons in *Crystalline* in January of 2004. Siding with the Court of Appeal, the Supreme Court concluded that, absent a contractual release from the landlord, the original tenant *cum* assignor under the lease would remain liable on the covenant to the landlord, notwithstanding the insolvency of the assignee and notwithstanding any consequent repudiation of the lease. According to Mr. Justice Major's reasons:

the repudiation must be construed as benefiting only the insolvent [e.g.. the assignee]. Nothing . . . protects third parties [e.g. the assignor] . . . from the consequences of an insolvent's repudiation of a commercial lease. That is to say that they remain liable . . .

Although the foregoing analysis was in our view, wholly dispositive of the matter before the Court, much to the delight of the Canadian commercial bar, the Supreme Court of Canada did not limit itself to simply the specific issue of assignor liability post lease disclaimer/repudiation. Instead, the Court took it upon itself to "walk on the wild side" by, once and for all, addressing the bigger normative issue posed by *Cummer-Yonge*: just what should happen to third party sureties after the insolvency of the tenant-in-possession and the disclaimer or repudiation of the lease as a result of such insolvency? It is this *obiter dicta* that has literally taken the Canadian commercial leasing bar by storm.

It has to be remembered that the rule in *Cummer-Yonge* also created similar disturbances in English commercial landlord and tenant practice (although, of course, the doctrine was never referred to as such in England). Long before *Cummer-Yonge*, the English Queen's Bench, in its landmark decision in *Stacey v. Hill*, [1901] 1 Q.B. 660, found, much in the same way as had the Ontario High Court in *Cummer-Yonge* some six decades later, that surety liability ends with the bankruptcy. It was not until almost a century after *Stacey v. Hill* that the House of Lords, in *Hindcastle Ltd. v. Barbara Attenborough Associates Ltd.*, [1997] A.C. 70 finally overturned that nation's equivalent to *Cummer-Yonge*. To the delight of many, the Supreme Court of Canada, seven years after *Hindcastle*, followed suit in *Crystalline*. In one fell swoop, the Court expressly overruled almost four decades of *Cummer-Yonge* legal dogma. In its own words, Mr. Justice Major concluded:

The House of Lords went on to overrule *Stacey v. Hill* . . . *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.

While the ultimate impact of the Supreme Court of Canada's ruling in *Crystalline* will not be fully appreciated for years to come, there is quickly emerging some excellent learned commentary on the *Crystalline* decision (see, e.g., D. Rogers "The Swan Lake of *Cummer-Yonge, sub nom.* Goodbye *Cummer-Yonge*, Again", *Six-Minute Commercial Leasing*, 2004 (The Law Society of Upper Canada). Already, there is debate brewing among jurists and practitioners alike as to the scope of *Crystalline*, and, far more tantalizing, rumours abound as to some perhaps unintended legal consequences arising from the decision which may have even greater impact on landlord and tenant law than *Cummer-Yonge* ever did. Indeed, we submit that legal history may ultimately record *Crystalline* as being the case that re-opened a line of legal argument long

since thought settled, rather than simply the case that finally closed the door on *Cummer-Yonge*. Alas, these theories are not yet fully developed and it would be perhaps premature to raise them now in a published forum.

Stay tuned . . .

Jeffrey W. Lem

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Transco Mills Ltd. v. Percan Enterprises Ltd. (1993), 76 B.C.L.R. (2d) 129, 100 D.L.R. (4th) 359, 29 R.P.R. (2d) 235, 23 B.C.A.C. 181, 39 W.A.C. 181, 1993 CarswellBC 19 (B.C. C.A.) — considered

Warnford Investments Ltd. v. Duckworth (1977), [1979] Ch. 127, [1978] 2 All E.R. 517 (Eng. Ch. Div.) — considered

Wotherspoon v. Canadian Pacific Ltd. (1979), 22 O.R. (2d) 385, 92 D.L.R. (3d) 545, 1979 CarswellOnt 758 (Ont. H.C.) — considered

Statutes considered:

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

Generally — considered

Pt. III — referred to

s. 62(3) — considered

s. 65.2 [en. 1992, c. 27, s. 30; am. 1997, c. 12, s. 42] — considered

s. 65.2(1) [en. 1992, c. 27, s. 30] — considered

s. 65.2(2) [en. 1992, c. 27, s. 30] — considered

s. 65.2(3) [en. 1992, c. 27, s. 30] — referred to

s. 65.2(4) [en. 1992, c. 27, s. 30] — considered

s. 65.2(5) [en. 1992, c. 27, s. 30] — considered

s. 65.2(6) [en. 1992, c. 27, s. 30] — considered

s. 179 — considered

Landlord and Tenant (Covenants) Act 1995, (U.K.), c. 30

Generally — referred to

Rules considered:

Rules of Civil Procedure, R.R.O. 1990, Reg. 194

R. 20.04(2) — considered

APPEAL by tenant from judgment reported at 2002 CarswellOnt 705, 31 C.B.R. (4th) 225, 210 D.L.R. (4th) 659, 156 O.A.C. 392, 58 O.R. (3d) 549, 49 R.P.R. (3d) 171, 27 B.L.R. (3d) 102 (Ont. C.A.) allowing landlords' appeal from decision granting tenant's motion for summary judgment dismissing landlords' actions for rent arrears and other damages.

POURVOI de la locataire à l'encontre de l'arrêt publié à 2002 CarswellOnt 705, 31 C.B.R. (4th) 225, 210 D.L.R. (4th) 659, 156 O.A.C. 392, 58 O.R. (3d) 549, 49 R.P.R. (3d) 171, 27 B.L.R. (3d) 102 (Ont. C.A.), qui a accueilli le pourvoi des locatrices à l'encontre du jugement qui avait accueilli la requête pour jugement sommaire de la locataire et rejeté les actions des locatrices en paiement des arrérages de loyer et d'autres dommages-intérêts.

***Major J.*:**

I. Introduction

1 This appeal arises from a motion for summary judgment. The facts are undisputed. The respondents, Crystalline Investments Limited ("Crystalline") and Burnac Leaseholds Limited ("Burnac"), while owners of different properties, are referred to collectively as the landlords.

2 Dominion Stores Limited was the original tenant of the landlords. It is not clear from the record nor is it relevant whether Dominion Stores Limited became Domgroup Limited ("Domgroup") by reorganization or by a change of name. For purposes of this appeal, the appellant Domgroup can be viewed as the original tenant.

3 Domgroup assigned the leases to Coastal Foods Limited, ("Coastal Foods"), a wholly owned subsidiary. The consent of the landlords was not required under the leases for the assignments. Domgroup subsequently sold Coastal Foods which amalgamated to form Food Group Inc. ("Food Group"). Food Group later became insolvent and attempted a reorganization under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, as amended to 1994.

4 The question is whether the terms of the reorganization by the insolvent assignee through its trustee where it purported to repudiate the leases under s. 65.2 of the Act affect the obligations between the landlords and the original tenant.

5 The procedure for granting summary judgment in Ontario was set out in rule 20.04(2) of the *Rules of Civil Procedure*, R.R.O. 1990, Reg. 194. That rule provided as follows at the time:

> **20.04** . . .
>
> (2) Where the court is satisfied that there is no genuine issue for trial with respect to a claim or defence, the court shall grant summary judgment accordingly.

6 In *Guarantee Co. of North America v. Gordon Capital Corp.*, [1999] 3 S.C.R. 423 (S.C.C.), at para. 27, Iacobucci and Bastarache JJ. discussed the legal principles that govern a motion for summary judgment:

> The appropriate test to be applied on a motion for summary judgment is satisfied when the applicant has shown that there is no genuine issue of material fact requiring trial, and therefore summary judgment is a proper question for consideration by the court. See *Hercules Managements Ltd. v. Ernst & Young*, [1997] 2 S.C.R. 165, at para. 15; *Dawson v. Rexcraft Storage and Warehouse Inc.* (1998), 164 D.L.R. (4th) 257 (Ont. C.A.), at pp. 267-68; *Irving Ungerman Ltd. v. Galanis* (1991), 4 O.R. (3d) 545 (C.A.), at pp. 550-51. Once the moving party has made this showing, the respondent must then "establish his claim as being one with a real chance of success" (*Hercules*, *supra*, at para. 15).

The parties do not dispute the test for summary judgment.

7 The motions judge held that notices of repudiation given under s. 65.2 terminated the leases for all purposes. Relying on *Cummer-Yonge Investments Ltd. v. Fagot*, [1965] 2 O.R. 152 (Ont. H.C.), he found that, since the leases no longer existed, the liabilities that would have been owed by the original tenant to the landlords also disappeared. He granted summary judgment dismissing the claims of the landlords who sought damages from the original tenant. The Ontario Court of Appeal reversed the trial judge and held that the rights between the landlords and the original tenant were unaffected by proceedings under s. 65.2. The appeal was allowed and the summary judgments set aside.

8 For the reasons that follow, I agree with the Ontario Court of Appeal that the insolvency of the assignee and the order made pursuant to the Act do not affect the landlords who can continue to look to the original tenant for enforcement of the leases. The order affects the insolvent assignee and its creditors, including the original tenant and assignor of the leases, but does not reach to the landlords. I would dismiss the appeal.

9 In this appeal, the appellant sought to rely on certain common law remedies and, in particular, advanced the defence of surrender which was neither pleaded nor raised before the motions judge or the Court of Appeal. Surrender must be pleaded. See *McNeil v. Train* (1848), 5 U.C.Q.B. 91 (U.C. Q.B.); *Wotherspoon v. Canadian Pacific Ltd.* (1979), 22 O.R. (2d) 385 (Ont. H.C.), at p. 562. In these circumstances the court refused to consider the question.

10 This appeal is limited to confirming that Food Group's repudiation of the leases assigned to it by Domgroup did not, by virtue of s. 65.2 alone, terminate Domgroup's rights and obligations under the leases. Section 65.2 relates to the repudiation of leases by insolvent commercial tenants. It is not concerned with the effects of that repudiation on third parties, such as assignors and guarantors. Whether the leases were terminated by surrender, as Domgroup argues for the first time in the Court, or by the application of some other principle of common law, is a question best left for trial.

II. Background

11 On April 30, 1979, Domgroup leased premises from Crystalline. On April 24, 1980, Domgroup leased a different location from Burnac. Both premises were located in New Brunswick. The leases had 25-year terms and contained the following assignment clause:

> Notwithstanding any assignment or sublease the Lessee shall remain fully liable under this lease and shall not be released from performing any of its covenants, obligations or agreements in this lease and shall continue to be bound by this lease.

12 On May 25, 1985, Domgroup assigned both leases to Coastal Foods which later became Food Group.

13 Food Group encountered financial difficulty and attempted a reorganization. In February of 1994, Food Group filed a notice of intention to make a proposal pursuant to Part III of the Act.

14 Food Group then prepared and filed its proposal, stating that it believed the proposal would be "of benefit to its creditors and employees, and will enable the Food Group to continue in business, albeit on a much reduced scale". Part of the proposal was that Food Group's leases with Burnac and Crystalline be terminated pursuant to s. 65.2.

15 On February 18, 1994, the insolvent Food Group, through its trustee, gave the original landlords, Burnac and Crystalline, notice of its intention to repudiate the leases. Neither Burnac nor Crystalline applied to the court to challenge the repudiation of the lease although entitled to do so under the Act. At no time did Food Group advise Domgroup of the proceedings.

16 On March 18, 1994, the proposal was approved by the Court of Queen's Bench for New Brunswick in Bankruptcy. On March 24, 1994, Burnac and Crystalline received compensation payments of $173,704.39 and $131,154.54, respectively, being the equivalent of six months rent under the leases pursuant to s. 65.2(3) of the Act. The repudiation was declared to be effective as of March 31, 1994.

17 Food Group vacated Crystalline's premises in March of 1994. It had previously vacated Burnac's premises one year earlier, but had continued to pay rent.

18 Burnac, one of the original landlords, entered into short-term leases with a bingo operation and started modifications to the premises to accommodate another tenant. Similarly, the other landlord, Crystalline, licensed its premises to kiosk-based vendors.

19 On January 20, 1995, Burnac and Crystalline informed the original tenant, Domgroup, by mail that the insolvent, Food Group, had repudiated the leases. At the same time, they asserted their rights to be paid outstanding rent pursuant to the assignment clause in the leases. The letters did not acknowledge the termination of the leases as of March 31, 1994.

20 Domgroup declined to pay. Burnac and Crystalline both sued in Ontario Superior Court. Domgroup, on application, was granted summary judgment in both cases. Both were later reversed by the Ontario Court of Appeal.

III. Relevant Statutory Provisions

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

> 65.2 (1) At any time between the filing of a notice of intention and the filing of a proposal, or on the filing of a proposal, in respect of an insolvent person who is a commercial tenant under a lease of real property, the insolvent person may repudiate the lease on giving thirty days notice to the landlord in the prescribed manner, subject to subsection (2).
>
> (2) Within fifteen days after being given notice of the repudiation of a lease under subsection (1), the landlord may apply to the court for a declaration that subsection (1) does not apply in respect of that lease, and the court, on notice to such parties as it may direct, shall make such a declaration unless the insolvent person satisfies the court that the insolvent person would not be able to make a viable proposal, or that the proposal the insolvent person has made would not be viable, without the repudiation of that lease and all other leases that the tenant has repudiated under subsection (1).
>
> (3) Where a lease is repudiated pursuant to subsection (1), a proposal filed by the insolvent person must provide for payment to the landlord, immediately after court approval of the proposal, of compensation equal to the lesser of
>
> (a) an amount equal to six months rent under the lease, and
>
> (b) the rent for the remainder of the lease, from the date on which the repudiation takes effect.
>
> (4) For the purpose of voting on any question relating to a proposal referred to in subsection (3), the landlord does not have any claim in respect of accelerated rent, damages arising out of the repudiation, or the compensation referred to in subsection (3).

(5) Nothing in subsections (1) to (4) affects the operation of section 146 in the event of bankruptcy.

(6) Where an insolvent person who has made a proposal referred to in subsection (3) becomes bankrupt

(a) after court approval of the proposal and before the proposal is fully performed, and

(b) after compensation referred to in subsection (3) has been paid,

the landlord has no claim against the estate of the bankrupt for accelerated rent.

IV. Judicial History

A. Ontario Superior Court of Justice (2001), 39 R.P.R. (3d) 49 (Ont. S.C.J.)

22 The motions for summary judgment by Domgroup were heard by Trafford J. on March 1, 2001, and by consent, the legal issue was stated as follows:

> Is a landlord, following the Court-approved termination of a commercial lease under s. 65.2 of the 1992 Act and following acceptance of the compensation provided for by the statutory code, entitled to arrears of rent, or for damages, in respect of the unexpired term of the terminated lease as against the pre-proposal assignor of the lease?

23 The motions judge held that the court-approved termination of the leases ended all obligations of the parties and rendered the assignment clause inoperative. The compensation paid to the landlords under s. 65.2 constituted the total compensation for all damages to which they were entitled under the leases. Since the entire lease, including the assignment clause, was terminated by the court order, there was no basis in law for the claims made against the original tenant, Domgroup. He granted summary judgment in both cases.

B. Ontario Court of Appeal (2002), 58 O.R. (3d) 549 (Ont. C.A.)

24 The Ontario Court of Appeal rejected the conclusion of the motions judge that the provisions of s. 65.2 terminated the leases for all purposes. In the view of Carthy J.A., the rights between the landlords and the original tenant were unaffected by the insolvency proceedings. He found no change in this result was warranted by the 1997 amendment to the English version of s. 65.2 from the term "repudiate" to "disclaim".

25 The Court of Appeal held that the consequences of repudiation should be restricted to those provided for in s. 65.2 having regard to the purposes of insolvency proceedings as a whole. While the insolvency proceedings permitted Food Group as the insolvent to shed its obligations, the rights and liabilities of Domgroup to the landlords under the leases remained intact.

V. Analysis

A. The Construction of Section 65.2

26 The dispute is whether the Act has relieved the appellant Domgroup of its obligations by the assignment of the leases ultimately to the insolvent. More precisely, should s. 65.2 be interpreted to bring all the obligations between the appellant and respondents to an end when the leases were repudiated by the insolvent, Food Group?

27 While the drafting of s. 65.2 focusses on bilateral relationships, such as a simple lease between a landlord and a tenant, the effect of the repudiation does not change in circumstances such as the present ones, involving a tripartite arrangement resulting from the assignment of a lease. In both situations, the repudiation must be construed as benefiting only the insolvent.

28 I, thus, agree with the Court of Appeal that s. 65.2 should be read narrowly. The plain purposes of the section are to free an insolvent from the obligations under a commercial lease that have become too onerous, to compensate the landlord for the early determination of the lease, and to allow the insolvent to resume viable operations as best it can. Nothing in s. 65.2, or any part of the Act, protects third parties (i.e., guarantors, assignors or others) from the consequences of an insolvent's repudiation of a commercial lease. That is to say that they remain liable when the party on whose behalf they acted becomes insolvent.

29 When a lease is finalized, the landlord and tenant then have privity of contract and privity of estate. See *Francini v. Canuck Properties Ltd.* (1982), 35 O.R. (2d) 321 (Ont. C.A.), at pp. 322-23. When the lease is assigned, the landlord's privity of estate with the original tenant comes to an end, but the privity of contract continues and the original tenant remains liable upon its covenant. The estate or interest in the tenancy is transferred to the assignee, who, by being entitled to possession, is obliged to make payment of rent, but, subject to the terms of the lease and the agreement of the parties, the original tenant remains liable should his assignee not pay the rent. See C. S. Goldfarb, "The Rights and Obligations of the Original Tenant and Subsequent Tenants after an Assignment of Lease", in H. M. Haber, ed., *Assignment, Subletting and Change of Control in a Commercial Lease* (2002), 157.

30 Both the British Columbia Court of Appeal in *Transco Mills Ltd. v. Percan Enterprises Ltd.* (1993), 100 D.L.R. (4th) 359 (B.C. C.A.), at p. 366, and Carthy J.A., here, at para. 16, quoted from Vice-Chancellor Megarry in *Warnford Investments Ltd. v. Duckworth* (1977), [1978] 2 All E.R. 517 (Eng. Ch. Div.), at p. 526, where the position of an original tenant in bankruptcy proceedings is discussed. It is worth repeating:

> The original lessee is a person who as principal, undertook towards the lessor, the obligations of the lease for the whole term; and there is nothing in the process of assignment which replaced this liability by the mere collateral liability of a surety who must pay the rent only if the assignee does not. The bankruptcy of the assignee has for the time being destroyed the original lessee's right against the assignee to require him to discharge the obligations of the lease, and it has impaired the lessee's right of indemnity against him when he has to discharge the obligations himself; but it has not affected his primary liability towards the lessor, which continues unaffected. At no time does an original lessee become a mere guarantor to the lessor of the liability of any assignee of the lease.
>
> [Emphasis added.]

31 From the time a lease is completed, the original tenant is bound by all the conditions, including the term. Despite the hardship that may later develop, the covenant is fully enforceable even if it has been assigned. In England, however, public concern over the continuing liability of original tenants in post-assignment bankruptcy situations resulted in the enactment of the *Landlord and Tenant (Covenants) Act 1995* (U.K.), 1995, c. 30. As a result, when a tenant in England lawfully assigns a lease, that tenant will have no further obligations with respect to the covenant. To effect the same result in Canada, similar legislation is needed.

B. Does the Common Law Indemnification Right Frustrate the Act?

32 If the liabilities remain enforceable by the landlord against the original tenant, then presumably the original tenant can exercise its common law indemnification rights against its assignee as an unsecured creditor. See *Peterborough Hydraulic Power Co. v. McAllister* (1908), 17 O.L.R. 145 (Ont. C.A.), at p. 151. The original tenant could therefore prove a claim in insolvency against that assignee under this right of indemnity. As a result, the insolvent assignee could face an additional claim on the lease in excess of the preferred payment required to be paid to the landlord under s. 65.2.

33 The appellant submits this result would frustrate the objectives of the Act and is the reason that a repudiation under s. 65.2 should terminate a lease for all purposes. I disagree for two reasons.

34 First, an assignor is no different from other alternative debtors, none of which is excused under the Act. For example, s. 179 states:

> **179.** An order of discharge does not release a person who at the date of the bankruptcy was a partner or co-trustee with the bankrupt or was jointly bound or had made a joint contract with him, or a person who was surety or in the nature of a surety for him.

While s. 62(3) provides:

> **62.** (3) The acceptance of a proposal by a creditor does not release any person who would not be released under this Act by the discharge of the debtor.

Parliament therefore saw fit to conserve the liabilities of alternative debtors, yet chose not to extinguish their common law rights of indemnity.

35 Second, where an original tenant seeks indemnification on a contingent claim, provided the claim is provable and not disallowed, it would fall into the insolvency to be dealt with in accordance with the scheme of the Act. The assignor simply joins the other unsecured creditors in the proceedings. If such a claim is approved, it cannot satisfy and at the same time frustrate the Act.

36 Simply stated, the mere possibility that the original tenant may have a right of indemnity against his insolvent assignee and is able to make a claim to participate in the proposal proceedings as an unsecured creditor is not inconsistent with the statutory scheme. On the contrary, it is consistent with the circumstances applicable to other alternative covenantors, and does not affect or alter the nature of the original tenant's contractual relationship and obligations. More importantly, it does not require that the original tenant be discharged from liability.

37 I also question whether there is any justification for distinguishing between a guarantor and an assignor post-disclaimer. In *Cummer-Yonge*, *supra*, the landlord brought an action against guarantors of a bankrupt tenant for the unpaid rent accruing after the tenant's bankruptcy but prior to the reletting of the leased premises. The trustee in bankruptcy had disclaimed the lease in accordance with the trustees' rights under the then applicable federal bankruptcy and provincial landlord and tenancy legislation. The guarantee provision contained in the disclaimed lease provided as follows (at p. 153):

> The Guarantors if one is a party hereto join for the first five (5) years of the term hereby granted for valuable consideration and for the purpose of guaranteeing the due performance by the Lessee of all its covenants in this lease including the covenant to pay rent on the part of the Lessee to be performed.

38 Gale C.J.H.C. applied the reasoning of the English Court of Appeal in *Stacey v. Hill*, [1901] 1 Q.B. 660 (Eng. C.A.). He read the guarantee clause strictly as a pure surety provision and found that when the lease was disclaimed by a trustee in bankruptcy, the bankrupt's covenants to perform were dissolved. Since the guarantors' obligation is to assure performance of those covenants, their obligations disappeared with the covenants. The Ontario Court of Appeal affirmed the decision without reasons ([1965] 2 O.R. 157n (Ont. C.A.)).

39 *Cummer-Yonge* has created uncertainty in leasing and bankruptcy. Not only have drafters of leases attempted to circumvent the holding in *Cummer-Yonge* by playing upon the primary and secondary obligation distinction, but courts have also performed what has been called "tortuous distinctions" in order to reimpose liability on guarantors. See J. W. Lem and S. T. Proniuk, "Goodbye '*Cummer-Yonge*': A Review of Modern Developments in the Law Relating to the Liability of Guarantors of Bankrupt Tenants" (1993), 1 *D.R.P.L.* 419, at p. 436.

40 Despite the division over *Cummer-Yonge*, the distinction between guarantors as having secondary obligations that disappear when a lease is disclaimed by a trustee in bankruptcy, and assignors as having primary obligations that survive a disclaimer, thrives in Canadian case law.

41 Not surprisingly, *Stacey v. Hill*, *supra*, led to a similar situation in England. In *Hindcastle Ltd. v. Barbara Attenborough Associates Ltd.*, [1996] 1 All E.R. 737 (U.K. H.L.), Lord Nicholls, faced with facts involving a guarantor of an assignor of a lease, gave a convincing illustration of the absurdity of maintaining this distinction, at p. 754:

> This would make no sort of legal or commercial sense. This would mean that directors who guarantee their company's obligations would not be liable if their own company became insolvent whilst tenant, but they would be liable if an assignee from their company encountered financial difficulties whilst tenant. Mr. Whitten, as guarantor of CIT's obligations, remains liable to the landlord. According to *Stacey v. Hill*, had he been a guarantor of Prest's liabilities [the assignee who became bankrupt], the disclaimer would have released him. What sort of a law would this be?
>
> [Emphasis in original.]

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.

43 The appellant submits that the English bankruptcy statute that was applied in *Hindcastle* clearly stated that disclaimer will not "affect the rights or liabilities of any other person", and that s. 65.2 of the Act has no similar wording. I agree with the respondents' rebuttal to this argument that the English wording affirms the ordinary construction of the statute. In other words, explicit statutory language is required to divest persons of rights they otherwise enjoy at law. As Carthy J.A. observed in the Court of Appeal, at paras. 11-12, the lease may have real value to the original tenant and, on the wording of s. 65.2, cannot be eliminated in the absence of the original tenant's agreement. In any event, so long as the doctrine of paramountcy is not triggered, federally regulated bankruptcy and insolvency proceedings cannot be used to subvert provincially regulated property and civil rights. See *Husky Oil Operations Ltd. v. Minister of National Revenue*, [1995] 3 S.C.R. 453 (S.C.C.); *Giffen, Re*, [1998] 1 S.C.R. 91 (S.C.C.).

44 As previously noted, the appellant sought to argue surrender in this Court despite not having pleaded surrender in either action as a defence, and not raising the issue before the motions judge or the Court of Appeal. Like the other defences, surrender represents an issue for trial. The decision whether to allow amendments to the pleadings, and on what terms if any, should be left to the trial judge.

VI. Disposition

45 I would dismiss the appeal and award the respondents their costs in this Court and below.

Appeal dismissed.

Pourvoi rejeté.

TAB 11

Most Negative Treatment: Application/Notice of Appeal
Most Recent Application/Notice of Appeal: R. v. Puddicombe | 2014 CarswellOnt 554 | (S.C.C., Jan 22, 2014)

2013 ONCA 506
Ontario Court of Appeal

R. v. Puddicombe

2013 CarswellOnt 10743, 2013 ONCA 506, [2013] O.J. No. 3507, 108 W.C.B. (2d) 650, 299 C.C.C. (3d) 534, 308 O.A.C. 70, 5 C.R. (7th) 31

Her Majesty the Queen, Respondent and Nicola Puddicombe, Appellant

Doherty, Rosenberg, Simmons, Armstrong, Tulloch JJ.A.

Heard: January 30-31, 2013
Judgment: August 7, 2013
Docket: CA C52286

Counsel: David E. Harris, for Appellant
Elise Nakelsky, for Respondent
John North, Iona Jaffe, for Intervener, Public Prosecution Service of Canada
Peter Copeland, Ryan Clements, for Intervener, Criminal Lawyers' Association (Ontario)

Subject: Criminal; Evidence; Civil Practice and Procedure
Related Abridgment Classifications
Criminal law
XIX Attempts, conspiracies and accessories
XIX.2 Conspiracy
XIX.2.c Evidence
XIX.2.c.i Co-conspirators
Criminal law
XXXII Jury
XXXII.2 Charging jury
XXXII.2.c Direction on theory of Crown
Criminal law
XXXII Jury
XXXII.2 Charging jury
XXXII.2.e Review of evidence
XXXII.2.e.iii Miscellaneous
Criminal law
XXXII Jury
XXXII.2 Charging jury
XXXII.2.f Direction on corroboration
XXXII.2.f.ii Accomplices and witnesses of disreputable character [Vetrovec]
Criminal law
XXXII Jury
XXXII.2 Charging jury
XXXII.2.i Direction on circumstantial evidence

Evidence
IX Hearsay
IX.3 Traditional exceptions to rule against admission
IX.3.a Admissions and adoptive statements
IX.3.a.ii Co-conspirator statements
Judges and courts
XVIII Stare decisis
XVIII.10 Obiter dicta
XVIII.10.d Of Supreme Court of Canada

Headnote

Criminal law --- Offences — Conspiracy — Evidence — Co-conspirators — Declarations of co-conspirators in furtherance of conspiracy

Accused was charged with first degree murder in beating death of her boyfriend — Crown alleged that accused and her girlfriend P conspired to murder victim, P carried out beating, and accused was liable as aider or abettor — P confessed that she acted alone and accused had nothing to do with murder — Confession was excluded from evidence at P's trial and she was acquitted — At accused's trial, Crown relied on co-conspirator's exception to hearsay rule for P's statements to be admissible against accused — Trial judge gave jury "Carter instruction" on three-step process exception to hearsay rule for use of statements of one co-conspirator against other to prove guilt — Accused was convicted and appealed, submitting that three-step instruction should not apply to two-person conspiracy because of substantial risk that jury would conflate steps and conclude that proof of conspiracy constituted proof of participation in conspiracy — Appeal dismissed — Carter instruction applies to two-person conspiracies — Trial judge did not expressly instruct jury that accused's participation in planning and execution of plan to kill deceased would constitute abetting and/or counselling, but tenor of her instructions conveyed that message — Defence submitted that court should reverse its holding in R. v. Bogiatzis and declare that Carter instruction should not be given where Crown alleges two-person conspiracy — It was previously held that binding obiter dicta in Supreme Court of Canada declared that Carter instruction applies to two-person conspiracy — Bogiatzis was correctly decided — Apart from obligations of stare decisis, properly tailored Carter instruction can be given in cases involving alleged two-person agreement — Trial judge made no reversible error.

Evidence --- Hearsay — Exceptions — Co-conspirators

Accused was charged with first degree murder in beating death of her boyfriend — Crown alleged that accused and her girlfriend P conspired to murder victim, P carried out beating, and accused was liable as aider or abettor — P confessed that she acted alone and accused had nothing to do with murder — Confession was excluded from evidence at P's trial and she was acquitted — At accused's trial, Crown relied on co-conspirator's exception to hearsay rule for P's statements to be admissible against accused — Trial judge gave jury "Carter instruction" on three-step process exception to hearsay rule for use of statements of one co-conspirator against other to prove guilt — Accused was convicted and appealed, submitting that three-step instruction should not apply to two-person conspiracy because of substantial risk that jury would conflate steps and conclude that proof of conspiracy constituted proof of participation in conspiracy — Appeal dismissed — Carter instruction applies to two-person conspiracies — Trial judge did not expressly instruct jury that accused's participation in planning and execution of plan to kill deceased would constitute abetting and/or counselling, but tenor of her instructions conveyed that message — Defence submitted that court should reverse its holding in R. v. Bogiatzis and declare that Carter instruction should not be given where Crown alleges two-person conspiracy — It was previously held that binding obiter dicta in Supreme Court of Canada declared that Carter instruction applies to two-person conspiracy — Bogiatzis was correctly decided — Apart from obligations of stare decisis, properly tailored Carter instruction can be given in cases involving alleged two-person agreement — Trial judge made no reversible error.

Judges and courts --- Stare decisis — Obiter dicta — Of Supreme Court of Canada

Accused was charged with first degree murder in beating death of her boyfriend — Crown alleged that accused and her girlfriend P conspired to murder victim, P carried out beating, and accused was liable as aider or abettor — P confessed that she acted alone and accused had nothing to do with murder — Confession was excluded from evidence at P's trial and she was acquitted — At accused's trial, Crown relied on co-conspirator's exception to hearsay rule for P's statements to be admissible against accused — Trial judge gave jury "Carter instruction" on three-step process exception to hearsay

rule for use of statements of one co-conspirator against other to prove guilt — Accused was convicted and appealed, submitting that court should reverse its holding in R. v. Bogiatzis and declare that Carter instruction should not be given where Crown alleges two-person conspiracy — Appeal dismissed — It was held in Bogiatzis that binding obiter dicta in Supreme Court of Canada in R. v. Barrow declared that Carter instruction applies to two-person conspiracy — Court was being asked to hold that obiter in decision of Supreme Court of Canada was not binding and to depart from its prior holding wherein it declared that obiter was binding — Bogiatzis was correctly decided — Obiter in Barrow was binding — Carter instruction applies to two-person conspiracies — Doctrine of stare decisis precluded revision of rule set down by Supreme Court — Apart from obligations of stare decisis, and bearing in mind functional purpose underlying all jury instructions, properly tailored Carter instruction can be given in cases involving alleged two-person agreement — Trial judge made no reversible error.

Criminal law --- Trial procedure — Charging jury or self-instruction — Direction on corroboration — Accomplices and witnesses of disreputable character — Accomplice

Accused was charged with first degree murder in beating death of her boyfriend — Crown alleged that accused and her girlfriend P conspired to murder victim, P carried out beating, and accused was liable as aider or abettor — P confessed that she acted alone and accused had nothing to do with murder — Confession was excluded from evidence at P's trial and she was acquitted — At accused's trial, Crown relied on co-conspirator's exception to hearsay rule for P's statements to be admissible against accused — Trial judge gave jury "Carter instruction" on three-step process exception to hearsay rule for use of statements of one co-conspirator against other to prove guilt — Accused was convicted and appealed, submitting that three-step instruction should not apply to two-person conspiracy because of substantial risk that jury would conflate steps and conclude that proof of conspiracy constituted proof of participation in conspiracy — Appeal dismissed — Carter instruction applies to two-person conspiracies — Trial judge did not expressly instruct jury that accused's participation in planning and execution of plan to kill deceased would constitute abetting and/or counselling, but tenor of her instructions conveyed that message — It was previously held that binding obiter dicta in Supreme Court of Canada declared that Carter instruction applies to two-person conspiracy — Apart from obligations of stare decisis, properly tailored Carter instruction can be given in cases involving alleged two-person agreement — Proper instruction in case involving two-person conspiracy would not only make three-step Carter instruction clear to jury, but would also caution against following incorrect path directly from stage one to conviction — Trial judge made no reversible error.

Criminal law --- Trial procedure — Charging jury or self-instruction — Direction on theory of Crown

Party liability — Accused was charged with first degree murder in beating death of her boyfriend — Crown alleged that accused and her girlfriend P conspired to murder victim, P carried out beating, and accused was liable as aider or abettor — P confessed that she acted alone and accused had nothing to do with murder — Confession was excluded from evidence at P's trial and she was acquitted — At accused's trial, Crown relied on co-conspirator's exception to hearsay rule for P's statements to be admissible against accused — Accused was convicted and appealed, submitting that trial judge erred in her party liability instruction — Appeal dismissed — Trial judge defined aiding, abetting and counselling for jury and reviewed evidence relevant to each mode of criminal participation — On evidence, jury could find that accused encouraged P to murder victim by leading P to believe that victim was abusing her and that she could be safe and with P only if victim were killed — Trial judge also told jury that evidence of what accused did after murder could provide evidence that she had aided or abetted murder by agreeing to and participating in plan formulated with P to murder victim and mislead police — Instructions with respect to aiding and abetting were correct in law — Trial judge also correctly instructed jury to consider, in assessing whether accused manipulated P into agreeing to murder victim, all of evidence about formation and development of relationship between accused and P — There was cogent evidence that P was obsessed with accused, believed that victim was abusing accused, wanted to protect accused from victim, and feared victim — Trial judge's review of evidence pertaining to victim's abuse of accused was not skewed in favour of Crown.

Criminal law --- Trial procedure — Charging jury or self-instruction — Direction on circumstantial evidence

Inferences from post-offence conduct properly left with jury.

Criminal law --- Trial procedure — Charging jury or self-instruction — Review of evidence — Miscellaneous

Leaving with jury possibility that accused was guilty of murder as perpetrator.

Annotation

In *R. v. Puddicombe*, Doherty J.A. offers a characteristically clear analysis of a difficult evidence problem: the applicability of the notoriously complex *Carter* rule in the context of a two-person conspiracy. In one respect, however, the analysis may invite some linguistic and conceptual slippage. In describing the way the rule applied in the case at hand, Doherty J.A. described the question at step one of the *Carter* analysis as whether there is proof beyond a reasonable doubt of the existence of the alleged murder *plan*. This way of framing the issue seems distinct from the way step one of the *Carter* analysis is normally described, as a question whether there is proof beyond a reasonable doubt of the existence of the *conspiracy* or *agreement*. The problem is that while a conspiracy or an agreement can only exist between two or more persons, a plan can exist entirely in the head of one person. Potentially, therefore, framing the question as involving the existence of a plan risks misleading the jury into thinking this requirement can be met without any meeting of the minds.

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APPEAL by accused from conviction for first degree murder.

***Doherty J.A.*:**

I

Overview of the Appeal

1 The appellant appeals her conviction on a charge of first degree murder. Counsel advances several grounds of appeal, all of which arise out of the jury instructions. [1]

2 The Crown alleged that the appellant and her girlfriend planned the murder of the victim and that the girlfriend murdered the victim pursuant to that plan. It was the Crown's position that the appellant was liable as an aider, abetter or counsellor. The trial judge, following this court's judgment in *R. v. Bogiatzis*, 2010 ONCA 902, 285 C.C.C. (3d) 437 (Ont. C.A.), gave the jury what is known as a *Carter* instruction. That instruction explains to a jury how and when the acts and declarations of one alleged party to an agreement to commit a crime can be used against another party to that agreement.

3 Most of the arguments made on appeal were directed at the *Carter* instruction. Those submissions fall into two categories. First, counsel argued that this court should reverse its holding in *Bogiatzis* and declare that the *Carter* instruction should not be given where the Crown alleges a two-person agreement to commit the crime. Counsel argues that the *Carter* instruction creates the very real risk that the jury will use evidence of the acts and declarations of the other alleged party to the agreement to convict an accused even where those acts and declarations are not properly admissible against the accused.

4 This court determined in *Bogiatzis* that binding *obiter dicta* in *R. v. Barrow*, [1987] 2 S.C.R. 694 (S.C.C.) declared that the *Carter* instruction applied to a two-person conspiracy. Consequently, a five judge panel was convened to consider whether *Bogiatzis* was correctly decided. The Public Prosecution Service of Canada intervened to support the Crown's

contention that *Bogiatzis* was correctly decided. The Criminal Lawyers' Association (Ontario) intervened to support the appellant's contention that *Bogiatzis* should be overruled.

5 The second category of submissions challenging the *Carter* instruction accepts that *Bogiatzis* was properly decided and the *Carter* instruction applies to a two-person agreement. Counsel submits that the trial judge made various errors in her *Carter* instruction.

6 I would reject the arguments aimed at the *Carter* instruction. I think *Bogiatzis* was correctly decided. I am also satisfied that apart from the obligations of *stare decisis*, and bearing in mind the functional purpose underlying all jury instructions, a *Carter* type instruction, properly tailored to the individual case, can be given in cases involving an alleged two-person agreement. With respect to the alleged errors in the trial judge's *Carter* instruction, while as with virtually any jury instruction hindsight reveals possible improvements, none of the shortcomings rise to the level of reversible error.

7 I also would not give effect to the grounds of appeal involving the issues other than the *Carter* instruction. Those grounds of appeal will be addressed at the end of these reasons.

II

Overview of the Trial Proceeding

8 On October 27, 2006 in the early morning, Dennis Hoy, the appellant's boyfriend, was struck six times on the head with the blunt end of an axe while he lay asleep in the appellant's bed. He was dead when the paramedics arrived. Later that day, the police, on the strength of a confession obtained after lengthy questioning, charged Ashleigh Pechaluk, the appellant's roommate and girlfriend with murder. In her confession, Pechaluk indicated that the appellant had nothing to do with the homicide.

9 The police investigation continued after Pechaluk's arrest. In March 2007, the police charged the appellant with Hoy's murder. The police believed that Pechaluk and the appellant had planned the murder together and had fabricated a story involving an unknown intruder who came into the apartment and murdered Hoy while the appellant was in the shower. The police believed that Pechaluk had wielded the axe and the appellant had misled the police as planned.

10 The Crown proceeded separately against Pechaluk and the appellant. Pechaluk was tried first. Her confession was excluded from evidence and she was acquitted.

11 The Crown called Pechaluk at the appellant's trial. By the time of the appellant's trial, Pechaluk and the appellant were estranged. Pechaluk, who was very much in love with the appellant, had learned after the appellant's arrest in March 2007 that the appellant had become pregnant while Pechaluk was in custody. Pechaluk felt betrayed.

12 According to Pechaluk's trial testimony, the appellant had raised the possibility of murdering Hoy many times with Pechaluk. In the days before Hoy's murder, the appellant had devised a plan whereby she would see to it that Hoy fell asleep in her bed. The appellant would then signal Pechaluk who would come into the bedroom and beat Hoy to death with a baseball bat. The appellant would call the police and tell them that Hoy had been killed by an intruder while she was in the shower. The appellant told Pechaluk that she would make the story about the intruder more believable by telling the police that Hoy had extensive connections to criminal gangs and had been involved in serious criminal activity.

13 Pechaluk testified that when the time came, she could not go through with the plan. The appellant, however, came to her later the same evening and told her that Hoy had been beaten to death by an intruder while she was in the shower. The appellant called 911 and when the police arrived told them the "intruder" story just as she and Pechaluk had discussed in the days leading up to the murder.

14 It was the Crown's position at trial that the appellant wanted Hoy dead for two reasons. He had been unfaithful to her and she was his beneficiary under his pension plan and life insurance policy. The appellant stood to gain over $250,000 from Hoy's death.

15 The Crown argued that the appellant used Pechaluk to kill Hoy. The appellant knew that Pechaluk, who was about 11 years younger than the appellant, was infatuated with her. The appellant manipulated Pechaluk by pretending that she wanted to spend her life with Pechaluk if only she could get away from Hoy. The appellant led Pechaluk to believe that Hoy was abusive, had an extensive criminal background and would kill the appellant rather than let her be with Pechaluk. On the Crown's theory, Pechaluk joined in the appellant's murder plot firmly believing that Hoy's murder was morally justified.

16 The appellant did not testify and did not call a defence. The defence argued to the jury that Pechaluk, as she initially told the police, acted on her own when she murdered Hoy. The defence maintained that the appellant's statement to the police when they first arrived at her apartment was the truth as far as she knew it at that time. She believed that an intruder had come into her bedroom and killed Hoy while she was in the shower.

III

The Evidence

A. The Evidence of Pechaluk

17 The Crown's case depended mainly on Pechaluk's testimony. The summary set out below, to the extent that it describes discussions between Pechaluk and the appellant, is taken from Pechaluk's evidence. Her credibility was vigorously challenged at trial.

18 The appellant and Hoy had been in a relationship for about 11 years at the time of his death in October 2006. In the last year of that relationship, Hoy was seeing other women and the appellant had become romantically involved with Pechaluk.

19 The appellant, who was a manager of a Loblaws store, met Pechaluk in early 2005 through a mutual friend. Pechaluk, who was 21 years old, worked at a different Loblaws store. The appellant and Pechaluk became friends. Pechaluk met Hoy and knew he was the appellant's boyfriend. The three went out together from time to time.

20 By September 2005, the relationship between the appellant and Pechaluk had changed and become an intimate one. In the following months, Pechaluk became devoted to the appellant. They spent a great deal of time together and exchanged numerous texts and notes expressing their strong feelings for each other.

21 In late 2005, the relationship between the appellant and Hoy had deteriorated, in part because Hoy was seeing other women. The appellant began to tell Pechaluk that Hoy was physically and emotionally abusive. She also indicated that Hoy would at times forbid the appellant from spending time with Pechaluk.

22 In the following months, the appellant repeatedly told Pechaluk that she was afraid of Hoy who, according to the appellant, was a gang member, had killed people in the past, and was involved in serious criminal activity. The appellant reiterated complaints about Hoy's longstanding physical and emotional abuse of her.

23 Hoy was a large man and had been a bouncer. There was no evidence that he was in fact a gang member or had been involved in serious criminal activity. There was some evidence that he had told people that he had gang affiliations. It is not clear whether the stories the appellant told Pechaluk came from Hoy or were made up by the appellant. In either case, it was the Crown's position that the appellant told these stories to Pechaluk, in part at least, to motivate her to kill Hoy.

24 By June 2006, Pechaluk wanted to marry the appellant. She believed that Hoy was dangerous and that his ongoing relationship with the appellant presented a real danger to the appellant. Pechaluk hoped that Hoy would lose interest in the appellant in favour of one of the other women that he was seeing at the time.

25 In June 2006, the appellant went with Hoy on a holiday to Las Vegas. She repeatedly texted Pechaluk telling her that Hoy was mistreating her and she was having a terrible time. Photographs of the appellant and Hoy taken during the Las Vegas trip suggested that the appellant was, in reality, having a good time on her vacation with Hoy.

26 The appellant had given Pechaluk a journal to keep while she was in Las Vegas. Pechaluk's journal entries, made at the encouragement of the appellant, demonstrate that Pechaluk firmly believed that Hoy was abusing the appellant and had to be stopped. Pechaluk even contemplated driving to Las Vegas to stop the mistreatment of the appellant.

27 In September 2006, Pechaluk moved into an empty bedroom in the appellant's apartment. She went to great lengths to avoid any contact with Hoy when he would visit the apartment. The appellant told Pechaluk that it would be very difficult to continue their relationship as long as Hoy was "in my life".

28 The appellant talked to Pechaluk about "getting rid of" Hoy. After Pechaluk moved into the apartment, the discussions became more frequent and more detailed. Initially, the appellant suggested poisoning Hoy. Later, she suggested killing Hoy and claiming self-defence. In the initial version put forward by the appellant, she would be the one to actually kill Hoy.

29 In October 2006, someone slashed tires on two of Hoy's automobiles. He was concerned about his safety and decided to stay at the appellant's apartment. Pechaluk stayed in her bedroom to avoid Hoy.

30 Pechaluk did not want Hoy staying at the apartment. The appellant professed to want Hoy out of the apartment as well. The appellant spoke to Pechaluk about different ways of killing Hoy, including beating him to death with a baseball bat and claiming that an intruder had come into the apartment while the appellant was in the shower. The appellant told Pechaluk that because of her Catholic beliefs, she could not actually kill Hoy and that Pechaluk would have to inflict the fatal blows. The appellant explained to Pechaluk that the "intruder" story would be made more credible by Hoy's criminal associations and the recent incidents involving the slashing of the tires on his cars. The appellant made it clear to Pechaluk that she wanted Hoy killed in the very near future. On October 21, some six days before the murder, the appellant told Pechaluk that she wanted Hoy killed in her bed.

31 Over the next few days, the appellant spoke to Pechaluk about killing Hoy several times. She added details to the story about the intruder. The appellant again told Pechaluk that Pechaluk would have to wield the baseball bat, explaining that Pechaluk should commit the murder because she was stronger than the appellant.

32 Pechaluk testified that when the appellant brought up the various plans to kill Hoy, she did not say anything to discourage the appellant because she did not want to lose the appellant's affection.

33 Pechaluk testified that the longer Hoy stayed in the apartment, the more the appellant talked about killing him. On October 23, four days before the homicide, she indicated to Pechaluk that she wanted to kill Hoy that night while he was asleep. That same day, she sent a text message to Pechaluk describing Hoy as a "jackass" and telling Pechaluk "I want to be with you so much but my hands are tied".

34 The appellant and Pechaluk exchanged further emails on October 24, including one in the early morning of October 25, in which the appellant asked:

> Why aren't you sleeping? You are going to need your rest for tomorrow.

35 In the late afternoon of October 26, Pechaluk picked up the appellant at work. When they arrived at the apartment, Pechaluk went straight to her room to avoid any contact with Hoy who was still staying with the appellant. At one point during the evening, the appellant knocked on Pechaluk's door and asked her if she was "ready". Pechaluk responded that she could not kill Hoy. The appellant said nothing and walked away from Pechaluk's bedroom.

36 Later that evening, Pechaluk awoke to the sound of the appellant banging at her bedroom door. The appellant told Pechaluk that she thought Hoy was dead. Pechaluk and the appellant ran to the bedroom of Kilpatrick Knowles who also lived in the apartment and told him that they believed there was an intruder in the house. The appellant called 911 and told the "intruder" story. She did not ask for an ambulance or for any medical help for Hoy.

37 The police arrived at the apartment shortly after the 911 call. A police officer, using very general language, asked the appellant what had happened in the apartment. The appellant launched into a detailed monologue that included reference to Hoy's extensive criminal connections, the slashing of his tires, and the appellant's taking of a shower with the radio on at the time the attack apparently occurred. These details were among those mentioned by the appellant when she was discussing her plan to kill Hoy with Pechaluk in the days before the homicide.

B. The Evidence of Sarah Sousa and Keisha Brooks

38 Sarah Sousa and Keisha Brooks worked at the same Loblaws store as Pechaluk. All three were good friends.

39 Ms. Sousa knew from Pechaluk that she and the appellant were involved in a relationship. During the summer and early fall of 2006, Pechaluk spoke to Sousa about Hoy's abusive conduct toward the appellant. Pechaluk was angry and frustrated. She believed Hoy was interfering with her relationship with the appellant.

40 Over time, Sousa's discussions with Pechaluk turned from frustration and anger with Hoy to ways that Pechaluk might "get rid" of Hoy. Pechaluk spoke of the possibility of poisoning Hoy and asked Sousa about drugs that might induce a heart attack. Pechaluk also spoke of the possibility of killing Hoy and making it appear as though the appellant had acted in self-defence.

41 Sousa said that in these conversations Pechaluk was asking her "how do I get rid of Dennis [Hoy]?" Sousa mainly listened to Pechaluk's statements about killing Hoy, although she did ask some questions. In Sousa's mind, Pechaluk was trying to work out various possible scenarios for Hoy's murder. Sousa testified that when Pechaluk talked about potential plans to murder Hoy, she would use the pronoun "we".

42 On October 20, 2006, a week before the murder, Pechaluk spoke with Sousa outside of the Loblaws store. She told Sousa they were "doing it the next day". Pechaluk mentioned that Hoy's tires had been slashed so that now was the perfect time to kill him. The plan was to attack Hoy while he slept in the appellant's bed and beat him to death with a baseball bat. Pechaluk was an accomplished baseball player. After the beating, the appellant would phone 911 and tell the authorities that someone had broken into the apartment and murdered her boyfriend while she was taking a shower. The appellant would also tell the police about Hoy's prior abuse of her and his many connections to criminal activities and criminal gangs. According to Sousa, Pechaluk was calm during this conversation.

43 Sousa testified that she asked Pechaluk various questions about the plan to murder Hoy. For example, she asked how they would deal with the presence of Mr. Knowles at the apartment. Pechaluk had answers for the questions Sousa posed.

44 In her testimony, Pechaluk acknowledged speaking to Sousa about plans to kill Hoy. She testified, however, that she never described it as her plan and never indicated that she would kill Hoy. Pechaluk testified that she told Sousa that the appellant wanted her to beat Hoy to death with a bat, but that she had not agreed to do so.

45 Keisha Brooks testified that Pechaluk spoke to her about Hoy's verbal and physical abuse of the appellant. She told Brooks that Hoy was a dangerous person with criminal connections. According to Brooks, Pechaluk spoke about murdering Hoy in late 2005. Brooks told Pechaluk that she should not get herself involved in the relationship between the appellant and Hoy.

46 Brooks testified that in early 2006, Pechaluk spoke about poisoning Hoy. Brooks did not take these statements seriously.

47 On October 25, 2006, Pechaluk told Brooks that she and the appellant had decided to get rid of Hoy before the end of the weekend. Brooks, once again, told Pechaluk that she should let the appellant deal with Hoy on her own. Pechaluk insisted that the appellant was not strong enough to get rid of Hoy. According to Brooks, Pechaluk was very upset during the conversation on October 25. When Brooks told Pechaluk she did not want to hear about any plans to murder Hoy and that it was wrong, Pechaluk replied that Brooks did not understand the situation.

48 Brooks testified that she was devastated when she learned of Hoy's death on October 28. She had not reported her discussions with Pechaluk to anybody because she did not think Pechaluk would go through with it.

49 In her evidence, Pechaluk admitted to speaking to Brooks about poisoning Hoy. She also admitted to speaking to Brooks on October 25, 2006. She denied, however, that she said that she and the appellant were going to kill Hoy before the weekend was over. According to Pechaluk, she told Brooks that the appellant wanted the murder done within a couple of days. Pechaluk denied that she ever told Brooks that she would kill Hoy.

C. The Other Evidence

50 The Crown led physical evidence to demonstrate that the "intruder" story was a fabrication and evidence connecting the appellant and Pechaluk to the murder weapon. I need not review that evidence. When the case went to the jury, no one suggested that anyone other than Pechaluk and/or the appellant had murdered Hoy.

51 The appellant was the beneficiary under Hoy's life insurance policy valued at $238,000 and was entitled to survivor benefits under his pension plan. Within four days of Hoy's murder, the appellant contacted his employer to inquire about collecting the survivor benefits. She made certain misrepresentations to the employer in an apparent effort to speed up the process. The appellant received survivor pension benefits in the amount of $20,305.82 in February 2007. No life insurance proceeds were ever paid out to the appellant.

52 There was a great deal of evidence about Hoy's abuse of the appellant. That evidence came from statements made by the appellant to various people, including Pechaluk. There was no other evidence of physical abuse. There was some evidence from Pechaluk and another witness that Hoy did on occasion become quite angry with the appellant.

IV

The Carter Grounds of Appeal

A: The Trial Context

53 The Crown alleged that Hoy was killed in furtherance of a plan devised and promoted by the appellant whereby the appellant persuaded Pechaluk to come into her bedroom and bludgeon Hoy while he was asleep. The Crown argued that the plan included the "intruder" story devised to mislead the police.

54 The defence agreed that there was a plan to kill Hoy and that it included the "intruder" story. However, the defence argued that the plan was formulated by and involved only Pechaluk.

55 By the end of the evidence, the parties agreed that Hoy's homicide was a first degree murder. There were three possibilities. Hoy was murdered by Pechaluk acting alone (the defence position), the appellant acting alone (Pechaluk's testimony), or by Pechaluk and the appellant acting pursuant to a plan to kill Hoy (the Crown's position). The jury was left with only two possible verdicts - either guilty of first degree murder or not guilty.

56 On the Crown's theory, the Crown had to prove beyond a reasonable doubt that the appellant had planned Hoy's murder with Pechaluk and that the murder was perpetrated by Pechaluk in furtherance of that plan. If the Crown proved both beyond a reasonable doubt, it followed as a matter of law that the appellant was a party to the first degree murder committed by Pechaluk.

57 Because the Crown alleged that the appellant was party to the murder by virtue of her agreement with Pechaluk to murder Hoy, the trial judge was required to instruct the jury both as to the existence of the agreement as a basis upon which the appellant could be found to be a party (aider, abetter or counsellor) to the murder and on the evidentiary rule commonly referred to as the coconspirator exception to the hearsay rule. That rule potentially made certain acts and declarations of Pechaluk admissible against the appellant to prove that the appellant was a participant in the plan to murder Hoy.

58 The trial judge instructed the jury on the concepts of aiding, abetting and counselling at some length. She expressly told the jury that participation in the formulation and execution of the plan could constitute aiding:

> However, if you find that she was participating in the plan, certainly the act of participating in the plan and planning can be considered helping.

59 The trial judge did not expressly instruct the jury that the appellant's participation in the planning and execution of the plan to kill Hoy would constitute abetting and/or counselling. The tenor of her instructions, however, conveyed that message. I do not understand counsel to suggest that the jury would not understand that on the Crown's theory the appellant's liability as an aider, abettor or counsellor depended upon the Crown proving beyond a reasonable doubt that the appellant and Pechaluk had agreed to murder Hoy and that he was murdered in furtherance of that plan.

60 The trial judge also instructed the jury on the co-conspirator exception to the hearsay rule using the three-step process set out in *R. v. Carter*, [1982] 1 S.C.R. 938 (S.C.C.). That process as applied to this case proceeds as follows:

Step One:

- The jury must be satisfied beyond a reasonable doubt based on all of the evidence that the alleged plan to murder to Hoy existed.

Step Two:

- If the jury was satisfied that the alleged plan existed, it must review all of the evidence directly admissible against the appellant and decide whether she was probably a participant in the plan to murder Hoy.

Step Three:

- If the jury concluded at step two that the appellant probably participated in the plan, the jury must then decide whether the Crown had proved her participation beyond a reasonable doubt. In making that determination, the jury could use evidence of the acts and declarations of Pechaluk done during and in furtherance of the plan as long as the jury was satisfied on evidence directly admissible against Pechaluk that she was a probable participant in the plan.

B: Should Bogiatzis be Overruled?

(i) The argument

61 Counsel for the appellant submits that this court was wrong in *Bogiatzis* in holding that it was bound by the *obiter dicta* in *Barrow* to the effect that the Carter instruction applied to a two-person conspiracy. Counsel submits that *Barrow* did not actually hold that the *Carter* instruction applied to a two-person conspiracy and that, even if it did, that comment was not the kind of *obiter* that should be taken as binding on this court: see *R. v. Henry*, 2005 SCC 76, 3 S.C.R. 609 (S.C.C.) at para. 57. Counsel submits that nothing in *Barrow* compels this court to use the *Carter* instruction in cases where the conspiracy alleged involves only two persons.

62 Counsel next submits that the *Carter* instruction inevitably confuses the jury and prejudices an accused if the allegation involves a two-person conspiracy. Counsel contends that in cases involving a two-person conspiracy, a finding at stage one that the agreement alleged exists must inevitably lead to a finding at stage three that the accused was a member of that conspiracy. The finding of membership inevitably follows a finding of the existence of the agreement because the agreement cannot exist without at least two members. Counsel argues that whatever the jury may be told, the logical connection between a finding of the existence of the agreement and a finding of an accused's membership in the agreement is so strong where the allegation involves a two-person conspiracy that a jury will inevitably move directly from a finding of the agreement to a finding of membership. Counsel points out that the initial finding of the existence of the agreement may well be based on acts and declarations of others that are not properly admitted against an accused to prove his or her membership in the conspiracy.

63 Counsel relies on the judgment of Tyndale J.A., writing for himself, in *R. c. Comeau* (1991), [1992] R.J.Q. 339 (Que. C.A.), at 348, aff'd without reference to this point, [1992] 3 S.C.R. 473 (S.C.C.).[2] Tyndale J.A. held that the comments in *Barrow* about two-person conspiracies were not binding. In his view, the *Carter* instruction was confusing and prejudicial in cases involving two-person conspiracies. Tyndale J.A. opined that the jury should not be instructed on the co-conspirator exception to the hearsay rule if the Crown alleged a conspiracy involving only two persons, but should determine guilt strictly on the evidence directly admissible against an accused.

64 Counsel for the appellant also relies on observations in *Bogiatzis* at para. 24:

> The problem arises because the essence of a conspiracy is an agreement. If the jury has found an agreement and there are only two people involved, it follows that both must be guilty, otherwise there could be no agreement. I admit that the application of the *Carter* formula in a two-person conspiracy is challenging...

(ii) Stare decisis

65 The submission that this court should overrule *Bogiatzis* engages two different components of the *stare decisis* doctrine. First, the court is asked to hold that certain *obiter* in a decision of the Supreme Court of Canada is not binding. Second, the court is asked to depart from its own prior holding wherein it declared that the *obiter* was binding. The first part of the submission addresses the extent to which this court is bound by *obiter dicta* from the Supreme Court of Canada (vertical precedent). The second addresses this court's approach to overruling its own prior decisions (horizontal precedent): see *McNaughton Automotive Ltd. v. Co-operators General Insurance Co.* (2005), 76 O.R. (3d) 161 (Ont. C.A.), leave to appeal refused, [*Woods Estate v. ING Halifax Insurance Co.*] (2006), [2005] S.C.C.A. No. 388 (S.C.C.); Debra L. Parkes, "Precedent Unbound? Contemporary Approaches to Precedent in Canada" (2007) 32 Man. L.J. 135.

66 I think it best to begin with the first aspect of the *stare decisis* doctrine engaged by this submission. If *Bogiatzis* correctly reads the *obiter* in *Barrow* as binding, there is obviously no need to consider whether this court should overrule *Bogiatzis*.

67 *R. v. Henry* instructs that some *obiter* from the Supreme Court of Canada must be regarded as authoritative and other *obiter* will be persuasive only:

> All *obiter* do not have, and are not intended to have, the same weight. The weight decreases as one moves from the dispositive *ratio decidendi* to a wider circle of analysis which is obviously intended for guidance and which should be accepted as authoritative. Beyond that, there will be commentary, examples or exposition that are intended to be helpful and may be found to be persuasive, but are certainly not "binding"...

68 In *R. v. Prokofiew*, 2010 ONCA 423, 100 O.R. (3d) 401 (Ont. C.A.), aff'd without reference to this point, [2012] S.C.J. No. 49 (S.C.C.), this court, relying on *Henry*, distinguished between *obiter* that was integral to the analysis underlying the *ratio decidendi* of the judgment and *obiter* that was incidental or collateral to that analysis. The former kind of *obiter*,

but not the latter, is binding on this court. In characterizing *obiter* from the Supreme Court of Canada, lower courts should begin from the premise that the *obiter* was binding.

(iii) What does Barrow decide?

69 The Crown alleged a three-person conspiracy in *Barrow*. The appellant, Barrow, and one of the other alleged conspirators were tried together. The third alleged conspirator had pleaded guilty before trial. The trial judge instructed the jury in accordance with *Carter*. He told the jury that it must first be satisfied on all of the evidence and beyond a reasonable doubt that the conspiracy alleged existed. He next told the jury that if satisfied of the existence of the conspiracy, it could move to steps two and three of the *Carter* instruction to determine whether either or both of the accused were members of the conspiracy.

70 The appellant in *Barrow* argued that because a conspiracy required at least two members, if the Crown alleged a three-person conspiracy, the jury could only be satisfied of the existence of the conspiracy at step one of the *Carter* direction if the jury was satisfied that at least one of the two accused was a member of the conspiracy. Counsel argued that this finding could well be made on evidence that was not properly admissible against an accused to show his membership in the conspiracy. [3]

71 In support of the argument that the *Carter* instruction prejudiced the appellant, counsel for Barrow argued that the *Carter* instruction would clearly be prejudicial if the Crown alleged a two-person conspiracy because a finding of a conspiracy at step one would constitute a finding of membership in the conspiracy as against both alleged conspirators.

72 McIntyre J., speaking for the court on this issue, [4] rejected the appellant's submissions. He observed that the *Carter* instruction was intended to and did distinguish between the existence of the conspiracy - the subject matter of step one of the inquiry - and individual membership in the conspiracy - the subject matter of steps two and three of the inquiry. An affirmative finding at step one did not establish individual membership in the conspiracy under steps two and three: *Barrow*, paras. 74-75.

73 McIntyre J. also dealt with the two-person conspiracy argument. He observed that the case law established that where the Crown alleged a twoperson conspiracy, the jury could convict one accused and acquit the other. The possibility of the acquittal of one accused and the conviction of the other could only be explained on the basis that it was open to the jury to find that while the Crown had proved the existence of the two-person conspiracy beyond a reasonable doubt, it had not, on evidence properly admissible against one accused, proved that accused's membership in the conspiracy beyond a reasonable doubt.

74 McIntyre J., at para. 77, rejected the contention that the different verdicts in a case involving an alleged two-person conspiracy would demonstrate illogicality or inconsistency.

> In my view, there is no inconsistency in this position. The apparently inconsistent verdict does not result from the impossible conclusion that A conspired with B to commit a given crime and that B did not conspire with A on the same occasion to commit the same crime, but rather from the fact that there was evidence admissible against A to establish his guilt, but not sufficient evidence admissible against B to prove his participation.
>
> The fact that upon arrest Mr. A says to the police "yes, B and I agreed to murder X" will not be admissible against B, but does not deprive it of its evidentiary force against A.

75 I think the rejection of the two-person conspiracy argument in *Barrow* was central to the court's analysis of the claim that the *Carter* instruction had prejudiced the appellant in *Barrow*. The appellant argued that the *Carter* instruction had prejudiced him because of the substantial risk that the jury would conflate step one in the *Carter* instruction with steps two and three and conclude that proof of the conspiracy constituted proof of the appellant's membership in the conspiracy. That argument had its plainest and most powerful application in a case involving an alleged two-person

conspiracy. The appellant could only hope to convince the court that the *Carter* instruction had prejudiced his case if he could first demonstrate the inherent prejudice in the *Carter* instruction as applied to a two-person conspiracy.

76 I must, with respect, disagree with the observation of Tyndale J.A. in *Comeau*, at 348, that the two-person conspiracy argument was not "squarely raised, debated or decided" in *Barrow*. To the contrary, McIntyre J., at para. 76 in *Barrow*, described the two-person conspiracy argument as the "root of the argument advanced on this issue".

77 *Bogiatzis*, at para. 24, recognized that the references to the applicability of the *Carter* instruction to a two-person conspiracy were *obiter* in *Barrow*. The court did not attempt to characterize that *obiter*, but simply indicated that it was bound by it. I take from that conclusion that the court in *Bogiatzis* was satisfied that the two-person conspiracy analysis in *Barrow* was integral to the analysis leading to the rejection of the submission that the *Carter* instruction should not have been given in *Barrow*.

78 Not only am I satisfied from a reading of *Barrow* that the observations relating to a two-person conspiracy were integral to the analysis, I also see no other basis upon which to question the *obiter* in *Barrow*. Unlike *Prokofiew*, there is no Supreme Court of Canada authority, prior or subsequent to *Barrow*, that contradicts or even casts any doubt upon the correctness of the *obiter* in *Barrow*.

79 On appeal, no one argued that the brief reasons of the Supreme Court of Canada in *Comeau*, affirming the decision of the Quebec Court of Appeal, supported the view of Tyndale J.A. that *Carter* had no application to a two-person conspiracy. Cory J., speaking for a unanimous court, simply acknowledged errors in the instructions "regarding evidence of conspiracy" and explained why the curative *proviso* applied. He made no reference to *Barrow*, *Carter*, or the reasons of Tyndale J.A. [5]

80 Lastly, I find nothing in the other provincial appellate authorities counsel referred to in support of the argument that the *obiter* in *Barrow* is not binding. Those cases recognize that the *Carter* instruction can present difficulties if a twoperson conspiracy is alleged. They also recognize that some modification of the *Carter* instruction or some added instruction might be appropriate. None suggests that the *Carter* instruction should not be given: see e.g. *Buckingham v. Newfoundland (Provincial Court Judge)* (1998), 162 Nfld. & P.E.I.R. 211 (Nfld. C.A.), at paras. 21-24; *R. v. Viandante* (1995), 102 Man. R. (2d) 126 (Man. C.A.), leave to appeal refused, [1996] S.C.C.A. No. 243 (S.C.C.), at paras. 42-53.

81 For the reasons set out above, I agree with the holding in *Bogiatzis*. The *obiter* in *Barrow* is binding on this court.

(iv) The Carter instruction and two-person conspiracies

82 As I am satisfied that *Bogiatzis* correctly bowed to the *obiter* in *Barrow*, it is unnecessary to address the merits of the argument that the *Carter* instruction cannot be fairly applied to an allegation of a two-person conspiracy. However, given the thorough submissions received from the parties and the interveners, I will, for the sake of completeness, address the merits of that argument.

83 In my view, the *Carter* instruction can properly be given where the Crown alleges a two-person conspiracy. Before explaining my reasons for coming to that conclusion, I want to make one point crystal clear. The *Carter* instruction, like all jury instructions, is intended to give to the jury information the jury needs to properly decide the case. The functional approach to the content of all jury instructions dictates that those instructions, including the *Carter* instruction, must be modified and tailored to meet the needs of the specific case. Consequently, when I say the *Carter* instruction has application to a two-person conspiracy, I do not mean to suggest that the instruction cannot be modified or even bypassed as the circumstances of the particular case demand: see *R. v. Viandante* at para. 51. [6]

84 I have three reasons for concluding that the *Carter* instruction applies to two-person conspiracies:

- The rationale underlying the *Carter* instruction applies as much to twoperson conspiracies as to conspiracies involving multiple persons.

- The logical difficulties inherent in the *Carter* instruction as applied to a twoperson conspiracy, while undeniable, can be overcome by an appropriately tailored instruction.

- No viable alternative to a *Carter* instruction has been offered.

(a) The rationale for the instruction

85 Allegations of conspiracy and substantive offences committed in pursuit of a common design present a unique evidentiary problem. Generally, a declaration is admissible only against its maker and an act is admissible only against the doer of that act. However, evidence of acts and declarations made during the course of a conspiracy and in furtherance of the object of that conspiracy are receivable against other conspirators to prove their membership in the conspiracy. The evidentiary rule, however, is predicated on proof of the existence of the agreement. That agreement is the crime itself, if conspiracy is charged, and the basis upon which the Crown alleges that an individual is a party to the offence if a substantive offence is charged. It seems that either the rule has no value since it applies only if the conspiracy has already been established, or that the rule works unfairly against an accused in that it assumes the existence of the agreement, a fact which the Crown is required to prove beyond a reasonable doubt.

86 The *Carter* instruction is a uniquely Canadian response to the conundrum posed by the application of the co-conspirator exception to the hearsay rule. [7] The direction seeks to provide the jury with reliable evidence relevant to an accused's membership in the agreement in the form of the acts and declarations in furtherance of the conspiracy by other conspirators, while ensuring that the jury is satisfied that two preconditions to that reliability, the existence of the agreement, and the accused's probable membership in the agreement, have been established on evidence properly admissible for those purposes.

87 In *R. v. Mapara*, 2005 SCC 23, [2005] 1 S.C.R. 358 (S.C.C.), the court considered a challenge to the continued viability of the co-conspirator exception to the hearsay rule under the modern principled approach to the admission of hearsay evidence first enunciated in *R. v. Khan*, [1990] 2 S.C.R. 531 (S.C.C.) and further developed in *R. v. Starr*, 2000 SCC 40, [2000] 2 S.C.R. 144 (S.C.C.). The court concluded that the coconspirator exception did survive scrutiny. In so holding, the court relied on the three-step *Carter* instruction as an effective means of establishing sufficient circumstantial indicators of the reliability of the proffered hearsay evidence. The court also held that the rule, as constrained by the *Carter* instruction, did not operate unfairly against an accused and that its operation promoted the effective administration of criminal justice: *Mapara*, paras. 28-29. *Mapara* clearly viewed the *Carter* instruction as essential to the continued viability of the co-conspirator exception to the rule against hearsay.

88 I see no connection between the number of members of a conspiracy and the rationale for the three-step approach to the co-conspirator exception to the hearsay rule. The justification for that rule and the reliability enhancing function played by the three-step approach designed in *Carter* are as germane to a twoperson conspiracy as they are to a multi-person conspiracy.

89 Tyndale J.A., in *Comeau* at 348-49, would eliminate both the need for a separate inquiry into the existence of the alleged agreement and the operation of the co-conspirator exception to the hearsay rule if the Crown alleged a two-person conspiracy. With respect to Tyndale J.A., there is no justification for excluding what is otherwise reliable hearsay evidence in the form of a co-conspirator's acts and declarations simply because the criminal agreement involved only two members. As the Chief Justice observed in *Mapara*, at para. 29, when referring to the co-conspirator exception as articulated in *Carter*:

> The rule allows the Crown to effectively prosecute criminal conspiracies. It would become difficult and in many cases impossible to marshal the evidence of criminal conspiracy without the ability to use coconspirator statements of what was said in furtherance of the conspiracy against each other. To deprive the Crown of the right to use double

hearsay evidence of co-conspirators as to what they variously said in furtherance of the conspiracy would mean that serious criminal conspiracies would often go unpunished.

90 The "serious criminal conspiracies" alluded to by the Chief Justice may involve only two persons. I cannot support an approach which would exclude potentially valuable evidence from a jury's consideration in those cases.

(b) An appropriate jury instruction can be given

91 Many courts, including this one in *Bogiatzis*, at para. 29, have commented on the difficulty, in the context of a two-person conspiracy, of explaining to a jury the distinction between the finding at step one that the conspiracy existed and the finding after step three that an accused was a member of the conspiracy: see e.g. *Ahern v. R* 80 A.L.R. 161 (H.C.). Those problems are real but not insurmountable: see *R. v. Duff* (1994), 95 Man. R. (2d) 167 (Man. C.A.) at paras. 48-54.

92 Unfortunately, some rules governing criminal trials are of necessity complicated. Others are counterintuitive and inconsistent with how a reasonable person might approach the same problem if left unguided by judicial instruction. The limitations surrounding the use that can be made of evidence of an accused's bad character is perhaps a good example of a rule that requires delicate instruction because it runs contrary to what many would see as common sense and logic.

93 Our system of trial by jury, however, presumes that juries can and do understand and apply instructions given to them by trial judges: see *R. v. Emms*, 2010 ONCA 817, 104 O.R. (3d) 201 (Ont. C.A.), aff'd, [2012] S.C.J. No. 74 (S.C.C.), at paras. 26-27. If those instructions can be plainly put, I do not think that one should assume that a jury cannot follow them simply because they may seem illogical to the jury.

94 A proper instruction in a case involving a two-person conspiracy would not only make the three steps of the *Carter* instruction clear to the jury, but would also caution against following the incorrect path directly from stage one to a conviction. I have set out in Appendix A to these reasons a draft instruction that contains a caution against resort to the logical, but improper assumption that proof of the existence of the agreement at stage one can constitute proof of participation in that agreement as against the individual accused. No doubt, other acceptable formulations of that caution could also be articulated.

(c) Alternative approaches

95 The intervener, the Criminal Lawyers' Association (Ontario), in its helpful submissions, suggests essentially three alternatives to the *Carter* instruction.

96 Counsel submits that step one of the *Carter* instruction could be left to the trial judge. This possibility was vetted in *Bogiatzis* and is also advanced by counsel for the appellant. On this approach, the trial judge would decide, on some standard of proof, whether the Crown had established that the alleged agreement existed. If the judge was so satisfied, the jury would then be instructed to determine whether the Crown had proved that the accused was a member of the conspiracy by the application of steps two and three of the *Carter* instruction. This is the American approach: e.g. see *Bourjaily v. United States*, 483 U.S. 171 (U.S. Ohio S.C. 1987).

97 I have two problems with this approach. First, it removes from the jury's consideration a fundamental factual question - the existence of the alleged agreement. While it may be that in many cases membership in the conspiracy and not the existence of the conspiracy will be the focus of the trial, there are cases where the existence of the agreement is very much in issue. It is, in my view, unacceptable in a case of trial by jury that the jury not decide what may be the factual focal point of the trial.

98 The approach is also contrary to the binding authority in *Mapara*. In *Mapara*, the appellant argued that both steps one and two of the *Carter* instruction should be left to the trial judge to avoid potential unfairness and prejudice to an accused. In rejecting this submission, Chief Justice McLachlin said, at para. 32:

> While courts may adjust common law rules incrementally to avoid apparent injustice, they do so only where there is clear indication of a need to change the rule in the interests of justice. That is not established in this case. Indeed, the appellant's suggestion was considered and rejected in *Carter* precisely because of the danger that the jury might confuse the direct and hearsay evidence against the accused and rely on the latter to convict the accused. The court concluded that the three-stage approach was better suited to bring home to the jury the need to find independent evidence of the accused's participation in conspiracy. I would not accede to this request.

99 The Chief Justice's words apply equally to two-person conspiracies. Regardless of the number of alleged conspirators, the instruction must "bring home to the jury the need to find independent evidence of the accused's participation in conspiracy". The *Carter* instruction does that by distinguishing between the agreement and membership, directing the jury to look only at evidence directly admissible against an accused in determining probable membership in the agreement, and by the "in furtherance" limitation on the use of acts and declarations of the co-conspirator.

100 Although I do not accept the submission of the Criminal Lawyers' Association (Ontario) that the finding required by step one of the *Carter* instruction should be left to the trial judge, I do accept the related submission that in some cases it will be unnecessary to give any separate instruction as to the existence of the agreement. If having regard to the evidence and the position of the parties it is clear that the agreement existed, the trial judge may be able to so instruct the jury and move directly to steps two and three of the *Carter* direction. I do not see that, however, as a rejection of the *Carter* instruction as applied to two-person conspiracies, but rather as an example of the modification of that instruction to suit the needs of a specific case.

101 I can deal briefly with the other two alternatives put forward by the Criminal Lawyers' Association (Ontario). Counsel suggests that the determination of the existence of the conspiracy at step one in the *Carter* direction could be moved to the end of the instruction, meaning that the jury would first determine the question of membership in the agreement. I do not think this approach would make anything clearer. If anything, the jury would be confounded by an instruction that first told them to look for membership in the conspiracy and, second, told them to look for the existence of the conspiracy.

102 The third alternative put forward by the Criminal Lawyers' Association (Ontario) would eliminate any instructions along the lines of step one in the *Carter* direction. From the jury's perspective, this is no different than the suggestion that the trial judge determine the question posed at step one of the *Carter* direction. I have already considered and rejected that possibility. I would observe, however, that this alternative removes the safeguard of at least having the trial judge determine whether there is adequate evidence of the existence of the agreement.

103 In summary, I do not pretend that the jury instruction in cases involving allegations of conspiracy or common design is an easy one, particularly if the allegation involves only two persons. However, the rationale driving the formulation of the three-step approach in *Carter* applies equally to a two-person conspiracy. The jury must understand that the existence of the agreement and membership in the agreement are discrete issues and the jury must understand how to approach the evidence in respect of both issues, particularly the issue of individual membership in the conspiracy. The *Carter* direction accomplishes both ends. None of the alternative suggestions do this as well, much less better. The instruction appropriately tailored to the case and accompanied with a clear caution against assuming membership based on the existence of the agreement will, in my view, avoid prejudice to the accused.

C. The Alleged Errors in the Carter Instruction

104 Counsel for the appellant made several submissions in his factum challenging various aspects of the trial judge's *Carter* instruction. He did not pursue all of those arguments in his oral submissions. I would not give effect to any of the arguments and will address what I regard as the principal submissions advanced on behalf of the appellant. Those submissions relate to step one and step three of the *Carter* instruction and the adequacy of the caution given by the

trial judge in the face of the particular potential for prejudice posed by the *Carter* instruction in cases involving two-person conspiracies.

(i) Step One

105 The trial judge, applying *Carter*, explained to the jury that in determining the evidence that could potentially be used against the appellant to prove her membership in the plan to murder Hoy, the jury must first determine whether there was in fact a plan to murder Hoy. The trial judge outlined for the jury the evidence it could consider at this first step.

106 The appellant alleges two errors. He submits that the jury should not have been told that Pechaluk's testimony constituted evidence of the plan to murder Hoy because Pechaluk denied being a party to that plan. The appellant further submits that the trial judge erred in instructing the jury that the evidence of Sousa and Brooks about statements made to them by Pechaluk concerning the plan to kill Hoy could be considered at the first stage of the *Carter* instruction.

107 The first submission must be rejected. Pechaluk described in detail the evolution of the plan to murder Hoy and her conversations with the appellant about that plan. Her evidence concerning these conversations presents no hearsay issues, is clearly logically relevant to the existence of the alleged plan and is, therefore, admissible. I would add that Pechaluk's evidence about the appellant's actions and statements relating to the plan were also admissible to show the appellant's involvement in the plan at step two of the *Carter* instruction: see *R. v. Yumnu*, 2010 ONCA 637, 260 C.C.C. (3d) 421 (Ont. C.A.) at para. 342.

108 Pechaluk's testimony that the plan was exclusively the appellant's and that she did not join the plan was irrelevant to the admissibility of her testimony on the issue of whether the plan existed. In any event, the jury was free to reject that part of Pechaluk's evidence. There was ample other evidence from which the jury could conclude that Pechaluk was a participant in the plan. The trial judge properly left Pechaluk's testimony describing the plan as evidence from which the jury could infer the existence of the plan.

109 The second submission challenging the instruction at step one of the *Carter* direction raises a more complicated question. The answer to that question begins by determining what the trial judge said to the jury. Crown counsel persuasively submits that the trial judge did not instruct the jury that the evidence of Sousa and Brooks as to what Pechaluk said to them about the plan was admissible at step one of the *Carter* instruction. The Crown submits that the trial judge told the jury that Pechaluk's own testimony of what she said to Sousa and Brooks was admissible at step one. The Crown contends that it cannot be disputed that Pechaluk's own evidence about what she said to Sousa and Brooks about the plan to murder Hoy was admissible at step one of the *Carter* instruction.

110 The charge to the jury is not entirely clear on this point. However, considering the charge as a whole, I agree with the appellant's submission that the trial judge told the jury that the evidence of Sousa and Brooks about statements made to them by Pechaluk concerning the plan could be considered when determining whether the plan existed. The instruction is perhaps most clearly put in the passage in which the trial judge is explaining the various uses of the testimony of Sousa and Brooks. Included in those potential uses was the following:

> It [the evidence of Sousa and Brooks] may help you consider whether there was a plan to murder Dennis and mislead the police, and whether Ashleigh [Pechaluk] was part of that plan.

111 In *Carter*, at p. 947, the court, in describing step one of the *Carter* instruction, indicated that the jury must consider "all of the evidence" when deciding whether the Crown had proved the existence of the alleged agreement beyond a reasonable doubt: see also *Bogiatzis* at paras. 19, 57. "All of the evidence" must refer to evidence properly admissible under the rules of evidence. Those rules begin with the primary command of relevance. Evidence that as a matter of logic and human experience makes the existence of the conspiracy more likely is relevant to prove the existence of the conspiracy unless excluded by some specific rule.

112 Evidence offered to prove the existence of the alleged agreement will not often engage the hearsay rule. Generally, at the step one inquiry, testimony of things said and done by alleged conspirators is tendered not for its truth, but as circumstantial evidence of the existence of the agreement. The admissibility of the evidence depends on whether as a matter of logic and human experience an inference of the existence of the agreement is available from the evidence considered in its totality. Admissibility on the question of the existence of the agreement does not depend on whether the evidence consists of acts and declarations in furtherance of the conspiracy: see David Paciocco & Lee Stuesser, *The Law of Evidence*, 6th ed. (Toronto, Irwin Law, 2011), at pp. 156-58; *R. v. Smith*, 2007 NSCA 19, 216 C.C.C. (3d) 490 (N.S. C.A.) at paras. 187-91, paras. 235-38.

113 Evidence that, during the development of the alleged plan to murder Hoy, Pechaluk spoke to friends several times about the plan, discussed the reasons for the need to kill Hoy, the feasibility of the plan, the means that might be used to kill Hoy, and sought input about the plan from at least one of those friends (Sousa), would, as a matter of common sense and human experience, support the inference that a plan existed. That evidence was properly considered at step one of the *Carter* instruction. [8]

114 Before leaving the appellant's submissions directed at step one of the *Carter* direction, I would add that I see no possibility that any inadequacy in the step one instruction could have prejudiced the appellant. The existence of the plan was not a live issue at trial. Participation in the plan by the appellant was the issue. That participation is addressed at steps two and three of the *Carter* direction.

(ii) Step Three

115 The trial judge's instructions at step three, the "in furtherance" instruction, are challenged in one respect. The trial judge told the jury that it was open to them to conclude that Pechaluk's statements to Sousa prior to Hoy's murder about the plan to murder Hoy were made in furtherance of that plan and, therefore, were potentially admissible at stage three of the *Carter* direction to prove the appellant's participation in the plan beyond a reasonable doubt. I do not understand the appellant to take issue with the content of that instruction. Rather, the appellant argues that on a reasonable interpretation, the statements to Sousa could not be seen as being in furtherance of the plan to kill Hoy, but were instead a narrative of Pechaluk's discussions with the appellant.

116 It is ultimately up to the jury to determine whether an act or a statement of a co-conspirator is said or done in furtherance of the alleged conspiracy: *R. v. Mota* (1979), 46 C.C.C. (2d) 273 (Ont. C.A.) at para. 27. The evidence must, however, be reasonably capable of that interpretation before it can be properly left with the jury as potentially an act or declaration in furtherance of the conspiracy.

117 I agree with the Crown's submission that it was open to the jury to view Pechaluk's conversations with Sousa as an attempt by Pechaluk to advance the plan to kill Hoy by using Sousa as a sounding board to test out various possible schemes and obtain feedback. For example, the conversation about drugs that might cause a heart attack could reasonably be understood as Pechaluk seeking information from her friend about the means she could use to kill Hoy. That kind of inquiry clearly seeks to further the plan to murder Hoy.

118 Although the argument that the conversations between Pechaluk and Sousa were in furtherance of the plan to murder Hoy does not seem to be a particularly strong one, there was enough in the evidence to raise a legitimate question for the jury. I doubt, however, that the evidence of what Pechaluk said to Sousa ultimately played any significant role in the jury's determination of whether the appellant was a participant in the plan to murder Hoy. There was, quite frankly, an abundance of evidence on that issue beginning with Pechaluk's testimony about her conversations with the appellant and ending with the appellant's conduct during the 911 call and her immediate and detailed recital of the "intruder" story when first questioned by the police.

(iii) The caution to not conflate step one and step three of the Carter direction

119 The appellant submits that the trial judge should have "put the jury on high alert" that a finding of the existence of the agreement did not establish membership in the agreement. Counsel acknowledges that the trial judge did provide a caution, but argues that it was insufficient.

120 The trial judge, after instructing the jury on step one in the *Carter* direction and indicating she was now moving on to the question of the appellant's participation in the agreement, said to the jury:

> Now, when you get to consider the participation of Nicola Puddicombe, potential participation of Nicola Puddicombe, be careful here. Just because you have found that there was a common unlawful design does not mean automatically that Nicola Puddicombe was a part of it. You must go on to determine if based on her only [own] actions and statements that she was probably a participant in the plan. ...

121 As with any caution, other language may have been used that would perhaps have given added emphasis to the caution. I have suggested alternative language in Appendix A that has the benefit of explaining to the jury how it is that a finding at step one does not determine the finding at step three. I think that explanation adds to the effectiveness of the caution.

122 The question on appeal is, however, the adequacy of the caution and not whether a better caution could have been given. This caution was adequate. It made clear to the jury that proof of the existence of the plan to murder Hoy was different from proof of the appellant's participation in that plan. The jury were cautioned that a finding of the plan did not compel a finding of the appellant's participation in the plan.

V

The Other Grounds of Appeal

A. The Instruction on Post-Offence Conduct

123 In the part of her instructions described as addressing "conduct after the offence", the trial judge left three pieces of evidence with the jury as potentially inculpatory evidence. The appellant submits that none could reasonably bear any inculpatory inference. She also submits that the trial judge failed to give the jury a mandatory "clear, sharp warning" about the dangers of drawing inculpatory inferences from post-offence conduct. I will first examine the inferences available from the three pieces of evidence left with the jury as after the offence conduct. I will then consider the alleged failure to give a proper warning about that evidence.

(i) The post-offence conduct referred to by the trial judge

124 The appellant's speedy, determined and dishonest attempts to secure Hoy's pension benefits within days of his death could, in my view, support the Crown's contention that the appellant had a financial motive to participate in Hoy's murder. To the extent that it fortified the Crown's case on motive, the evidence supported an inculpatory inference.

125 Similarly, the appellant's statements to her former friend Edie Pearce about her feelings toward Hoy could support the Crown's contention that the appellant hated Hoy and wanted him out of her life at the time of his death. Evidence of animus toward the victim supports an inference of involvement in the murder.

126 Finally, the evidence of the appellant's solicitous treatment of Pechaluk's family while Pechaluk was in custody and before the appellant was charged could support the inference that the appellant was trying to preserve Pechaluk's loyalty at a time when Pechaluk had taken full responsibility for the crime in an attempt to protect the appellant. The appellant's treatment of Pechaluk's family offered some support for the Crown's claim that the appellant was anxious that Pechaluk continue to hide the appellant's role in the murder.

127 The inferences relied on by the Crown and summarized above were not the only inferences available on the evidence referred to by the trial judge. They were, however, reasonably available inferences and were, therefore, properly left with the jury.

(ii) The instructions to the jury

128 The trial judge's instructions did sound a cautionary note properly associated with the drawing of inculpatory inferences from post-offence conduct. The trial judge told the jury that it must look at the entirety of the relevant evidence, especially for explanations of post-offence conduct that were inconsistent with guilt. She said:

> You must not use this evidence about what she did or said afterwards in deciding or helping you decide that she committed the offence unless you reject any other explanation for it. Then and only then can you consider this evidence together with all the other evidence in reaching your verdict.

129 The trial judge's caution was appropriate and adequate. I would dismiss this ground of appeal.

B. The Trial Judge's Instruction that the Appellant Was Potentially Liable as the Perpetrator of the Murder

130 The Crown never suggested that the appellant wielded the axe that struck the fatal blows. On the Crown's theory, the appellant was liable as an aider, abetter or counsellor of the murder actually perpetrated by Pechaluk. The appellant submits that given the Crown's position, the trial judge erred in leaving with the jury the possibility that the appellant was guilty of murder as the perpetrator.

131 A trial judge, in determining the bases upon which potential liability should be explained to the jury, will pay careful attention to the position advanced by the Crown. Ultimately, however, it is the evidence that must dictate the bases of potential liability that must be left with the jury. If this jury believed Pechaluk's evidence without qualification, the only reasonable inference would have been that the appellant, acting on her own, murdered Hoy before going to Pechaluk's bedroom on the second occasion that evening. On this view of Pechaluk's evidence, the appellant was the perpetrator of the murder and her liability was not that of an aider, abetter or counsellor.

132 The trial judge properly left this basis of liability with the jury in the following passage from her charge:

> As I have told you, you can believe some, none or all of a witness's testimony. It is therefore possible that you will believe Ashleigh Pechaluk's testimony that Nicky [the appellant] planned the murder and that when Nicky came to her room around 10:30 the night of the murder to see if Ashleigh was ready, and Ashleigh said, "no, I'll never be ready", that Ashleigh went back to her room, smoked a joint and went to sleep only to be woken up about two hours and a bit later by Nicky, because Dennis was now dead.
>
> If you believe this evidence, it is open to you to conclude that Nicky Puddicombe killed Dennis.

C. The Party Liability Instruction

133 The trial judge defined aiding, abetting and counselling for the jury and reviewed the evidence relevant to each mode of criminal participation. In doing so, the trial judge distinguished between conduct that could constitute aiding, abetting or counselling, e.g. formulating and participating in a plan to murder Hoy and mislead the police, and conduct that provided evidence of aiding and abetting, e.g. the appellant's conversation with the 911 operator and her statement to the police when they arrived at the murder scene.

134 Contrary to the appellant's submission, the trial judge did not suggest that the appellant's conduct after the homicide could constitute aiding or abetting. Rather, the trial judge told the jury that evidence of what the appellant did after the homicide could provide evidence that she had aided or abetted the murder by agreeing to and participating in a plan formulated with Pechaluk to murder Hoy and mislead the police. The instructions were correct in law.

135 Nor do I see any error in the trial judge's instructions with respect to abetting. On the evidence, the jury could find that the appellant encouraged Pechaluk to murder Hoy by leading Pechaluk to believe that Hoy was abusing the appellant and that the appellant could be safe and with Pechaluk only if Hoy was killed. This kind of persuasive manipulation is clearly a form of encouragement and, therefore, constitutes abetting under s. 21(1)(b).

136 The trial judge also correctly instructed the jury that in assessing the Crown's contention that the appellant manipulated Pechaluk into agreeing to murder Hoy, the jury should consider the entirety of the evidence relevant to the formation and development of the relationship between the appellant and Pechaluk. That evidence stretched back several months before Hoy's murder and properly included the evidence surrounding the appellant's trip to Las Vegas and Pechaluk's reaction to the appellant's description of the manner in which she was being mistreated by Hoy while in Las Vegas.

137 I also cannot agree with the submission that the Crown's theory that the appellant encouraged Pechaluk to murder Hoy with stories of Hoy's abuse had viability only if Hoy was not abusing the appellant. From the perspective of the Crown's case, the evidence of Hoy's alleged abuse of the appellant was important because of its effect on Pechaluk and not its ultimate truth. There was cogent evidence that Pechaluk was obsessed with the appellant, firmly believed that Hoy was abusing the appellant, wanted to protect the appellant from Hoy, and feared Hoy. This volatile emotional mix gave credence to the Crown's contention that the appellant played on these concerns in persuading Pechaluk to murder Hoy.

138 Finally, the appellant submits that the trial judge's review of the evidence pertaining to Hoy's abuse of the appellant was skewed in favour of the Crown. I see no merit in this submission. There was no evidence from any source other than the appellant that Hoy was physically abusive. It is true that two witnesses did indicate he could become angry with the appellant. The trial judge did not refer to this evidence. In my view, her failure to do so has no impact on the correctness or fairness of the jury instruction.

VI

Conclusion

139 I would dismiss the appeal.

***M. Rosenberg J.A.*:**

I agree

***Janet Simmons J.A.*:**

I agree

***M. Tulloch J.A.*:**

I agree

Appeal dismissed.

Appendix A

Two-Person Conspiracy: Jury Caution if Only one Person is Charged

The Crown must establish two things beyond a reasonable doubt to prove Mr. A's guilt.

- First, the Crown must prove beyond a reasonable doubt that the agreement alleged existed.

• If the Crown proves beyond a reasonable doubt that the agreement existed, the Crown must then prove beyond a reasonable doubt that the accused, Mr. A, entered into or joined that agreement.

The existence of the agreement and Mr. A's membership in the agreement are two separate questions and must be addressed separately by you in the manner that I will describe.

The indictment alleges that only A and B agreed with each other. It might occur to you that logic would say that if you are satisfied beyond a reasonable doubt that the agreement between A and B existed, it must follow that both A and B entered into the agreement.

Whatever logic might say to you, that is not the law. It is not the law because as I will explain to you, the evidence you are entitled to consider on the first question, that is, whether the agreement alleged existed, and the evidence you are entitled to consider on the second question, that is, whether Mr. A entered into or joined that agreement, may be quite different. You could come to different answers to the two questions because you may be considering different evidence when answering each question.

I stress that you cannot simply jump from the conclusion that the agreement existed to the conclusion that the Crown has proved beyond a reasonable doubt that Mr. A entered into or joined in that agreement with B.

Footnotes

1 In his factum, counsel also challenged two evidentiary rulings made by the trial judge. Those grounds of appeal were, however, abandoned in oral argument.

2 Beauregard J.A. agreed with Tyndale J.A. that the trial judge's directions as to the applicability of the coconspirator exception to the hearsay rule were flawed and he agreed that the curative *proviso* should be applied. Beauregard J.A. did not refer to *Carter*. LeBel J.A. in dissent would have allowed the appeal. He opined that the *Carter* instruction had to be "modified" in cases alleging a two-person conspiracy. LeBel J.A. identified the relevant error as the failure to make it clear to the jury that the reasonable doubt standard applied to the question of whether the Crown had established the existence of the agreement. This error does not seem to me to arise from the *Carter* instruction.

3 The premise of this argument seems unsound to me. For example, if six members of the jury decided that one accused had conspired with the unindicted co-conspirator and the other six members of the jury decided that the second accused had conspired with the unindicted co-conspirator, the jury would be satisfied beyond a reasonable doubt that the conspiracy existed, but would not be satisfied beyond a reasonable doubt that either accused was a member of the conspiracy.

4 Dickson C.J.C., for the majority, at para. 50, expressly agreed with McIntyre J. on the issues addressed by him other than the question of whether the appellant was wrongly excluded from his trial.

5 Even Tyndale J.A., at p. 349, did not regard the applicability of the *Carter* instruction as essential to his analysis. In his view, apart entirely from the applicability of that instruction, the trial judge's instructions on conspiracy were wrong in law.

6 For example, on the facts of this case, the trial judge could have modified the usual instruction by using the word "plan" throughout the instructions rather than the words "conspiracy" or "common design". The use of the word "plan" implies no assumption about the number of people involved.

7 For a summary of the approaches developed in other jurisdictions, see Keith Spencer, "The Common Enterprise Exception to the Hearsay Rule" (2007) 11 Int'l J. Evidence & Proof 106.

8 The facts of this case do not require a determination of whether a statement by one co-conspirator after the termination or completion of the conspiracy, but referable to its existence, for example a confession, would be admissible at step one of the *Carter* instruction as evidence of the existence of the agreement. The admissibility of that kind of after-the-fact narrative statement would depend on what inference, if any, could be legitimately drawn concerning the existence of the agreement

from the making of that statement. In *Barrow*, the Supreme Court of Canada appears to have assumed the admissibility of that kind of evidence at step one of the *Carter* analysis: see also *Bogiatzis* at para. 25 and *R. v. Viandante* at paras. 46-47.

TAB 12

Most Negative Treatment: Distinguished
Most Recent Distinguished: Arrangement de MPECO Construction inc. | 2019 QCCS 297, 2019 CarswellQue 730, EYB 2019-306949, 67 C.B.R. (6th) 87 | (Que. Bktcy., Feb 4, 2019)

2010 SCC 60
Supreme Court of Canada

Ted Leroy Trucking [Century Services] Ltd., Re

2010 CarswellBC 3419, 2010 CarswellBC 3420, 2010 SCC 60, [2010] 3 S.C.R. 379, [2010] G.S.T.C. 186, [2010] S.C.J. No. 60, [2011] 2 W.W.R. 383, [2011] B.C.W.L.D. 533, [2011] B.C.W.L.D. 534, 12 B.C.L.R. (5th) 1, 196 A.C.W.S. (3d) 27, 2011 D.T.C. 5006 (Eng.), 2011 G.T.C. 2006 (Eng.), 296 B.C.A.C. 1, 326 D.L.R. (4th) 577, 409 N.R. 201, 503 W.A.C. 1, 72 C.B.R. (5th) 170, J.E. 2011-5

Century Services Inc. (Appellant) and Attorney General of Canada on behalf of Her Majesty The Queen in Right of Canada (Respondent)

Deschamps J., McLachlin C.J.C., Binnie, LeBel, Fish, Abella, Charron, Rothstein, Cromwell JJ.

Heard: May 11, 2010
Judgment: December 16, 2010
Docket: 33239

Proceedings: reversing *Ted Leroy Trucking Ltd., Re* (2009), 2009 CarswellBC 1195, 2009 G.T.C. 2020 (Eng.), 2009 BCCA 205, 270 B.C.A.C. 167, 454 W.A.C. 167, [2009] 12 W.W.R. 684, 98 B.C.L.R. (4th) 242, [2009] G.S.T.C. 79 (B.C. C.A.); reversing *Ted Leroy Trucking Ltd., Re* (2008), 2008 CarswellBC 2895, 2008 BCSC 1805, [2008] G.S.T.C. 221, 2009 G.T.C. 2011 (Eng.) (B.C. S.C. [In Chambers])

Counsel: Mary I.A. Buttery, Owen J. James, Matthew J.G. Curtis for Appellant
Gordon Bourgard, David Jacyk, Michael J. Lema for Respondent

Subject: Estates and Trusts; Goods and Services Tax (GST); Tax — Miscellaneous; Insolvency
Related Abridgment Classifications
Tax
I General principles
I.5 Priority of tax claims in bankruptcy proceedings
Tax
III Goods and Services Tax
III.14 Collection and remittance
III.14.b GST held in trust
Headnote
Tax --- Goods and Services Tax — Collection and remittance — GST held in trust
Debtor owed Crown under Excise Tax Act (ETA) for unremitted GST — Debtor sought relief under Companies' Creditors Arrangement Act (CCAA) — Under order of BC Supreme Court, amount of GST debt was placed in trust account and remaining proceeds of sale of assets paid to major secured creditor — Debtor's application for partial lifting of stay of proceedings to assign itself into bankruptcy was granted, while Crown's application for payment of tax debt was dismissed — Crown's appeal to BC Court of Appeal was allowed — Creditor appealed to Supreme Court of Canada — Appeal allowed — Analysis of ETA and CCAA yielded conclusion that CCAA provides that statutory deemed trusts do not apply, and that Parliament did not intend to restore Crown's deemed trust priority in GST claims under CCAA when it amended ETA in 2000 — Parliament had moved away from asserting priority for Crown claims under both

CCAA and Bankruptcy and Insolvency Act (BIA), and neither statute provided for preferred treatment of GST claims — Giving Crown priority over GST claims during CCAA proceedings but not in bankruptcy would reduce use of more flexible and responsive CCAA regime — Parliament likely inadvertently succumbed to drafting anomaly — Section 222(3) of ETA could not be seen as having impliedly repealed s. 18.3 of CCAA by its subsequent passage, given recent amendments to CCAA — Court had discretion under CCAA to construct bridge to liquidation under BIA, and partially lift stay of proceedings to allow entry into liquidation — No "gap" should exist when moving from CCAA to BIA — Court order segregating funds did not have certainty that Crown rather than creditor would be beneficiary sufficient to support express trust — Amount held in respect of GST debt was not subject to deemed trust, priority or express trust in favour of Crown — Excise Tax Act, R.S.C. 1985, c. E-15, ss. 222(1), (1.1).

Tax --- General principles — Priority of tax claims in bankruptcy proceedings

Debtor owed Crown under Excise Tax Act (ETA) for unremitted GST — Debtor sought relief under Companies' Creditors Arrangement Act (CCAA) — Under order of BC Supreme Court, amount of GST debt was placed in trust account and remaining proceeds of sale of assets paid to major secured creditor — Debtor's application for partial lifting of stay of proceedings to assign itself into bankruptcy was granted, while Crown's application for payment of tax debt was dismissed — Crown's appeal to BC Court of Appeal was allowed — Creditor appealed to Supreme Court of Canada — Appeal allowed — Analysis of ETA and CCAA yielded conclusion that CCAA provides that statutory deemed trusts do not apply, and that Parliament did not intend to restore Crown's deemed trust priority in GST claims under CCAA when it amended ETA in 2000 — Parliament had moved away from asserting priority for Crown claims under both CCAA and Bankruptcy and Insolvency Act (BIA), and neither statute provided for preferred treatment of GST claims — Giving Crown priority over GST claims during CCAA proceedings but not in bankruptcy would reduce use of more flexible and responsive CCAA regime — Parliament likely inadvertently succumbed to drafting anomaly — Section 222(3) of ETA could not be seen as having impliedly repealed s. 18.3 of CCAA by its subsequent passage, given recent amendments to CCAA — Court had discretion under CCAA to construct bridge to liquidation under BIA, and partially lift stay of proceedings to allow entry into liquidation — No "gap" should exist when moving from CCAA to BIA — Court order segregating funds did not have certainty that Crown rather than creditor would be beneficiary sufficient to support express trust — Amount held in respect of GST debt was not subject to deemed trust, priority or express trust in favour of Crown.

Taxation --- Taxe sur les produits et services — Perception et versement — Montant de TPS détenu en fiducie

Débitrice devait à la Couronne des montants de TPS qu'elle n'avait pas remis, en vertu de la Loi sur la taxe d'accise (LTA) — Débitrice a entamé des procédures judiciaires en vertu de la Loi sur les arrangements avec les créanciers des compagnies (LACC) — En vertu d'une ordonnance du tribunal, le montant de la créance fiscale a été déposé dans un compte en fiducie et la balance du produit de la vente des actifs a servi à payer le créancier garanti principal — Demande de la débitrice visant à obtenir la levée partielle de la suspension de procédures afin qu'elle puisse faire cession de ses biens a été accordée, alors que la demande de la Couronne visant à obtenir le paiement des montants de TPS non remis a été rejetée — Appel interjeté par la Couronne a été accueilli — Créancier a formé un pourvoi — Pourvoi accueilli — Analyse de la LTA et de la LACC conduisait à la conclusion que le législateur ne saurait avoir eu l'intention de redonner la priorité, dans le cadre de la LACC, à la fiducie réputée de la Couronne à l'égard de ses créances relatives à la TPS quand il a modifié la LTA, en 2000 — Législateur avait mis un terme à la priorité accordée aux créances de la Couronne sous les régimes de la LACC et de la Loi sur la faillite et l'insolvabilité (LFI), et ni l'une ni l'autre de ces lois ne prévoyaient que les créances relatives à la TPS bénéficiaient d'un traitement préférentiel — Fait de faire primer la priorité de la Couronne sur les créances découlant de la TPS dans le cadre de procédures fondées sur la LACC mais pas en cas de faillite aurait pour effet de restreindre le recours à la possibilité de se restructurer sous le régime plus souple et mieux adapté de la LACC — Il semblait probable que le législateur avait par inadvertance commis une anomalie rédactionnelle — On ne pourrait pas considérer l'art. 222(3) de la LTA comme ayant implicitement abrogé l'art. 18.3 de la LACC, compte tenu des modifications récemment apportées à la LACC — Sous le régime de la LACC, le tribunal avait discrétion pour établir une passerelle vers une liquidation opérée sous le régime de la LFI et de lever la suspension partielle des procédures afin de permettre à la débitrice de procéder à la transition au régime de liquidation — Il n'y avait aucune certitude, en vertu de l'ordonnance du tribunal, que la Couronne était le bénéficiaire véritable de la fiducie ni de fondement pour donner

naissance à une fiducie expresse — Montant perçu au titre de la TPS ne faisait l'objet d'aucune fiducie présumée, priorité ou fiducie expresse en faveur de la Couronne.

Taxation --- Principes généraux — Priorité des créances fiscales dans le cadre de procédures en faillite

Débitrice devait à la Couronne des montants de TPS qu'elle n'avait pas remis, en vertu de la Loi sur la taxe d'accise (LTA) — Débitrice a entamé des procédures judiciaires en vertu de la Loi sur les arrangements avec les créanciers des compagnies (LACC) — En vertu d'une ordonnance du tribunal, le montant de la créance fiscale a été déposé dans un compte en fiducie et la balance du produit de la vente des actifs a servi à payer le créancier garanti principal — Demande de la débitrice visant à obtenir la levée partielle de la suspension de procédures afin qu'elle puisse faire cession de ses biens a été accordée, alors que la demande de la Couronne visant à obtenir le paiement des montants de TPS non remis a été rejetée — Appel interjeté par la Couronne a été accueilli — Créancier a formé un pourvoi — Pourvoi accueilli — Analyse de la LTA et de la LACC conduisait à la conclusion que le législateur ne saurait avoir eu l'intention de redonner la priorité, dans le cadre de la LACC, à la fiducie réputée de la Couronne à l'égard de ses créances relatives à la TPS quand il a modifié la LTA, en 2000 — Législateur avait mis un terme à la priorité accordée aux créances de la Couronne sous les régimes de la LACC et de la Loi sur la faillite et l'insolvabilité (LFI), et ni l'une ni l'autre de ces lois ne prévoyaient que les créances relatives à la TPS bénéficiaient d'un traitement préférentiel — Fait de faire primer la priorité de la Couronne sur les créances découlant de la TPS dans le cadre de procédures fondées sur la LACC mais pas en cas de faillite aurait pour effet de restreindre le recours à la possibilité de se restructurer sous le régime plus souple et mieux adapté de la LACC — Il semblait probable que le législateur avait par inadvertance commis une anomalie rédactionnelle — On ne pourrait pas considérer l'art. 222(3) de la LTA comme ayant implicitement abrogé l'art. 18.3 de la LACC, compte tenu des modifications récemment apportées à la LACC — Sous le régime de la LACC, le tribunal avait discrétion pour établir une passerelle vers une liquidation opérée sous le régime de la LFI et de lever la suspension partielle des procédures afin de permettre à la débitrice de procéder à la transition au régime de liquidation — Il n'y avait aucune certitude, en vertu de l'ordonnance du tribunal, que la Couronne était le bénéficiaire véritable de la fiducie ni de fondement pour donner naissance à une fiducie expresse — Montant perçu au titre de la TPS ne faisait l'objet d'aucune fiducie présumée, priorité ou fiducie expresse en faveur de la Couronne.

The debtor company owed the Crown under the Excise Tax Act (ETA) for GST that was not remitted. The debtor commenced proceedings under the Companies' Creditors Arrangement Act (CCAA). Under an order by the B.C. Supreme Court, the amount of the tax debt was placed in a trust account, and the remaining proceeds from the sale of the debtor's assets were paid to the major secured creditor. The debtor's application for a partial lifting of the stay of proceedings in order to assign itself into bankruptcy was granted, while the Crown's application for the immediate payment of the unremitted GST was dismissed.

The Crown's appeal to the B.C. Court of Appeal was allowed. The Court of Appeal found that the lower court was bound by the ETA to give the Crown priority once bankruptcy was inevitable. The Court of Appeal ruled that there was a deemed trust under s. 222 of the ETA or that an express trust was created in the Crown's favour by the court order segregating the GST funds in the trust account.

The creditor appealed to the Supreme Court of Canada.

Held: The appeal was allowed.

Per Deschamps J. (McLachlin C.J.C., Binnie, LeBel, Charron, Rothstein, Cromwell JJ. concurring): A purposive and contextual analysis of the ETA and CCAA yielded the conclusion that Parliament could not have intended to restore the Crown's deemed trust priority in GST claims under the CCAA when it amended the ETA in 2000. Parliament had moved away from asserting priority for Crown claims in insolvency law under both the CCAA and Bankruptcy and Insolvency Act (BIA). Unlike for source deductions, there was no express statutory basis in the CCAA or BIA for concluding that GST claims enjoyed any preferential treatment. The internal logic of the CCAA also militated against upholding a deemed trust for GST claims.

Giving the Crown priority over GST claims during CCAA proceedings but not in bankruptcy would, in practice, deprive companies of the option to restructure under the more flexible and responsive CCAA regime. It seemed likely that Parliament had inadvertently succumbed to a drafting anomaly, which could be resolved by giving precedence to s. 18.3 of the CCAA. Section 222(3) of the ETA could no longer be seen as having impliedly repealed s. 18.3 of the CCAA by

being passed subsequently to the CCAA, given the recent amendments to the CCAA. The legislative context supported the conclusion that s. 222(3) of the ETA was not intended to narrow the scope of s. 18.3 of the CCAA.

The breadth of the court's discretion under the CCAA was sufficient to construct a bridge to liquidation under the BIA, so there was authority under the CCAA to partially lift the stay of proceedings to allow the debtor's entry into liquidation. There should be no gap between the CCAA and BIA proceedings that would invite a race to the courthouse to assert priorities.

The court order did not have the certainty that the Crown would actually be the beneficiary of the funds sufficient to support an express trust, as the funds were segregated until the dispute between the creditor and the Crown could be resolved. The amount collected in respect of GST but not yet remitted to the Receiver General of Canada was not subject to a deemed trust, priority or express trust in favour of the Crown.

Per Fish J. (concurring): Parliament had declined to amend the provisions at issue after detailed consideration of the insolvency regime, so the apparent conflict between s. 18.3 of the CCAA and s. 222 of the ETA should not be treated as a drafting anomaly. In the insolvency context, a deemed trust would exist only when two complementary elements co-existed: first, a statutory provision creating the trust; and second, a CCAA or BIA provision confirming its effective operation. Parliament had created the Crown's deemed trust in the Income Tax Act, Canada Pension Plan and Employment Insurance Act and then confirmed in clear and unmistakable terms its continued operation under both the CCAA and the BIA regimes. In contrast, the ETA created a deemed trust in favour of the Crown, purportedly notwithstanding any contrary legislation, but Parliament did not expressly provide for its continued operation in either the BIA or the CCAA. The absence of this confirmation reflected Parliament's intention to allow the deemed trust to lapse with the commencement of insolvency proceedings. Parliament's evident intent was to render GST deemed trusts inoperative upon the institution of insolvency proceedings, and so s. 222 of the ETA mentioned the BIA so as to exclude it from its ambit, rather than include it as the other statutes did. As none of these statutes mentioned the CCAA expressly, the specific reference to the BIA had no bearing on the interaction with the CCAA. It was the confirmatory provisions in the insolvency statutes that would determine whether a given deemed trust would subsist during insolvency proceedings.

Per Abella J. (dissenting): The appellate court properly found that s. 222(3) of the ETA gave priority during CCAA proceedings to the Crown's deemed trust in unremitted GST. The failure to exempt the CCAA from the operation of this provision was a reflection of clear legislative intent. Despite the requests of various constituencies and case law confirming that the ETA took precedence over the CCAA, there was no responsive legislative revision and the BIA remained the only exempted statute. There was no policy justification for interfering, through interpretation, with this clarity of legislative intention and, in any event, the application of other principles of interpretation reinforced this conclusion. Contrary to the majority's view, the "later in time" principle did not favour the precedence of the CCAA, as the CCAA was merely re-enacted without significant substantive changes. According to the Interpretation Act, in such circumstances, s. 222(3) of the ETA remained the later provision. The chambers judge was required to respect the priority regime set out in s. 222(3) of the ETA and so did not have the authority to deny the Crown's request for payment of the GST funds during the CCAA proceedings.

La compagnie débitrice devait à la Couronne des montants de TPS qu'elle n'avait pas remis, en vertu de la Loi sur la taxe d'accise (LTA). La débitrice a entamé des procédures judiciaires en vertu de la Loi sur les arrangements avec les créanciers des compagnies (LACC). En vertu d'une ordonnance du tribunal, le montant de la créance fiscale a été déposé dans un compte en fiducie et la balance du produit de la vente des actifs de la débitrice a servi à payer le créancier garanti principal. La demande de la débitrice visant à obtenir la levée partielle de la suspension de procédures afin qu'elle puisse faire cession de ses biens a été accordée, alors que la demande de la Couronne visant à obtenir le paiement immédiat des montants de TPS non remis a été rejetée.

L'appel interjeté par la Couronne a été accueilli. La Cour d'appel a conclu que le tribunal se devait, en vertu de la LTA, de donner priorité à la Couronne une fois la faillite inévitable. La Cour d'appel a estimé que l'art. 222 de la LTA établissait une fiducie présumée ou bien que l'ordonnance du tribunal à l'effet que les montants de TPS soient détenus dans un compte en fiducie créait une fiducie expresse en faveur de la Couronne.

Le créancier a formé un pourvoi.

Arrêt: Le pourvoi a été accueilli.

Deschamps, J. (McLachlin, J.C.C., Binnie, LeBel, Charron, Rothstein, Cromwell, JJ., souscrivant à son opinion) : Une analyse téléologique et contextuelle de la LTA et de la LACC conduisait à la conclusion que le législateur ne saurait avoir eu l'intention de redonner la priorité, dans le cadre de la LACC, à la fiducie réputée de la Couronne à l'égard de ses créances relatives à la TPS quand il a modifié la LTA, en 2000. Le législateur avait mis un terme à la priorité accordée aux créances de la Couronne dans le cadre du droit de l'insolvabilité, sous le régime de la LACC et celui de la Loi sur la faillite et l'insolvabilité (LFI). Contrairement aux retenues à la source, aucune disposition législative expresse ne permettait de conclure que les créances relatives à la TPS bénéficiaient d'un traitement préférentiel sous le régime de la LACC ou celui de la LFI. La logique interne de la LACC allait également à l'encontre du maintien de la fiducie réputée à l'égard des créances découlant de la TPS.

Le fait de faire primer la priorité de la Couronne sur les créances découlant de la TPS dans le cadre de procédures fondées sur la LACC mais pas en cas de faillite aurait pour effet, dans les faits, de priver les compagnies de la possibilité de se restructurer sous le régime plus souple et mieux adapté de la LACC. Il semblait probable que le législateur avait par inadvertance commis une anomalie rédactionnelle, laquelle pouvait être corrigée en donnant préséance à l'art. 18.3 de la LACC. On ne pouvait plus considérer l'art. 222(3) de la LTA comme ayant implicitement abrogé l'art. 18.3 de la LACC parce qu'il avait été adopté après la LACC, compte tenu des modifications récemment apportées à la LACC. Le contexte législatif étayait la conclusion suivant laquelle l'art. 222(3) de la LTA n'avait pas pour but de restreindre la portée de l'art. 18.3 de la LACC.

L'ampleur du pouvoir discrétionnaire conféré au tribunal par la LACC était suffisant pour établir une passerelle vers une liquidation opérée sous le régime de la LFI, de sorte qu'il avait, en vertu de la LACC, le pouvoir de lever la suspension partielle des procédures afin de permettre à la débitrice de procéder à la transition au régime de liquidation. Il n'y avait aucune certitude, en vertu de l'ordonnance du tribunal, que la Couronne était le bénéficiaire véritable de la fiducie ni de fondement pour donner naissance à une fiducie expresse, puisque les fonds étaient détenus à part jusqu'à ce que le litige entre le créancier et la Couronne soit résolu. Le montant perçu au titre de la TPS mais non encore versé au receveur général du Canada ne faisait l'objet d'aucune fiducie présumée, priorité ou fiducie expresse en faveur de la Couronne.

Fish, J. (souscrivant aux motifs des juges majoritaires) : Le législateur a refusé de modifier les dispositions en question suivant un examen approfondi du régime d'insolvabilité, de sorte qu'on ne devrait pas qualifier l'apparente contradiction entre l'art. 18.3 de la LACC et l'art. 222 de la LTA d'anomalie rédactionnelle. Dans un contexte d'insolvabilité, on ne pourrait conclure à l'existence d'une fiducie présumée que lorsque deux éléments complémentaires étaient réunis : en premier lieu, une disposition législative qui crée la fiducie et, en second lieu, une disposition de la LACC ou de la LFI qui confirme l'existence de la fiducie. Le législateur a établi une fiducie présumée en faveur de la Couronne dans la Loi de l'impôt sur le revenu, le Régime de pensions du Canada et la Loi sur l'assurance-emploi puis, il a confirmé en termes clairs et explicites sa volonté de voir cette fiducie présumée produire ses effets sous le régime de la LACC et de la LFI. Dans le cas de la LTA, il a établi une fiducie présumée en faveur de la Couronne, sciemment et sans égard pour toute législation à l'effet contraire, mais n'a pas expressément prévu le maintien en vigueur de celle-ci sous le régime de la LFI ou celui de la LACC. L'absence d'une telle confirmation témoignait de l'intention du législateur de laisser la fiducie présumée devenir caduque au moment de l'introduction de la procédure d'insolvabilité. L'intention du législateur était manifestement de rendre inopérantes les fiducies présumées visant la TPS dès l'introduction d'une procédure d'insolvabilité et, par conséquent, l'art. 222 de la LTA mentionnait la LFI de manière à l'exclure de son champ d'application, et non de l'y inclure, comme le faisaient les autres lois. Puisqu'aucune de ces lois ne mentionnait spécifiquement la LACC, la mention explicite de la LFI n'avait aucune incidence sur l'interaction avec la LACC. C'était les dispositions confirmatoires que l'on trouvait dans les lois sur l'insolvabilité qui déterminaient si une fiducie présumée continuerait d'exister durant une procédure d'insolvabilité.

Abella, J. (dissidente) : La Cour d'appel a conclu à bon droit que l'art. 222(3) de la LTA donnait préséance à la fiducie présumée qui est établie en faveur de la Couronne à l'égard de la TPS non versée. Le fait que la LACC n'ait pas été soustraite à l'application de cette disposition témoignait d'une intention claire du législateur. Malgré les demandes répétées de divers groupes et la jurisprudence ayant confirmé que la LTA l'emportait sur la LACC, le législateur n'est pas intervenu et la LFI est demeurée la seule loi soustraite à l'application de cette disposition. Il n'y avait pas de considération de politique générale qui justifierait d'aller à l'encontre, par voie d'interprétation législative, de l'intention aussi clairement exprimée par le législateur et, de toutes manières, cette conclusion était renforcée par l'application d'autres principes

d'interprétation. Contrairement à l'opinion des juges majoritaires, le principe de la préséance de la « loi postérieure » ne militait pas en faveur de la présance de la LACC, celle-ci ayant été simplement adoptée à nouveau sans que l'on ne lui ait apporté de modifications importantes. En vertu de la Loi d'interprétation, dans ces circonstances, l'art. 222(3) de la LTA demeurait la disposition postérieure. Le juge siégeant en son cabinet était tenu de respecter le régime de priorités établi à l'art. 222(3) de la LTA, et il ne pouvait pas refuser la demande présentée par la Couronne en vue de se faire payer la TPS dans le cadre de la procédure introduite en vertu de la LACC.

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Winding-up and Restructuring Act, R.S.C. 1985, c. W-11
Generally — referred to

APPEAL by creditor from judgment reported at 2009 CarswellBC 1195, 2009 BCCA 205, [2009] G.S.T.C. 79, 98 B.C.L.R. (4th) 242, [2009] 12 W.W.R. 684, 270 B.C.A.C. 167, 454 W.A.C. 167, 2009 G.T.C. 2020 (Eng.) (B.C. C.A.), allowing Crown's appeal from dismissal of application for immediate payment of tax debt.

***Deschamps J.*:**

1 For the first time this Court is called upon to directly interpret the provisions of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"). In that respect, two questions are raised. The first requires reconciliation of provisions of the *CCAA* and the *Excise Tax Act*, R.S.C. 1985, c. E-15 ("*ETA*"), which lower courts have held to be in conflict with one another. The second concerns the scope of a court's discretion when supervising reorganization. The relevant statutory provisions are reproduced in the Appendix. On the first question, having considered the evolution of Crown priorities in the context of insolvency and the wording of the various statutes creating Crown priorities, I conclude that it is the *CCAA* and not the *ETA* that provides the rule. On the second question, I conclude that the broad discretionary jurisdiction conferred on the supervising judge must be interpreted having regard to the remedial nature of the *CCAA* and insolvency legislation generally. Consequently, the court had the discretion to partially lift a stay of proceedings to allow the debtor to make an assignment under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*"). I would allow the appeal.

1. Facts and Decisions of the Courts Below

2 Ted LeRoy Trucking Ltd. ("LeRoy Trucking") commenced proceedings under the *CCAA* in the Supreme Court of British Columbia on December 13, 2007, obtaining a stay of proceedings with a view to reorganizing its financial affairs. LeRoy Trucking sold certain redundant assets as authorized by the order.

3 Amongst the debts owed by LeRoy Trucking was an amount for Goods and Services Tax ("GST") collected but unremitted to the Crown. The *ETA* creates a deemed trust in favour of the Crown for amounts collected in respect of GST. The deemed trust extends to any property or proceeds held by the person collecting GST and any property of that person held by a secured creditor, requiring that property to be paid to the Crown in priority to all security interests. The *ETA* provides that the deemed trust operates despite any other enactment of Canada except the *BIA*. However, the *CCAA* also provides that subject to certain exceptions, none of which mentions GST, deemed trusts in favour of the Crown do not operate under the *CCAA*. Accordingly, under the *CCAA* the Crown ranks as an unsecured creditor in respect of GST. Nonetheless, at the time LeRoy Trucking commenced *CCAA* proceedings the leading line of jurisprudence held that the *ETA* took precedence over the *CCAA* such that the Crown enjoyed priority for GST claims under the *CCAA*, even though it would have lost that same priority under the *BIA*. The *CCAA* underwent substantial amendments in 2005 in which some of the provisions at issue in this appeal were renumbered and reformulated (S.C. 2005, c. 47). However, these amendments only came into force on September 18, 2009. I will refer to the amended provisions only where relevant.

4 On April 29, 2008, Brenner C.J.S.C., in the context of the *CCAA* proceedings, approved a payment not exceeding $5 million, the proceeds of redundant asset sales, to Century Services, the debtor's major secured creditor. LeRoy Trucking

proposed to hold back an amount equal to the GST monies collected but unremitted to the Crown and place it in the Monitor's trust account until the outcome of the reorganization was known. In order to maintain the *status quo* while the success of the reorganization was uncertain, Brenner C.J.S.C. agreed to the proposal and ordered that an amount of $305,202.30 be held by the Monitor in its trust account.

5 On September 3, 2008, having concluded that reorganization was not possible, LeRoy Trucking sought leave to make an assignment in bankruptcy under the *BIA*. The Crown sought an order that the GST monies held by the Monitor be paid to the Receiver General of Canada. Brenner C.J.S.C. dismissed the latter application. Reasoning that the purpose of segregating the funds with the Monitor was "to facilitate an ultimate payment of the GST monies which were owed pre-filing, but only if a viable plan emerged", the failure of such a reorganization, followed by an assignment in bankruptcy, meant the Crown would lose priority under the *BIA* (2008 BCSC 1805, [2008] G.S.T.C. 221 (B.C. S.C. [In Chambers])).

6 The Crown's appeal was allowed by the British Columbia Court of Appeal (2009 BCCA 205, [2009] G.S.T.C. 79, 270 B.C.A.C. 167 (B.C. C.A.)). Tysoe J.A. for a unanimous court found two independent bases for allowing the Crown's appeal.

7 First, the court's authority under s. 11 of the *CCAA* was held not to extend to staying the Crown's application for immediate payment of the GST funds subject to the deemed trust after it was clear that reorganization efforts had failed and that bankruptcy was inevitable. As restructuring was no longer a possibility, staying the Crown's claim to the GST funds no longer served a purpose under the *CCAA* and the court was bound under the priority scheme provided by the *ETA* to allow payment to the Crown. In so holding, Tysoe J.A. adopted the reasoning in *Ottawa Senators Hockey Club Corp. (Re)*, [2005] G.S.T.C. 1, 73 O.R. (3d) 737 (Ont. C.A.), which found that the *ETA* deemed trust for GST established Crown priority over secured creditors under the *CCAA*.

8 Second, Tysoe J.A. concluded that by ordering the GST funds segregated in the Monitor's trust account on April 29, 2008, the judge had created an express trust in favour of the Crown from which the monies in question could not be diverted for any other purposes. The Court of Appeal therefore ordered that the money held by the Monitor in trust be paid to the Receiver General.

2. Issues

9 This appeal raises three broad issues which are addressed in turn:

(1) Did s. 222(3) of the *ETA* displace s. 18.3(1) of the *CCAA* and give priority to the Crown's *ETA* deemed trust during *CCAA* proceedings as held in *Ottawa Senators*?

(2) Did the court exceed its *CCAA* authority by lifting the stay to allow the debtor to make an assignment in bankruptcy?

(3) Did the court's order of April 29, 2008 requiring segregation of the Crown's GST claim in the Monitor's trust account create an express trust in favour of the Crown in respect of those funds?

3. Analysis

10 The first issue concerns Crown priorities in the context of insolvency. As will be seen, the *ETA* provides for a deemed trust in favour of the Crown in respect of GST owed by a debtor "[d]espite ... any other enactment of Canada (except the *Bankruptcy and Insolvency Act*)" (s. 222(3)), while the *CCAA* stated at the relevant time that "notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be [so] regarded" (s. 18.3(1)). It is difficult to imagine two statutory provisions more apparently in conflict. However, as is often the case, the apparent conflict can be resolved through interpretation.

11 In order to properly interpret the provisions, it is necessary to examine the history of the *CCAA*, its function amidst the body of insolvency legislation enacted by Parliament, and the principles that have been recognized in the

jurisprudence. It will be seen that Crown priorities in the insolvency context have been significantly pared down. The resolution of the second issue is also rooted in the context of the *CCAA*, but its purpose and the manner in which it has been interpreted in the case law are also key. After examining the first two issues in this case, I will address Tysoe J.A.'s conclusion that an express trust in favour of the Crown was created by the court's order of April 29, 2008.

3.1 Purpose and Scope of Insolvency Law

12 Insolvency is the factual situation that arises when a debtor is unable to pay creditors (see generally, R. J. Wood, *Bankruptcy and Insolvency Law* (2009), at p. 16). Certain legal proceedings become available upon insolvency, which typically allow a debtor to obtain a court order staying its creditors' enforcement actions and attempt to obtain a binding compromise with creditors to adjust the payment conditions to something more realistic. Alternatively, the debtor's assets may be liquidated and debts paid from the proceeds according to statutory priority rules. The former is usually referred to as reorganization or restructuring while the latter is termed liquidation.

13 Canadian commercial insolvency law is not codified in one exhaustive statute. Instead, Parliament has enacted multiple insolvency statutes, the main one being the *BIA*. The *BIA* offers a self-contained legal regime providing for both reorganization and liquidation. Although bankruptcy legislation has a long history, the *BIA* itself is a fairly recent statute — it was enacted in 1992. It is characterized by a rules-based approach to proceedings. The *BIA* is available to insolvent debtors owing $1000 or more, regardless of whether they are natural or legal persons. It contains mechanisms for debtors to make proposals to their creditors for the adjustment of debts. If a proposal fails, the *BIA* contains a bridge to bankruptcy whereby the debtor's assets are liquidated and the proceeds paid to creditors in accordance with the statutory scheme of distribution.

14 Access to the *CCAA* is more restrictive. A debtor must be a company with liabilities in excess of $5 million. Unlike the *BIA*, the *CCAA* contains no provisions for liquidation of a debtor's assets if reorganization fails. There are three ways of exiting *CCAA* proceedings. The best outcome is achieved when the stay of proceedings provides the debtor with some breathing space during which solvency is restored and the *CCAA* process terminates without reorganization being needed. The second most desirable outcome occurs when the debtor's compromise or arrangement is accepted by its creditors and the reorganized company emerges from the *CCAA* proceedings as a going concern. Lastly, if the compromise or arrangement fails, either the company or its creditors usually seek to have the debtor's assets liquidated under the applicable provisions of the *BIA* or to place the debtor into receivership. As discussed in greater detail below, the key difference between the reorganization regimes under the *BIA* and the *CCAA* is that the latter offers a more flexible mechanism with greater judicial discretion, making it more responsive to complex reorganizations.

15 As I will discuss at greater length below, the purpose of the *CCAA* — Canada's first reorganization statute — is to permit the debtor to continue to carry on business and, where possible, avoid the social and economic costs of liquidating its assets. Proposals to creditors under the *BIA* serve the same remedial purpose, though this is achieved through a rules-based mechanism that offers less flexibility. Where reorganization is impossible, the *BIA* may be employed to provide an orderly mechanism for the distribution of a debtor's assets to satisfy creditor claims according to predetermined priority rules.

16 Prior to the enactment of the *CCAA* in 1933 (S.C. 1932-33, c. 36), practice under existing commercial insolvency legislation tended heavily towards the liquidation of a debtor company (J. Sarra, *Creditor Rights and the Public Interest: Restructuring Insolvent Corporations* (2003), at p. 12). The battering visited upon Canadian businesses by the Great Depression and the absence of an effective mechanism for reaching a compromise between debtors and creditors to avoid liquidation required a legislative response. The *CCAA* was innovative as it allowed the insolvent debtor to attempt reorganization under judicial supervision outside the existing insolvency legislation which, once engaged, almost invariably resulted in liquidation (*Reference re Companies' Creditors Arrangement Act (Canada)*, [1934] S.C.R. 659 (S.C.C.), at pp. 660-61; Sarra, *Creditor Rights*, at pp. 12-13).

17 Parliament understood when adopting the *CCAA* that liquidation of an insolvent company was harmful for most of those it affected — notably creditors and employees — and that a workout which allowed the company to survive was optimal (Sarra, *Creditor Rights*, at pp. 13-15).

18 Early commentary and jurisprudence also endorsed the *CCAA's* remedial objectives. It recognized that companies retain more value as going concerns while underscoring that intangible losses, such as the evaporation of the companies' goodwill, result from liquidation (S. E. Edwards, "Reorganizations Under the Companies' Creditors Arrangement Act" (1947), 25 *Can. Bar Rev.* 587, at p. 592). Reorganization serves the public interest by facilitating the survival of companies supplying goods or services crucial to the health of the economy or saving large numbers of jobs (*ibid.*, at p. 593). Insolvency could be so widely felt as to impact stakeholders other than creditors and employees. Variants of these views resonate today, with reorganization justified in terms of rehabilitating companies that are key elements in a complex web of interdependent economic relationships in order to avoid the negative consequences of liquidation.

19 The *CCAA* fell into disuse during the next several decades, likely because amendments to the Act in 1953 restricted its use to companies issuing bonds (S.C. 1952-53, c. 3). During the economic downturn of the early 1980s, insolvency lawyers and courts adapting to the resulting wave of insolvencies resurrected the statute and deployed it in response to new economic challenges. Participants in insolvency proceedings grew to recognize and appreciate the statute's distinguishing feature: a grant of broad and flexible authority to the supervising court to make the orders necessary to facilitate the reorganization of the debtor and achieve the *CCAA's* objectives. The manner in which courts have used *CCAA* jurisdiction in increasingly creative and flexible ways is explored in greater detail below.

20 Efforts to evolve insolvency law were not restricted to the courts during this period. In 1970, a government-commissioned panel produced an extensive study recommending sweeping reform but Parliament failed to act (see *Bankruptcy and Insolvency: Report of the Study Committee on Bankruptcy and Insolvency Legislation* (1970)). Another panel of experts produced more limited recommendations in 1986 which eventually resulted in enactment of the *Bankruptcy and Insolvency Act* of 1992 (S.C. 1992, c. 27) (see *Proposed Bankruptcy Act Amendments: Report of the Advisory Committee on Bankruptcy and Insolvency* (1986)). Broader provisions for reorganizing insolvent debtors were then included in Canada's bankruptcy statute. Although the 1970 and 1986 reports made no specific recommendations with respect to the *CCAA*, the House of Commons committee studying the *BIA*'s predecessor bill, C-22, seemed to accept expert testimony that the *BIA*'s new reorganization scheme would shortly supplant the *CCAA*, which could then be repealed, with commercial insolvency and bankruptcy being governed by a single statute (*Minutes of Proceedings and Evidence of the Standing Committee on Consumer and Corporate Affairs and Government Operations*, Issue No. 15, October 3, 1991, at pp. 15:15-15:16).

21 In retrospect, this conclusion by the House of Commons committee was out of step with reality. It overlooked the renewed vitality the *CCAA* enjoyed in contemporary practice and the advantage that a flexible judicially supervised reorganization process presented in the face of increasingly complex reorganizations, when compared to the stricter rules-based scheme contained in the *BIA*. The "flexibility of the *CCAA* [was seen as] a great benefit, allowing for creative and effective decisions" (Industry Canada, Marketplace Framework Policy Branch, *Report on the Operation and Administration of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act* (2002), at p. 41). Over the past three decades, resurrection of the *CCAA* has thus been the mainspring of a process through which, one author concludes, "the legal setting for Canadian insolvency restructuring has evolved from a rather blunt instrument to one of the most sophisticated systems in the developed world" (R. B. Jones, "The Evolution of Canadian Restructuring: Challenges for the Rule of Law", in J. P. Sarra, ed., *Annual Review of Insolvency Law 2005* (2006), 481, at p. 481).

22 While insolvency proceedings may be governed by different statutory schemes, they share some commonalities. The most prominent of these is the single proceeding model. The nature and purpose of the single proceeding model are described by Professor Wood in *Bankruptcy and Insolvency Law*:

> They all provide a collective proceeding that supersedes the usual civil process available to creditors to enforce their claims. The creditors' remedies are collectivized in order to prevent the free-for-all that would otherwise prevail if creditors were permitted to exercise their remedies. In the absence of a collective process, each creditor is armed with the knowledge that if they do not strike hard and swift to seize the debtor's assets, they will be beat out by other creditors. [pp. 2-3]

The single proceeding model avoids the inefficiency and chaos that would attend insolvency if each creditor initiated proceedings to recover its debt. Grouping all possible actions against the debtor into a single proceeding controlled in a single forum facilitates negotiation with creditors because it places them all on an equal footing, rather than exposing them to the risk that a more aggressive creditor will realize its claims against the debtor's limited assets while the other creditors attempt a compromise. With a view to achieving that purpose, both the *CCAA* and the *BIA* allow a court to order all actions against a debtor to be stayed while a compromise is sought.

23 Another point of convergence of the *CCAA* and the *BIA* relates to priorities. Because the *CCAA* is silent about what happens if reorganization fails, the *BIA* scheme of liquidation and distribution necessarily supplies the backdrop for what will happen if a *CCAA* reorganization is ultimately unsuccessful. In addition, one of the important features of legislative reform of both statutes since the enactment of the *BIA* in 1992 has been a cutback in Crown priorities (S.C. 1992, c. 27, s. 39; S.C. 1997, c. 12, ss. 73 and 125; S.C. 2000, c. 30, s. 148; S.C. 2005, c. 47, ss. 69 and 131; S.C. 2009, c. 33, ss. 25 and 29; see also *Alternative granite & marbre inc., Re*, 2009 SCC 49, [2009] 3 S.C.R. 286, [2009] G.S.T.C. 154 (S.C.C.); *Quebec (Deputy Minister of Revenue) c. Rainville* (1979), [1980] 1 S.C.R. 35 (S.C.C.); *Proposed Bankruptcy Act Amendments: Report of the Advisory Committee on Bankruptcy and Insolvency* (1986)).

24 With parallel *CCAA* and *BIA* restructuring schemes now an accepted feature of the insolvency law landscape, the contemporary thrust of legislative reform has been towards harmonizing aspects of insolvency law common to the two statutory schemes to the extent possible and encouraging reorganization over liquidation (see *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts*, S.C. 2005, c. 47; *Gauntlet Energy Corp., Re*, 2003 ABQB 894, [2003] G.S.T.C. 193, 30 Alta. L.R. (4th) 192 (Alta. Q.B.), at para. 19).

25 Mindful of the historical background of the *CCAA* and *BIA*, I now turn to the first question at issue.

3.2 GST Deemed Trust Under the CCAA

26 The Court of Appeal proceeded on the basis that the *ETA* precluded the court from staying the Crown's enforcement of the GST deemed trust when partially lifting the stay to allow the debtor to enter bankruptcy. In so doing, it adopted the reasoning in a line of cases culminating in *Ottawa Senators*, which held that an *ETA* deemed trust remains enforceable during *CCAA* reorganization despite language in the *CCAA* that suggests otherwise.

27 The Crown relies heavily on the decision of the Ontario Court of Appeal in *Ottawa Senators* and argues that the later in time provision of the *ETA* creating the GST deemed trust trumps the provision of the *CCAA* purporting to nullify most statutory deemed trusts. The Court of Appeal in this case accepted this reasoning but not all provincial courts follow it (see, e.g., *Komunik Corp., Re*, 2009 QCCS 6332 (C.S. Que.), leave to appeal granted, 2010 QCCA 183 (C.A. Que.)). Century Services relied, in its written submissions to this Court, on the argument that the court had authority under the *CCAA* to continue the stay against the Crown's claim for unremitted GST. In oral argument, the question of whether *Ottawa Senators* was correctly decided nonetheless arose. After the hearing, the parties were asked to make further written submissions on this point. As appears evident from the reasons of my colleague Abella J., this issue has become prominent before this Court. In those circumstances, this Court needs to determine the correctness of the reasoning in *Ottawa Senators*.

28 The policy backdrop to this question involves the Crown's priority as a creditor in insolvency situations which, as I mentioned above, has evolved considerably. Prior to the 1990s, Crown claims largely enjoyed priority in insolvency. This

was widely seen as unsatisfactory as shown by both the 1970 and 1986 insolvency reform proposals, which recommended that Crown claims receive no preferential treatment. A closely related matter was whether the *CCAA* was binding at all upon the Crown. Amendments to the *CCAA* in 1997 confirmed that it did indeed bind the Crown (see *CCAA*, s. 21, as am. by S.C. 1997, c. 12, s. 126).

29 Claims of priority by the state in insolvency situations receive different treatment across jurisdictions worldwide. For example, in Germany and Australia, the state is given no priority at all, while the state enjoys wide priority in the United States and France (see B. K. Morgan, "Should the Sovereign be Paid First? A Comparative International Analysis of the Priority for Tax Claims in Bankruptcy" (2000), 74 *Am. Bank. L.J.* 461, at p. 500). Canada adopted a middle course through legislative reform of Crown priority initiated in 1992. The Crown retained priority for source deductions of income tax, Employment Insurance ("EI") and Canada Pension Plan ("CPP") premiums, but ranks as an ordinary unsecured creditor for most other claims.

30 Parliament has frequently enacted statutory mechanisms to secure Crown claims and permit their enforcement. The two most common are statutory deemed trusts and powers to garnish funds third parties owe the debtor (see F. L. Lamer, *Priority of Crown Claims in Insolvency* (loose-leaf), at § 2).

31 With respect to GST collected, Parliament has enacted a deemed trust. The *ETA* states that every person who collects an amount on account of GST is deemed to hold that amount in trust for the Crown (s. 222(1)). The deemed trust extends to other property of the person collecting the tax equal in value to the amount deemed to be in trust if that amount has not been remitted in accordance with the *ETA*. The deemed trust also extends to property held by a secured creditor that, but for the security interest, would be property of the person collecting the tax (s. 222(3)).

32 Parliament has created similar deemed trusts using almost identical language in respect of source deductions of income tax, EI premiums and CPP premiums (see s. 227(4) of the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) ("*ITA*"), ss. 86(2) and (2.1) of the *Employment Insurance Act*, S.C. 1996, c. 23, and ss. 23(3) and (4) of the *Canada Pension Plan*, R.S.C. 1985, c. C-8). I will refer to income tax, EI and CPP deductions as "source deductions".

33 In *Royal Bank v. Sparrow Electric Corp.*, [1997] 1 S.C.R. 411 (S.C.C.), this Court addressed a priority dispute between a deemed trust for source deductions under the *ITA* and security interests taken under both the *Bank Act*, S.C. 1991, c. 46, and the Alberta *Personal Property Security Act*, S.A. 1988, c. P-4.05 ("*PPSA*"). As then worded, an *ITA* deemed trust over the debtor's property equivalent to the amount owing in respect of income tax became effective at the time of liquidation, receivership, or assignment in bankruptcy. *Sparrow Electric* held that the *ITA* deemed trust could not prevail over the security interests because, being fixed charges, the latter attached as soon as the debtor acquired rights in the property such that the *ITA* deemed trust had no property on which to attach when it subsequently arose. Later, in *First Vancouver Finance v. Minister of National Revenue*, 2002 SCC 49, [2002] G.S.T.C. 23, [2002] 2 S.C.R. 720 (S.C.C.), this Court observed that Parliament had legislated to strengthen the statutory deemed trust in the *ITA* by deeming it to operate from the moment the deductions were not paid to the Crown as required by the *ITA*, and by granting the Crown priority over all security interests (paras. 27-29) (the "*Sparrow Electric* amendment").

34 The amended text of s. 227(4.1) of the *ITA* and concordant source deductions deemed trusts in the *Canada Pension Plan* and the *Employment Insurance Act* state that the deemed trust operates notwithstanding any other enactment of Canada, except ss. 81.1 and 81.2 of the *BIA*. The *ETA* deemed trust at issue in this case is similarly worded, but it excepts the *BIA* in its entirety. The provision reads as follows:

> **222.** (3) Despite any other provision of this Act (except subsection (4)), any other enactment of Canada (except the *Bankruptcy and Insolvency Act*), any enactment of a province or any other law, if at any time an amount deemed by subsection (1) to be held by a person in trust for Her Majesty is not remitted to the Receiver General or withdrawn in the manner and at the time provided under this Part, property of the person and property held by any secured creditor of the person that, but for a security interest, would be property of the person, equal in value to the amount so deemed to be held in trust, is deemed ....

35 The Crown submits that the *Sparrow Electric* amendment, added by Parliament to the *ETA* in 2000, was intended to preserve the Crown's priority over collected GST under the *CCAA* while subordinating the Crown to the status of an unsecured creditor in respect of GST only under the *BIA*. This is because the *ETA* provides that the GST deemed trust is effective "despite" any other enactment except the *BIA*.

36 The language used in the *ETA* for the GST deemed trust creates an apparent conflict with the *CCAA*, which provides that subject to certain exceptions, property deemed by statute to be held in trust for the Crown shall not be so regarded.

37 Through a 1997 amendment to the *CCAA* (S.C. 1997, c. 12, s. 125), Parliament appears to have, subject to specific exceptions, nullified deemed trusts in favour of the Crown once reorganization proceedings are commenced under the Act. The relevant provision reads:

> **18.3** (1) Subject to subsection (2), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

This nullification of deemed trusts was continued in further amendments to the *CCAA* (S.C. 2005, c. 47), where s. 18.3(1) was renumbered and reformulated as s. 37(1):

> **37.** (1) Subject to subsection (2), despite any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as being held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

38 An analogous provision exists in the *BIA*, which, subject to the same specific exceptions, nullifies statutory deemed trusts and makes property of the bankrupt that would otherwise be subject to a deemed trust part of the debtor's estate and available to creditors (S.C. 1992, c. 27, s. 39; S.C. 1997, c. 12, s. 73; *BIA*, s. 67(2)). It is noteworthy that in both the *CCAA* and the *BIA*, the exceptions concern source deductions (*CCAA*, s. 18.3(2); *BIA*, s. 67(3)). The relevant provision of the *CCAA* reads:

> **18.3** (2) Subsection (1) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act*....

Thus, the Crown's deemed trust and corresponding priority in source deductions remain effective both in reorganization and in bankruptcy.

39 Meanwhile, in both s. 18.4(1) of the *CCAA* and s. 86(1) of the *BIA*, other Crown claims are treated as unsecured. These provisions, establishing the Crown's status as an unsecured creditor, explicitly exempt statutory deemed trusts in source deductions (*CCAA*, s. 18.4(3); *BIA*, s. 86(3)). The *CCAA* provision reads as follows:

> **18.4** (3) Subsection (1) [Crown ranking as unsecured creditor] does not affect the operation of
>
> (a) subsections 224(1.2) and (1.3) of the *Income Tax Act*,
>
> (b) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution ....

Therefore, not only does the *CCAA* provide that Crown claims do not enjoy priority over the claims of other creditors (s. 18.3(1)), but the exceptions to this rule (i.e., that Crown priority is maintained for source deductions) are repeatedly stated in the statute.

40 The apparent conflict in this case is whether the rule in the *CCAA* first enacted as s. 18.3 in 1997, which provides that subject to certain explicit exceptions, statutory deemed trusts are ineffective under the *CCAA*, is overridden by the one in the *ETA* enacted in 2000 stating that GST deemed trusts operate despite any enactment of Canada except the *BIA*. With respect for my colleague Fish J., I do not think the apparent conflict can be resolved by denying it and creating a rule requiring both a statutory provision enacting the deemed trust, and a second statutory provision confirming it. Such a rule is unknown to the law. Courts must recognize conflicts, apparent or real, and resolve them when possible.

41 A line of jurisprudence across Canada has resolved the apparent conflict in favour of the *ETA*, thereby maintaining GST deemed trusts under the *CCAA*. *Ottawa Senators*, the leading case, decided the matter by invoking the doctrine of implied repeal to hold that the later in time provision of the *ETA* should take precedence over the *CCAA* (see also *Solid Resources Ltd., Re* (2002), 40 C.B.R. (4th) 219, [2003] G.S.T.C. 21 (Alta. Q.B.); *Gauntlet*

42 The Ontario Court of Appeal in *Ottawa Senators* rested its conclusion on two considerations. First, it was persuaded that by explicitly mentioning the *BIA* in *ETA* s. 222(3), but not the *CCAA*, Parliament made a deliberate choice. In the words of MacPherson J.A.:

> The *BIA* and the *CCAA* are closely related federal statutes. I cannot conceive that Parliament would specifically identify the *BIA* as an exception, but accidentally fail to consider the *CCAA* as a possible second exception. In my view, the omission of the *CCAA* from s. 222(3) of the *ETA* was almost certainly a considered omission. [para. 43]

43 Second, the Ontario Court of Appeal compared the conflict between the *ETA* and the *CCAA* to that before this Court in *Doré c. Verdun (Municipalité)*, [1997] 2 S.C.R. 862 (S.C.C.), and found them to be "identical" (para. 46). It therefore considered *Doré* binding (para. 49). In *Doré*, a limitations provision in the more general and recently enacted *Civil Code of Québec*, S.Q. 1991, c. 64 ("*C.C.Q.*"), was held to have repealed a more specific provision of the earlier Quebec *Cities and Towns Act*, R.S.Q., c. C-19, with which it conflicted. By analogy, the Ontario Court of Appeal held that the later in time and more general provision, s. 222(3) of the *ETA*, impliedly repealed the more specific and earlier in time provision, s. 18.3(1) of the *CCAA* (paras. 47-49).

44 Viewing this issue in its entire context, several considerations lead me to conclude that neither the reasoning nor the result in *Ottawa Senators* can stand. While a conflict may exist at the level of the statutes' wording, a purposive and contextual analysis to determine Parliament's true intent yields the conclusion that Parliament could not have intended to restore the Crown's deemed trust priority in GST claims under the *CCAA* when it amended the *ETA* in 2000 with the *Sparrow Electric* amendment.

45 I begin by recalling that Parliament has shown its willingness to move away from asserting priority for Crown claims in insolvency law. Section 18.3(1) of the *CCAA* (subject to the s. 18.3(2) exceptions) provides that the Crown's deemed trusts have no effect under the *CCAA*. Where Parliament has sought to protect certain Crown claims through statutory deemed trusts and intended that these deemed trusts continue in insolvency, it has legislated so explicitly and elaborately. For example, s. 18.3(2) of the *CCAA* and s. 67(3) of the *BIA* expressly provide that deemed trusts for source deductions remain effective in insolvency. Parliament has, therefore, clearly carved out exceptions from the general rule that deemed trusts are ineffective in insolvency. The *CCAA* and *BIA* are in harmony, preserving deemed trusts and asserting Crown priority only in respect of source deductions. Meanwhile, there is no express statutory basis for concluding that GST claims enjoy a preferred treatment under the *CCAA* or the *BIA*. Unlike source deductions, which are clearly and expressly dealt with under both these insolvency statutes, no such clear and express language exists in those Acts carving out an exception for GST claims.

46 The internal logic of the *CCAA* also militates against upholding the *ETA* deemed trust for GST. The *CCAA* imposes limits on a suspension by the court of the Crown's rights in respect of source deductions but does not mention the *ETA* (s. 11.4). Since source deductions deemed trusts are granted explicit protection under the *CCAA*, it would be

inconsistent to afford a better protection to the *ETA* deemed trust absent explicit language in the *CCAA*. Thus, the logic of the *CCAA* appears to subject the *ETA* deemed trust to the waiver by Parliament of its priority (s. 18.4).

47 Moreover, a strange asymmetry would arise if the interpretation giving the *ETA* priority over the *CCAA* urged by the Crown is adopted here: the Crown would retain priority over GST claims during *CCAA* proceedings but not in bankruptcy. As courts have reflected, this can only encourage statute shopping by secured creditors in cases such as this one where the debtor's assets cannot satisfy both the secured creditors' and the Crown's claims (*Gauntlet*, at para. 21). If creditors' claims were better protected by liquidation under the *BIA*, creditors' incentives would lie overwhelmingly with avoiding proceedings under the *CCAA* and not risking a failed reorganization. Giving a key player in any insolvency such skewed incentives against reorganizing under the *CCAA* can only undermine that statute's remedial objectives and risk inviting the very social ills that it was enacted to avert.

48 Arguably, the effect of *Ottawa Senators* is mitigated if restructuring is attempted under the *BIA* instead of the *CCAA*, but it is not cured. If *Ottawa Senators* were to be followed, Crown priority over GST would differ depending on whether restructuring took place under the *CCAA* or the *BIA*. The anomaly of this result is made manifest by the fact that it would deprive companies of the option to restructure under the more flexible and responsive *CCAA* regime, which has been the statute of choice for complex reorganizations.

49 Evidence that Parliament intended different treatments for GST claims in reorganization and bankruptcy is scant, if it exists at all. Section 222(3) of the *ETA* was enacted as part of a wide-ranging budget implementation bill in 2000. The summary accompanying that bill does not indicate that Parliament intended to elevate Crown priority over GST claims under the *CCAA* to the same or a higher level than source deductions claims. Indeed, the summary for deemed trusts states only that amendments to existing provisions are aimed at "ensuring that employment insurance premiums and Canada Pension Plan contributions that are required to be remitted by an employer are fully recoverable by the Crown in the case of the bankruptcy of the employer" (Summary to S.C. 2000, c. 30, at p. 4a). The wording of GST deemed trusts resembles that of statutory deemed trusts for source deductions and incorporates the same overriding language and reference to the *BIA*. However, as noted above, Parliament's express intent is that only source deductions deemed trusts remain operative. An exception for the *BIA* in the statutory language establishing the source deductions deemed trusts accomplishes very little, because the explicit language of the *BIA* itself (and the *CCAA*) carves out these source deductions deemed trusts and maintains their effect. It is however noteworthy that no equivalent language maintaining GST deemed trusts exists under either the *BIA* or the *CCAA*.

50 It seems more likely that by adopting the same language for creating GST deemed trusts in the *ETA* as it did for deemed trusts for source deductions, and by overlooking the inclusion of an exception for the *CCAA* alongside the *BIA* in s. 222(3) of the *ETA*, Parliament may have inadvertently succumbed to a drafting anomaly. Because of a statutory lacuna in the *ETA*, the GST deemed trust could be seen as remaining effective in the *CCAA*, while ceasing to have any effect under the *BIA*, thus creating an apparent conflict with the wording of the *CCAA*. However, it should be seen for what it is: a facial conflict only, capable of resolution by looking at the broader approach taken to Crown priorities and by giving precedence to the statutory language of s. 18.3 of the *CCAA* in a manner that does not produce an anomalous outcome.

51 Section 222(3) of the *ETA* evinces no explicit intention of Parliament to repeal *CCAA* s. 18.3. It merely creates an apparent conflict that must be resolved by statutory interpretation. Parliament's intent when it enacted *ETA* s. 222(3) was therefore far from unambiguous. Had it sought to give the Crown a priority for GST claims, it could have done so explicitly as it did for source deductions. Instead, one is left to infer from the language of *ETA* s. 222(3) that the GST deemed trust was intended to be effective under the *CCAA*.

52 I am not persuaded that the reasoning in *Doré* requires the application of the doctrine of implied repeal in the circumstances of this case. The main issue in *Doré* concerned the impact of the adoption of the *C.C.Q.* on the administrative law rules with respect to municipalities. While Gonthier J. concluded in that case that the limitation provision in art. 2930 *C.C.Q.* had repealed by implication a limitation provision in the *Cities and Towns Act*, he did so on the basis of more than a textual analysis. The conclusion in *Doré* was reached after thorough contextual analysis of

both pieces of legislation, including an extensive review of the relevant legislative history (paras. 31-41). Consequently, the circumstances before this Court in *Doré* are far from "identical" to those in the present case, in terms of text, context and legislative history. Accordingly, *Doré* cannot be said to require the automatic application of the rule of repeal by implication.

53 A noteworthy indicator of Parliament's overall intent is the fact that in subsequent amendments it has not displaced the rule set out in the *CCAA*. Indeed, as indicated above, the recent amendments to the *CCAA* in 2005 resulted in the rule previously found in s. 18.3 being renumbered and reformulated as s. 37. Thus, to the extent the interpretation allowing the GST deemed trust to remain effective under the *CCAA* depends on *ETA* s. 222(3) having impliedly repealed *CCAA* s. 18.3(1) because it is later in time, we have come full circle. Parliament has renumbered and reformulated the provision of the *CCAA* stating that, subject to exceptions for source deductions, deemed trusts do not survive the *CCAA* proceedings and thus the *CCAA* is now the later in time statute. This confirms that Parliament's intent with respect to GST deemed trusts is to be found in the *CCAA*.

54 I do not agree with my colleague Abella J. that s. 44(*f*) of the *Interpretation Act*, R.S.C. 1985, c. I-21, can be used to interpret the 2005 amendments as having no effect. The new statute can hardly be said to be a mere re-enactment of the former statute. Indeed, the *CCAA* underwent a substantial review in 2005. Notably, acting consistently with its goal of treating both the *BIA* and the *CCAA* as sharing the same approach to insolvency, Parliament made parallel amendments to both statutes with respect to corporate proposals. In addition, new provisions were introduced regarding the treatment of contracts, collective agreements, interim financing and governance agreements. The appointment and role of the Monitor was also clarified. Noteworthy are the limits imposed by *CCAA* s. 11.09 on the court's discretion to make an order staying the Crown's source deductions deemed trusts, which were formerly found in s. 11.4. No mention whatsoever is made of GST deemed trusts (see Summary to S.C. 2005, c. 47). The review went as far as looking at the very expression used to describe the statutory override of deemed trusts. The comments cited by my colleague only emphasize the clear intent of Parliament to maintain its policy that only source deductions deemed trusts survive in *CCAA* proceedings.

55 In the case at bar, the legislative context informs the determination of Parliament's legislative intent and supports the conclusion that *ETA* s. 222(3) was not intended to narrow the scope of the *CCAA's* override provision. Viewed in its entire context, the conflict between the *ETA* and the *CCAA* is more apparent than real. I would therefore not follow the reasoning in *Ottawa Senators* and affirm that *CCAA* s. 18.3 remained effective.

56 My conclusion is reinforced by the purpose of the *CCAA* as part of Canadian remedial insolvency legislation. As this aspect is particularly relevant to the second issue, I will now discuss how courts have interpreted the scope of their discretionary powers in supervising a *CCAA* reorganization and how Parliament has largely endorsed this interpretation. Indeed, the interpretation courts have given to the *CCAA* helps in understanding how the *CCAA* grew to occupy such a prominent role in Canadian insolvency law.

3.3 Discretionary Power of a Court Supervising a CCAA Reorganization

57 Courts frequently observe that "[t]he *CCAA* is skeletal in nature" and does not "contain a comprehensive code that lays out all that is permitted or barred" (*ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.*, 2008 ONCA 587, 92 O.R. (3d) 513 (Ont. C.A.), at para. 44, *per* Blair J.A.). Accordingly, "[t]he history of CCAA law has been an evolution of judicial interpretation" (*Dylex Ltd., Re* (1995), 31 C.B.R. (3d) 106 (Ont. Gen. Div. [Commercial List])), at para. 10, *per* Farley J.).

58 *CCAA* decisions are often based on discretionary grants of jurisdiction. The incremental exercise of judicial discretion in commercial courts under conditions one practitioner aptly describes as "the hothouse of real-time litigation" has been the primary method by which the *CCAA* has been adapted and has evolved to meet contemporary business and social needs (see Jones, at p. 484).

59 Judicial discretion must of course be exercised in furtherance of the *CCAA's* purposes. The remedial purpose I referred to in the historical overview of the Act is recognized over and over again in the jurisprudence. To cite one early example:

> The legislation is remedial in the purest sense in that it provides a means whereby the devastating social and economic effects of bankruptcy or creditor initiated termination of ongoing business operations can be avoided while a court-supervised attempt to reorganize the financial affairs of the debtor company is made.
>
> (*Nova Metal Products Inc. v. Comiskey (Trustee of)* (1990), 41 O.A.C. 282 (Ont. C.A.), at para. 57, *per* Doherty J.A., dissenting)

60 Judicial decision making under the *CCAA* takes many forms. A court must first of all provide the conditions under which the debtor can attempt to reorganize. This can be achieved by staying enforcement actions by creditors to allow the debtor's business to continue, preserving the *status quo* while the debtor plans the compromise or arrangement to be presented to creditors, and supervising the process and advancing it to the point where it can be determined whether it will succeed (see, e.g., *Hongkong Bank of Canada v. Chef Ready Foods Ltd.* (1990), 51 B.C.L.R. (2d) 84 (B.C. C.A.), at pp. 88-89; *Pacific National Lease Holding Corp., Re* (1992), 19 B.C.A.C. 134 (B.C. C.A. [In Chambers]), at para. 27). In doing so, the court must often be cognizant of the various interests at stake in the reorganization, which can extend beyond those of the debtor and creditors to include employees, directors, shareholders, and even other parties doing business with the insolvent company (see, e.g., *Canadian Airlines Corp., Re*, 2000 ABQB 442, 84 Alta. L.R. (3d) 9 (Alta. Q.B.), at para. 144, *per* Paperny J. (as she then was); *Air Canada, Re* (2003), 42 C.B.R. (4th) 173 (Ont. S.C.J. [Commercial List]), at para. 3; *Air Canada, Re* [2003 CarswellOnt 4967 (Ont. S.C.J. [Commercial List])], 2003 CanLII 49366, at para. 13, *per* Farley J.; Sarra, *Creditor Rights*, at pp. 181-92 and 217-26). In addition, courts must recognize that on occasion the broader public interest will be engaged by aspects of the reorganization and may be a factor against which the decision of whether to allow a particular action will be weighed (see, e.g., *Canadian Red Cross Society / Société Canadienne de la Croix Rouge, Re* (2000), 19 C.B.R. (4th) 158 (Ont. S.C.J.), at para. 2, *per* Blair J. (as he then was); Sarra, *Creditor Rights*, at pp. 195-214).

61 When large companies encounter difficulty, reorganizations become increasingly complex. *CCAA* courts have been called upon to innovate accordingly in exercising their jurisdiction beyond merely staying proceedings against the debtor to allow breathing room for reorganization. They have been asked to sanction measures for which there is no explicit authority in the *CCAA*. Without exhaustively cataloguing the various measures taken under the authority of the *CCAA*, it is useful to refer briefly to a few examples to illustrate the flexibility the statute affords supervising courts.

62 Perhaps the most creative use of *CCAA* authority has been the increasing willingness of courts to authorize post-filing security for debtor in possession financing or super-priority charges on the debtor's assets when necessary for the continuation of the debtor's business during the reorganization (see, e.g., *Skydome Corp., Re* (1998), 16 C.B.R. (4th) 118 (Ont. Gen. Div. [Commercial List]); *United Used Auto & Truck Parts Ltd., Re*, 2000 BCCA 146, 135 B.C.A.C. 96 (B.C. C.A.), aff'g (1999), 12 C.B.R. (4th) 144 (B.C. S.C. [In Chambers]); and generally, J. P. Sarra, *Rescue! The Companies' Creditors Arrangement Act* (2007), at pp. 93-115). The *CCAA* has also been used to release claims against third parties as part of approving a comprehensive plan of arrangement and compromise, even over the objections of some dissenting creditors (see Metcalfe & Mansfield). As well, the appointment of a Monitor to oversee the reorganization was originally a measure taken pursuant to the *CCAA's* supervisory authority; Parliament responded, making the mechanism mandatory by legislative amendment.

63 Judicial innovation during *CCAA* proceedings has not been without controversy. At least two questions it raises are directly relevant to the case at bar: (1) what are the sources of a court's authority during *CCAA* proceedings? (2) what are the limits of this authority?

64 The first question concerns the boundary between a court's statutory authority under the *CCAA* and a court's residual authority under its inherent and equitable jurisdiction when supervising a reorganization. In authorizing measures during *CCAA* proceedings, courts have on occasion purported to rely upon their equitable jurisdiction to advance the purposes of the Act or their inherent jurisdiction to fill gaps in the statute. Recent appellate decisions have counselled against purporting to rely on inherent jurisdiction, holding that the better view is that courts are in most cases simply construing the authority supplied by the *CCAA* itself (see, e.g., *Skeena Cellulose Inc., Re*, 2003 BCCA 344, 13 B.C.L.R. (4th) 236 (B.C. C.A.), at paras. 45-47, *per* Newbury J.A.; *Stelco Inc. (Re)* (2005), 75 O.R. (3d) 5 (Ont. C.A.), paras. 31-33, *per* Blair J.A.).

65 I agree with Justice Georgina R. Jackson and Professor Janis Sarra that the most appropriate approach is a hierarchical one in which courts rely first on an interpretation of the provisions of the *CCAA* text before turning to inherent or equitable jurisdiction to anchor measures taken in a *CCAA* proceeding (see G. R. Jackson and J. Sarra, "Selecting the Judicial Tool to get the Job Done: An Examination of Statutory Interpretation, Discretionary Power and Inherent Jurisdiction in Insolvency Matters", in J. P. Sarra, ed., *Annual Review of Insolvency Law 2007* (2008), 41, at p. 42). The authors conclude that when given an appropriately purposive and liberal interpretation, the *CCAA* will be sufficient in most instances to ground measures necessary to achieve its objectives (p. 94).

66 Having examined the pertinent parts of the *CCAA* and the recent history of the legislation, I accept that in most instances the issuance of an order during *CCAA* proceedings should be considered an exercise in statutory interpretation. Particularly noteworthy in this regard is the expansive interpretation the language of the statute at issue is capable of supporting.

67 The initial grant of authority under the *CCAA* empowered a court "where an application is made under this Act in respect of a company ... on the application of any person interested in the matter ..., subject to this Act, [to] make an order under this section" (*CCAA*, s. 11(1)). The plain language of the statute was very broad.

68 In this regard, though not strictly applicable to the case at bar, I note that Parliament has in recent amendments changed the wording contained in s. 11(1), making explicit the discretionary authority of the court under the *CCAA*. Thus in s. 11 of the *CCAA* as currently enacted, a court may, "subject to the restrictions set out in this Act, ... make any order that it considers appropriate in the circumstances" (S.C. 2005, c. 47, s. 128). Parliament appears to have endorsed the broad reading of *CCAA* authority developed by the jurisprudence.

69 The *CCAA* also explicitly provides for certain orders. Both an order made on an initial application and an order on subsequent applications may stay, restrain, or prohibit existing or new proceedings against the debtor. The burden is on the applicant to satisfy the court that the order is appropriate in the circumstances and that the applicant has been acting in good faith and with due diligence (*CCAA*, ss. 11(3), (4) and (6)).

70 The general language of the *CCAA* should not be read as being restricted by the availability of more specific orders. However, the requirements of appropriateness, good faith, and due diligence are baseline considerations that a court should always bear in mind when exercising *CCAA* authority. Appropriateness under the *CCAA* is assessed by inquiring whether the order sought advances the policy objectives underlying the *CCAA*. The question is whether the order will usefully further efforts to achieve the remedial purpose of the *CCAA* — avoiding the social and economic losses resulting from liquidation of an insolvent company. I would add that appropriateness extends not only to the purpose of the order, but also to the means it employs. Courts should be mindful that chances for successful reorganizations are enhanced where participants achieve common ground and all stakeholders are treated as advantageously and fairly as the circumstances permit.

71 It is well-established that efforts to reorganize under the *CCAA* can be terminated and the stay of proceedings against the debtor lifted if the reorganization is "doomed to failure" (see *Chef Ready*, at p. 88; *Philip's Manufacturing*

Ltd., Re (1992), 9 C.B.R. (3d) 25 (B.C. C.A.), at paras. 6-7). However, when an order is sought that does realistically advance the *CCAA's* purposes, the ability to make it is within the discretion of a *CCAA* court.

72 The preceding discussion assists in determining whether the court had authority under the *CCAA* to continue the stay of proceedings against the Crown once it was apparent that reorganization would fail and bankruptcy was the inevitable next step.

73 In the Court of Appeal, Tysoe J.A. held that no authority existed under the *CCAA* to continue staying the Crown's enforcement of the GST deemed trust once efforts at reorganization had come to an end. The appellant submits that in so holding, Tysoe J.A. failed to consider the underlying purpose of the *CCAA* and give the statute an appropriately purposive and liberal interpretation under which the order was permissible. The Crown submits that Tysoe J.A. correctly held that the mandatory language of the *ETA* gave the court no option but to permit enforcement of the GST deemed trust when lifting the *CCAA* stay to permit the debtor to make an assignment under the *BIA*. Whether the *ETA* has a mandatory effect in the context of a *CCAA* proceeding has already been discussed. I will now address the question of whether the order was authorized by the *CCAA*.

74 It is beyond dispute that the *CCAA* imposes no explicit temporal limitations upon proceedings commenced under the Act that would prohibit ordering a continuation of the stay of the Crown's GST claims while lifting the general stay of proceedings temporarily to allow the debtor to make an assignment in bankruptcy.

75 The question remains whether the order advanced the underlying purpose of the *CCAA*. The Court of Appeal held that it did not because the reorganization efforts had come to an end and the *CCAA* was accordingly spent. I disagree.

76 There is no doubt that had reorganization been commenced under the *BIA* instead of the *CCAA*, the Crown's deemed trust priority for the GST funds would have been lost. Similarly, the Crown does not dispute that under the scheme of distribution in bankruptcy under the *BIA*, the deemed trust for GST ceases to have effect. Thus, after reorganization under the *CCAA* failed, creditors would have had a strong incentive to seek immediate bankruptcy and distribution of the debtor's assets under the *BIA*. In order to conclude that the discretion does not extend to partially lifting the stay in order to allow for an assignment in bankruptcy, one would have to assume a gap between the *CCAA* and the *BIA* proceedings. Brenner C.J.S.C.'s order staying Crown enforcement of the GST claim ensured that creditors would not be disadvantaged by the attempted reorganization under the *CCAA*. The effect of his order was to blunt any impulse of creditors to interfere in an orderly liquidation. His order was thus in furtherance of the *CCAA's* objectives to the extent that it allowed a bridge between the *CCAA* and *BIA* proceedings. This interpretation of the tribunal's discretionary power is buttressed by s. 20 of the *CCAA*. That section provides that the *CCAA* "may be applied together with the provisions of any Act of Parliament... that authorizes or makes provision for the sanction of compromises or arrangements between a company and its shareholders or any class of them", such as the *BIA*. Section 20 clearly indicates the intention of Parliament for the *CCAA* to operate *in tandem* with other insolvency legislation, such as the *BIA*.

77 The *CCAA* creates conditions for preserving the *status quo* while attempts are made to find common ground amongst stakeholders for a reorganization that is fair to all. Because the alternative to reorganization is often bankruptcy, participants will measure the impact of a reorganization against the position they would enjoy in liquidation. In the case at bar, the order fostered a harmonious transition between reorganization and liquidation while meeting the objective of a single collective proceeding that is common to both statutes.

78 Tysoe J.A. therefore erred in my view by treating the *CCAA* and the *BIA* as distinct regimes subject to a temporal gap between the two, rather than as forming part of an integrated body of insolvency law. Parliament's decision to maintain two statutory schemes for reorganization, the *BIA* and the *CCAA*, reflects the reality that reorganizations of differing complexity require different legal mechanisms. By contrast, only one statutory scheme has been found to be needed to liquidate a bankrupt debtor's estate. The transition from the *CCAA* to the *BIA* may require the partial lifting of a stay of proceedings under the *CCAA* to allow commencement of the *BIA* proceedings. However, as Laskin J.A. for the Ontario Court of Appeal noted in a similar competition between secured creditors and the Ontario Superintendent

of Financial Services seeking to enforce a deemed trust, "[t]he two statutes are related" and no "gap" exists between the two statutes which would allow the enforcement of property interests at the conclusion of *CCAA* proceedings that would be lost in bankruptcy *Ivaco Inc. (Re)* (2006), 83 O.R. (3d) 108 (Ont. C.A.), at paras. 62-63).

79 The Crown's priority in claims pursuant to source deductions deemed trusts does not undermine this conclusion. Source deductions deemed trusts survive under both the *CCAA* and the *BIA*. Accordingly, creditors' incentives to prefer one Act over another will not be affected. While a court has a broad discretion to stay source deductions deemed trusts in the *CCAA* context, this discretion is nevertheless subject to specific limitations applicable only to source deductions deemed trusts (*CCAA*, s. 11.4). Thus, if *CCAA* reorganization fails (e.g., either the creditors or the court refuse a proposed reorganization), the Crown can immediately assert its claim in unremitted source deductions. But this should not be understood to affect a seamless transition into bankruptcy or create any "gap" between the *CCAA* and the *BIA* for the simple reason that, regardless of what statute the reorganization had been commenced under, creditors' claims in both instances would have been subject to the priority of the Crown's source deductions deemed trust.

80 Source deductions deemed trusts aside, the comprehensive and exhaustive mechanism under the *BIA* must control the distribution of the debtor's assets once liquidation is inevitable. Indeed, an orderly transition to liquidation is mandatory under the *BIA* where a proposal is rejected by creditors. The *CCAA* is silent on the transition into liquidation but the breadth of the court's discretion under the Act is sufficient to construct a bridge to liquidation under the *BIA*. The court must do so in a manner that does not subvert the scheme of distribution under the *BIA*. Transition to liquidation requires partially lifting the *CCAA* stay to commence proceedings under the *BIA*. This necessary partial lifting of the stay should not trigger a race to the courthouse in an effort to obtain priority unavailable under the *BIA*.

81 I therefore conclude that Brenner C.J.S.C. had the authority under the *CCAA* to lift the stay to allow entry into liquidation.

3.4 Express Trust

82 The last issue in this case is whether Brenner C.J.S.C. created an express trust in favour of the Crown when he ordered on April 29, 2008, that proceeds from the sale of LeRoy Trucking's assets equal to the amount of unremitted GST be held back in the Monitor's trust account until the results of the reorganization were known. Tysoe J.A. in the Court of Appeal concluded as an alternative ground for allowing the Crown's appeal that it was the beneficiary of an express trust. I disagree.

83 Creation of an express trust requires the presence of three certainties: intention, subject matter, and object. Express or "true trusts" arise from the acts and intentions of the settlor and are distinguishable from other trusts arising by operation of law (see D. W. M. Waters, M. R. Gillen and L. D. Smith, eds., *Waters' Law of Trusts in Canada* (3rd ed. 2005), at pp. 28-29 especially fn. 42).

84 Here, there is no certainty to the object (i.e. the beneficiary) inferrable from the court's order of April 29, 2008, sufficient to support an express trust.

85 At the time of the order, there was a dispute between Century Services and the Crown over part of the proceeds from the sale of the debtor's assets. The court's solution was to accept LeRoy Trucking's proposal to segregate those monies until that dispute could be resolved. Thus there was no certainty that the Crown would actually be the beneficiary, or object, of the trust.

86 The fact that the location chosen to segregate those monies was the Monitor's trust account has no independent effect such that it would overcome the lack of a clear beneficiary. In any event, under the interpretation of *CCAA* s. 18.3(1) established above, no such priority dispute would even arise because the Crown's deemed trust priority over GST claims would be lost under the *CCAA* and the Crown would rank as an unsecured creditor for this amount. However, Brenner C.J.S.C. may well have been proceeding on the basis that, in accordance with *Ottawa Senators*, the Crown's GST claim would remain effective if reorganization was successful, which would not be the case if transition to the

liquidation process of the *BIA* was allowed. An amount equivalent to that claim would accordingly be set aside pending the outcome of reorganization.

87 Thus, uncertainty surrounding the outcome of the *CCAA* restructuring eliminates the existence of any certainty to permanently vest in the Crown a beneficial interest in the funds. That much is clear from the oral reasons of Brenner C.J.S.C. on April 29, 2008, when he said: "Given the fact that [*CCAA* proceedings] are known to fail and filings in bankruptcy result, it seems to me that maintaining the status quo in the case at bar supports the proposal to have the monitor hold these funds in trust." Exactly who might take the money in the final result was therefore evidently in doubt. Brenner C.J.S.C.'s subsequent order of September 3, 2008, denying the Crown's application to enforce the trust once it was clear that bankruptcy was inevitable, confirms the absence of a clear beneficiary required to ground an express trust.

4. Conclusion

88 I conclude that Brenner C.J.S.C. had the discretion under the *CCAA* to continue the stay of the Crown's claim for enforcement of the GST deemed trust while otherwise lifting it to permit LeRoy Trucking to make an assignment in bankruptcy. My conclusion that s. 18.3(1) of the *CCAA* nullified the GST deemed trust while proceedings under that Act were pending confirms that the discretionary jurisdiction under s. 11 utilized by the court was not limited by the Crown's asserted GST priority, because there is no such priority under the *CCAA*.

89 For these reasons, I would allow the appeal and declare that the $305,202.30 collected by LeRoy Trucking in respect of GST but not yet remitted to the Receiver General of Canada is not subject to deemed trust or priority in favour of the Crown. Nor is this amount subject to an express trust. Costs are awarded for this appeal and the appeal in the court below.

Fish J. (concurring):

I

90 I am in general agreement with the reasons of Justice Deschamps and would dispose of the appeal as she suggests.

91 More particularly, I share my colleague's interpretation of the scope of the judge's discretion under s. 11 of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"). And I share my colleague's conclusion that Brenner C.J.S.C. did not create an express trust in favour of the Crown when he segregated GST funds into the Monitor's trust account (2008 BCSC 1805, [2008] G.S.T.C. 221 (B.C. S.C. [In Chambers])).

92 I nonetheless feel bound to add brief reasons of my own regarding the interaction between the *CCAA* and the *Excise Tax Act*, R.S.C. 1985, c. E-15 ("*ETA*").

93 In upholding deemed trusts created by the *ETA* notwithstanding insolvency proceedings, *Ottawa Senators Hockey Club Corp. (Re)* (2005), 73 O.R. (3d) 737, [2005] G.S.T.C. 1 (Ont. C.A.), and its progeny have been unduly protective of Crown interests which Parliament itself has chosen to subordinate to competing prioritized claims. In my respectful view, a clearly marked departure from that jurisprudential approach is warranted in this case.

94 Justice Deschamps develops important historical and policy reasons in support of this position and I have nothing to add in that regard. I do wish, however, to explain why a comparative analysis of related statutory provisions adds support to our shared conclusion.

95 Parliament has in recent years given detailed consideration to the Canadian insolvency scheme. It has declined to amend the provisions at issue in this case. Ours is not to wonder why, but rather to treat Parliament's preservation of the relevant provisions as a deliberate exercise of the legislative discretion that is Parliament's alone. With respect, I reject any suggestion that we should instead characterize the apparent conflict between s. 18.3(1) (now s. 37(1)) of the *CCAA* and s. 222 of the *ETA* as a drafting anomaly or statutory lacuna properly subject to judicial correction or repair.

II

96 In the context of the Canadian insolvency regime, a deemed trust will be found to exist only where two complementary elements co-exist: first, a statutory provision *creating* the trust; and second, a *CCAA* or *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*") provision *confirming* — or explicitly preserving — its effective operation.

97 This interpretation is reflected in three federal statutes. Each contains a deemed trust provision framed in terms strikingly similar to the wording of s. 222 of the *ETA*.

98 The first is the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) ("*ITA*") where s. 227(4) *creates* a deemed trust:

> **227 (4) Trust for moneys deducted** — Every person who deducts or withholds an amount under this Act is deemed, notwithstanding any security interest (as defined in subsection 224(1.3)) in the amount so deducted or withheld, to hold the amount separate and apart from the property of the person and from property held by any secured creditor (as defined in subsection 224(1.3)) of that person that but for the security interest would be property of the person, in trust for Her Majesty and for payment to Her Majesty in the manner and at the time provided under this Act. [Here and below, the emphasis is of course my own.]

99 In the next subsection, Parliament has taken care to make clear that this trust is unaffected by federal or provincial legislation to the contrary:

> **(4.1) Extension of trust** — Notwithstanding any other provision of this Act, the *Bankruptcy and Insolvency Act* (except sections 81.1 and 81.2 of that Act), any other enactment of Canada, any enactment of a province or any other law, where at any time an amount deemed by subsection 227(4) to be held by a person in trust for Her Majesty is not paid to Her Majesty in the manner and at the time provided under this Act, property of the person ... equal in value to the amount so deemed to be held in trust is deemed
>
> > (a) to be held, from the time the amount was deducted or withheld by the person, separate and apart from the property of the person, in trust for Her Majesty whether or not the property is subject to such a security interest, ...
> >
> > ...
>
> ... and the proceeds of such property shall be paid to the Receiver General in priority to all such security interests.

100 The continued operation of this deemed trust is expressly *confirmed* in s. 18.3 of the *CCAA*:

> **18.3** (1) Subject to subsection (2), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as being held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.
>
> (2) Subsection (1) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act*....

101 The operation of the *ITA* deemed trust is also confirmed in s. 67 of the *BIA*:

> **67** (2) Subject to subsection (3), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a bankrupt shall not be regarded as held in trust for Her Majesty for the purpose of paragraph (1)(*a*) unless it would be so regarded in the absence of that statutory provision.

> (3) Subsection (2) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act*....

102 Thus, Parliament has first *created* and then *confirmed the continued operation of* the Crown's *ITA* deemed trust under *both* the *CCAA* and the *BIA* regimes.

103 The second federal statute for which this scheme holds true is the *Canada Pension Plan*, R.S.C. 1985, c. C-8 ("*CPP*"). At s. 23, Parliament creates a deemed trust in favour of the Crown and specifies that it exists despite all contrary provisions in any other Canadian statute. Finally, and in almost identical terms, the *Employment Insurance Act*, S.C. 1996, c. 23 ("*EIA*"), creates a deemed trust in favour of the Crown: see ss. 86(2) and (2.1).

104 As we have seen, the survival of the deemed trusts created under these provisions of the *ITA*, the *CPP* and the *EIA* is confirmed in s. 18.3(2) the *CCAA* and in s. 67(3) the *BIA*. In all three cases, Parliament's intent to enforce the Crown's deemed trust through insolvency proceedings is expressed in clear and unmistakable terms.

105 The same is not true with regard to the deemed trust created under the *ETA*. Although Parliament creates a deemed trust in favour of the Crown to hold unremitted GST monies, and although it purports to maintain this trust notwithstanding any contrary federal or provincial legislation, it does not *confirm* the trust — or expressly provide for its continued operation — in either the *BIA* or the *CCAA*. The second of the two mandatory elements I have mentioned is thus absent reflecting Parliament's intention to allow the deemed trust to lapse with the commencement of insolvency proceedings.

106 The language of the relevant *ETA* provisions is identical in substance to that of the *ITA*, *CPP*, and *EIA* provisions:

> **222. (1) [Deemed] Trust for amounts collected** — Subject to subsection (1.1), every person who collects an amount as or on account of tax under Division II is deemed, for all purposes and despite any security interest in the amount, to hold the amount in trust for Her Majesty in right of Canada, separate and apart from the property of the person and from property held by any secured creditor of the person that, but for a security interest, would be property of the person, until the amount is remitted to the Receiver General or withdrawn under subsection (2).
>
> ...
>
> **(3) Extension of trust** — Despite any other provision of this Act (except subsection (4)), any other enactment of Canada (except the *Bankruptcy and Insolvency Act*), any enactment of a province or any other law, if at any time an amount deemed by subsection (1) to be held by a person in trust for Her Majesty is not remitted to the Receiver General or withdrawn in the manner and at the time provided under this Part, property of the person and property held by any secured creditor of the person that, but for a security interest, would be property of the person, equal in value to the amount so deemed to be held in trust, is deemed
>
> > (a) to be held, from the time the amount was collected by the person, in trust for Her Majesty, separate and apart from the property of the person, whether or not the property is subject to a security interest, ...
> >
> > ...
>
> ... and the proceeds of the property shall be paid to the Receiver General in priority to all security interests.

107 Yet no provision of the *CCAA* provides for the continuation of this deemed trust after the *CCAA* is brought into play.

108 In short, Parliament has imposed *two* explicit conditions, or "building blocks", for survival under the *CCAA* of deemed trusts created by the *ITA*, *CPP*, and *EIA*. Had Parliament intended to likewise preserve under the *CCAA*

deemed trusts created by the *ETA*, it would have included in the *CCAA* the sort of confirmatory provision that explicitly preserves other deemed trusts.

109 With respect, unlike Tysoe J.A., I do not find it "inconceivable that Parliament would specifically identify the *BIA* as an exception when enacting the current version of s. 222(3) of the *ETA* without considering the *CCAA* as a possible second exception" (2009 BCCA 205, 98 B.C.L.R. (4th) 242, [2009] G.S.T.C. 79 (B.C. C.A.), at para. 37). *All* of the deemed trust provisions excerpted above make explicit reference to the *BIA*. Section 222 of the *ETA* does not break the pattern. Given the near-identical wording of the four deemed trust provisions, it would have been surprising indeed had Parliament not addressed the *BIA* at all in the *ETA*.

110 Parliament's evident intent was to render GST deemed trusts inoperative upon the institution of insolvency proceedings. Accordingly, s. 222 mentions the *BIA* so as to *exclude* it from its ambit — rather than to *include* it, as do the *ITA*, the *CPP*, and the *EIA*.

111 Conversely, I note that *none* of these statutes mentions the *CCAA* expressly. Their specific reference to the *BIA* has no bearing on their interaction with the *CCAA*. Again, it is the confirmatory provisions *in the insolvency statutes* that determine whether a given deemed trust will subsist during insolvency proceedings.

112 Finally, I believe that chambers judges should not segregate GST monies into the Monitor's trust account during *CCAA* proceedings, as was done in this case. The result of Justice Deschamps's reasoning is that GST claims become unsecured under the *CCAA*. Parliament has deliberately chosen to nullify certain Crown super-priorities during insolvency; this is one such instance.

III

113 For these reasons, like Justice Deschamps, I would allow the appeal with costs in this Court and in the courts below and order that the $305,202.30 collected by LeRoy Trucking in respect of GST but not yet remitted to the Receiver General of Canada be subject to no deemed trust or priority in favour of the Crown.

Abella J. (dissenting):

114 The central issue in this appeal is whether s. 222 of the *Excise Tax Act*, R.S.C. 1985, c. E-15 ("*EIA*"), and specifically s. 222(3), gives priority during *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"), proceedings to the Crown's deemed trust in unremitted GST. I agree with Tysoe J.A. that it does. It follows, in my respectful view, that a court's discretion under s. 11 of the *CCAA* is circumscribed accordingly.

115 Section 11 [1] of the *CCAA* stated:

> **11.** (1) Notwithstanding anything in the *Bankruptcy and Insolvency Act* or the *Winding-up Act*, where an application is made under this Act in respect of a company, the court, on the application of any person interested in the matter, may, subject to this Act, on notice to any other person or without notice as it may see fit, make an order under this section.

To decide the scope of the court's discretion under s. 11, it is necessary to first determine the priority issue. Section 222(3), the provision of the *ETA* at issue in this case, states:

> **222 (3) Extension of trust** — Despite any other provision of this Act (except subsection (4)), any other enactment of Canada (except the *Bankruptcy and Insolvency Act*), any enactment of a province or any other law, if at any time an amount deemed by subsection (1) to be held by a person in trust for Her Majesty is not remitted to the Receiver General or withdrawn in the manner and at the time provided under this Part, property of the person and property held by any secured creditor of the person that, but for a security interest, would be property of the person, equal in value to the amount so deemed to be held in trust, is deemed

> (a) to be held, from the time the amount was collected by the person, in trust for Her Majesty, separate and apart from the property of the person, whether or not the property is subject to a security interest, and
>
> (b) to form no part of the estate or property of the person from the time the amount was collected, whether or not the property has in fact been kept separate and apart from the estate or property of the person and whether or not the property is subject to a security interest
>
> and is property beneficially owned by Her Majesty in right of Canada despite any security interest in the property or in the proceeds thereof and the proceeds of the property shall be paid to the Receiver General in priority to all security interests.

116 Century Services argued that the *CCAA's* general override provision, s. 18.3(1), prevailed, and that the deeming provisions in s. 222 of the *ETA* were, accordingly, inapplicable during *CCAA* proceedings. Section 18.3(1) states:

> **18.3** (1) ... [N]otwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

117 As MacPherson J.A. correctly observed in *Ottawa Senators Hockey Club Corp. (Re)* (2005), 73 O.R. (3d) 737, [2005] G.S.T.C. 1 (Ont. C.A.), s. 222(3) of the *ETA* is in "clear conflict" with s. 18.3(1) of the *CCAA* (para. 31). Resolving the conflict between the two provisions is, essentially, what seems to me to be a relatively uncomplicated exercise in statutory interpretation: does the language reflect a clear legislative intention? In my view it does. The deemed trust provision, s. 222(3) of the *ETA*, has unambiguous language stating that it operates notwithstanding any law except the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*").

118 By expressly excluding only one statute from its legislative grasp, and by unequivocally stating that it applies despite any other law anywhere in Canada *except* the *BIA*, s. 222(3) has defined its boundaries in the clearest possible terms. I am in complete agreement with the following comments of MacPherson J.A. in *Ottawa Senators*:

> The legislative intent of s. 222(3) of the *ETA* is clear. If there is a conflict with "any other enactment of Canada (except the *Bankruptcy and Insolvency Act*)", s. 222(3) prevails. In these words Parliament did two things: it decided that s. 222(3) should trump all other federal laws and, importantly, it addressed the topic of exceptions to its trumping decision and identified a single exception, the *Bankruptcy and Insolvency Act* .... The *BIA* and the *CCAA* are closely related federal statutes. I cannot conceive that Parliament would specifically identify the *BIA* as an exception, but accidentally fail to consider the *CCAA* as a possible second exception. In my view, the omission of the *CCAA* from s. 222(3) of the *ETA* was almost certainly a considered omission. [para. 43]

119 MacPherson J.A.'s view that the failure to exempt the *CCAA* from the operation of the *ETA* is a reflection of a clear legislative intention, is borne out by how the *CCAA* was subsequently changed after s. 18.3(1) was enacted in 1997. In 2000, when s. 222(3) of the *ETA* came into force, amendments were also introduced to the *CCAA*. Section 18.3(1) was not amended.

120 The failure to amend s. 18.3(1) is notable because its effect was to protect the legislative *status quo*, notwithstanding repeated requests from various constituencies that s. 18.3(1) be amended to make the priorities in the *CCAA* consistent with those in the *BIA*. In 2002, for example, when Industry Canada conducted a review of the *BIA* and the *CCAA*, the Insolvency Institute of Canada and the Canadian Association of Insolvency and Restructuring Professionals recommended that the priority regime under the *BIA* be extended to the *CCAA* (Joint Task Force on Business Insolvency Law Reform, *Report* (March 15, 2002), Sch. B, proposal 71, at pp. 37-38). The same recommendations were made by the Standing Senate Committee on Banking, Trade and Commerce in its 2003 report, *Debtors and Creditors Sharing the Burden: A Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act*; by the Legislative Review Task Force (Commercial) of the Insolvency Institute of Canada and the Canadian Association of Insolvency and

Restructuring Professionals in its 2005 *Report on the Commercial Provisions of Bill C-55*; and in 2007 by the Insolvency Institute of Canada in a submission to the Standing Senate Committee on Banking, Trade and Commerce commenting on reforms then under consideration.

121 Yet the *BIA* remains the only exempted statute under s. 222(3) of the *ETA*. Even after the 2005 decision in *Ottawa Senators* which confirmed that the *ETA* took precedence over the *CCAA*, there was no responsive legislative revision. I see this lack of response as relevant in this case, as it was in *R. v. Tele-Mobile Co.*, 2008 SCC 12, [2008] 1 S.C.R. 305 (S.C.C.), where this Court stated:

> While it cannot be said that legislative silence is necessarily determinative of legislative intention, in this case the silence is Parliament's answer to the consistent urging of Telus and other affected businesses and organizations that there be express language in the legislation to ensure that businesses can be reimbursed for the reasonable costs of complying with evidence-gathering orders. I see the legislative history as reflecting Parliament's intention that compensation not be paid for compliance with production orders. [para. 42]

122 All this leads to a clear inference of a deliberate legislative choice to protect the deemed trust in s. 222(3) from the reach of s. 18.3(1) of the *CCAA*.

123 Nor do I see any "policy" justification for interfering, through interpretation, with this clarity of legislative intention. I can do no better by way of explaining why I think the policy argument cannot succeed in this case, than to repeat the words of Tysoe J.A. who said:

> I do not dispute that there are valid policy reasons for encouraging insolvent companies to attempt to restructure their affairs so that their business can continue with as little disruption to employees and other stakeholders as possible. It is appropriate for the courts to take such policy considerations into account, but only if it is in connection with a matter that has not been considered by Parliament. Here, Parliament must be taken to have weighed policy considerations when it enacted the amendments to the *CCAA* and *ETA* described above. As Mr. Justice MacPherson observed at para. 43 of *Ottawa Senators*, it is inconceivable that Parliament would specifically identify the *BIA* as an exception when enacting the current version of s. 222(3) of the *ETA* without considering the *CCAA* as a possible second exception. I also make the observation that the 1992 set of amendments to the *BIA* enabled proposals to be binding on secured creditors and, while there is more flexibility under the *CCAA*, it is possible for an insolvent company to attempt to restructure under the auspices of the *BIA*. [para. 37]

124 Despite my view that the clarity of the language in s. 222(3) is dispositive, it is also my view that even the application of other principles of interpretation reinforces this conclusion. In their submissions, the parties raised the following as being particularly relevant: the Crown relied on the principle that the statute which is "later in time" prevails; and Century Services based its argument on the principle that the general provision gives way to the specific (*generalia specialibus non derogant*).

125 The "later in time" principle gives priority to a more recent statute, based on the theory that the legislature is presumed to be aware of the content of existing legislation. If a new enactment is inconsistent with a prior one, therefore, the legislature is presumed to have intended to derogate from the earlier provisions (Ruth Sullivan, *Sullivan on the Construction of Statutes* (5th ed. 2008), at pp. 346-47; Pierre-André Côté, *The Interpretation of Legislation in Canada* (3rd ed. 2000), at p. 358).

126 The exception to this presumptive displacement of pre-existing inconsistent legislation, is the *generalia specialibus non derogant* principle that "[a] more recent, general provision will not be construed as affecting an earlier, special provision" (Côté, at p. 359). Like a Russian Doll, there is also an exception within this exception, namely, that an earlier, specific provision may in fact be "overruled" by a subsequent general statute if the legislature indicates, through its language, an intention that the general provision prevails (*Doré c. Verdun (Municipalité)*, [1997] 2 S.C.R. 862 (S.C.C.)).

127 The primary purpose of these interpretive principles is to assist in the performance of the task of determining the intention of the legislature. This was confirmed by MacPherson J.A. in *Ottawa Senators*, at para. 42:

> [T]he overarching rule of statutory interpretation is that statutory provisions should be interpreted to give effect to the intention of the legislature in enacting the law. This primary rule takes precedence over all maxims or canons or aids relating to statutory interpretation, including the maxim that the specific prevails over the general (*generalia specialibus non derogant*). As expressed by Hudson J. in *Canada v. Williams*, [1944] S.C.R. 226, ... at p. 239 ...:
>
> > The maxim *generalia specialibus non derogant* is relied on as a rule which should dispose of the question, but the maxim is not a rule of law but a rule of construction and bows to the intention of the legislature, if such intention can reasonably be gathered from all of the relevant legislation.

(See also Côté, at p. 358, and Pierre-Andre Côté, with the collaboration of S. Beaulac and M. Devinat, *Interprétation des lois* (4th ed. 2009), at para. 1335.)

128 I accept the Crown's argument that the "later in time" principle is conclusive in this case. Since s. 222(3) of the *ETA* was enacted in 2000 and s. 18.3(1) of the *CCAA* was introduced in 1997, s. 222(3) is, on its face, the later provision. This chronological victory can be displaced, as Century Services argues, if it is shown that the more recent provision, s. 222(3) of the *ETA*, is a general one, in which case the earlier, specific provision, s. 18.3(1), prevails (*generalia specialibus non derogant)*. But, as previously explained, the prior specific provision does not take precedence if the subsequent general provision appears to "overrule" it. This, it seems to me, is precisely what s. 222(3) achieves through the use of language stating that it prevails despite any law of Canada, of a province, or "any other law" *other than the BIA*. Section 18.3(1) of the *CCAA*, is thereby rendered inoperative for purposes of s. 222(3).

129 It is true that when the *CCAA* was amended in 2005, [2] s. 18.3(1) was re-enacted as s. 37(1) (S.C. 2005, c. 47, s. 131). Deschamps J. suggests that this makes s. 37(1) the new, "later in time" provision. With respect, her observation is refuted by the operation of s. 44(f) of the *Interpretation Act*, R.S.C. 1985, c. I-21, which expressly deals with the (non) effect of re-enacting, without significant substantive changes, a repealed provision (see *Canada (Attorney General) v. Canada (Public Service Staff Relations Board)*, [1977] 2 F.C. 663 (Fed. C.A.), dealing with the predecessor provision to s. 44(f)). It directs that new enactments not be construed as "new law" unless they differ in substance from the repealed provision:

> **44.** Where an enactment, in this section called the "former enactment", is repealed and another enactment, in this section called the "new enactment", is substituted therefor,
>
> ...
>
> (f) except to the extent that the provisions of the new enactment are not in substance the same as those of the former enactment, the new enactment shall not be held to operate as new law, but shall be construed and have effect as a consolidation and as declaratory of the law as contained in the former enactment;

Section 2 of the *Interpretation Act* defines an enactment as "an Act or regulation or *any portion of an Act or regulation*".

130 Section 37(1) of the current *CCAA* is almost identical to s. 18.3(1). These provisions are set out for ease of comparison, with the differences between them underlined:

> **37.**(1) Subject to subsection (2), despite any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as being held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.
>
> **18.3** (1) Subject to subsection (2), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

131 The application of s. 44(*f*) of the *Interpretation Act* simply confirms the government's clearly expressed intent, found in Industry Canada's clause-by-clause review of Bill C-55, where s. 37(1) was identified as "a technical amendment to reorder the provisions of this Act". During second reading, the Hon. Bill Rompkey, then the Deputy Leader of the Government in the Senate, confirmed that s. 37(1) represented only a technical change:

> On a technical note relating to the treatment of deemed trusts for taxes, the bill [*sic*] makes no changes to the underlying policy intent, despite the fact that in the case of a restructuring under the CCAA, sections of the act [*sic*] were repealed and substituted with renumbered versions due to the extensive reworking of the CCAA.
>
> (*Debates of the Senate*, vol. 142, 1st Sess., 38th Parl., November 23, 2005, at p. 2147)

132 Had the substance of s. 18.3(1) altered in any material way when it was replaced by s. 37(1), I would share Deschamps J.'s view that it should be considered a new provision. But since s. 18.3(1) and s. 37(1) are the same in substance, the transformation of s. 18.3(1) into s. 37(1) has no effect on the interpretive queue, and s. 222(3) of the *ETA* remains the "later in time" provision (Sullivan, at p. 347).

133 This means that the deemed trust provision in s. 222(3) of the *ETA* takes precedence over s. 18.3(1) during *CCAA* proceedings. The question then is how that priority affects the discretion of a court under s. 11 of the *CCAA*.

134 While s. 11 gives a court discretion to make orders notwithstanding the *BIA* and the *Winding-up Act*, R.S.C. 1985, c. W-11, that discretion is not liberated from the operation of any other federal statute. Any exercise of discretion is therefore circumscribed by whatever limits are imposed by statutes *other* than the *BIA* and the *Winding-up Act*. That includes the *ETA*. The chambers judge in this case was, therefore, required to respect the priority regime set out in s. 222(3) of the *ETA*. Neither s. 18.3(1) nor s. 11 of the *CCAA* gave him the authority to ignore it. He could not, as a result, deny the Crown's request for payment of the GST funds during the *CCAA* proceedings.

135 Given this conclusion, it is unnecessary to consider whether there was an express trust.

136 I would dismiss the appeal.

Appeal allowed.

Pourvoi accueilli.

Appendix

***Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (as at December 13, 2007)**

11. (1) Powers of court — Notwithstanding anything in the *Bankruptcy and Insolvency Act* or the *Winding-up Act*, where an application is made under this Act in respect of a company, the court, on the application of any person interested in the matter, may, subject to this Act, on notice to any other person or without notice as it may see fit, make an order under this section.

...

(3) Initial application court orders — A court may, on an initial application in respect of a company, make an order on such terms as it may impose, effective for such period as the court deems necessary not exceeding thirty days,

(a) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under an Act referred to in subsection (i);

(b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(c) prohibiting, until otherwise ordered by the court, the commencement of or proceeding with any other action, suit or proceeding against the company.

(4) Other than initial application court orders — A court may, on an application in respect of a company other than an initial application, make an order on such terms as it may impose,

(a) staying, until otherwise ordered by the court, for such period as the court deems necessary, all proceedings taken or that might be taken in respect of the company under an Act referred to in subsection (1);

(b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(c) prohibiting, until otherwise ordered by the court, the commencement of or proceeding with any other action, suit or proceeding against the company.

...

(6) Burden of proof on application — The court shall not make an order under subsection (3) or (4) unless

(a) the applicant satisfies the court that circumstances exist that make such an order appropriate; and

(b) in the case of an order under subsection (4), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

11.4 (1) Her Majesty affected — An order made under section 11 may provide that

(a) Her Majesty in right of Canada may not exercise rights under subsection 224(1.2) of the *Income Tax Act* or any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, in respect of the company if the company is a tax debtor under that subsection or provision, for such period as the court considers appropriate but ending not later than

(i) the expiration of the order,

(ii) the refusal of a proposed compromise by the creditors or the court,

(iii) six months following the court sanction of a compromise or arrangement,

(iv) the default by the company on any term of a compromise or arrangement, or

(v) the performance of a compromise or arrangement in respect of the company; and\

(b) Her Majesty in right of a province may not exercise rights under any provision of provincial legislation in respect of the company where the company is a debtor under that legislation and the provision has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

for such period as the court considers appropriate but ending not later than the occurrence or time referred to in whichever of subparagraphs (*a*)(i) to (v) may apply.

(2) When order ceases to be in effect — An order referred to in subsection (1) ceases to be in effect if

(a) the company defaults on payment of any amount that becomes due to Her Majesty after the order is made and could be subject to a demand under

(i) subsection 224(1.2) of the *Income Tax Act*,

(ii) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(iii) under any provision of provincial legislation that has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(A) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(B) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection; or

(b) any other creditor is or becomes entitled to realize a security on any property that could be claimed by Her Majesty in exercising rights under

(i) subsection 224(1.2) of the *Income Tax Act*,

(ii) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(iii) any provision of provincial legislation that has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(A) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(B) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection.

(3) Operation of similar legislation — An order made under section 11, other than an order referred to in subsection (1) of this section, does not affect the operation of

(a) subsections 224(1.2) and (1.3) of the *Income Tax Act*,

(b) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(c) any provision of provincial legislation that has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

and for the purpose of paragraph (*c*), the provision of provincial legislation is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as subsection 224(1.2) of the *Income Tax Act* in respect of a sum referred to in subparagraph (*c*)(i), or as subsection 23(2) of the *Canada Pension Plan* in respect of a sum referred to in subparagraph (*c*)(ii), and in respect of any related interest, penalties or other amounts.

18.3 (1) Deemed trusts — Subject to subsection (2), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

(2) Exceptions — Subsection (1) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* (each of which is in this subsection referred to as a "federal provision") nor in respect of amounts deemed to be held in trust under any law of a province that creates a deemed trust the sole purpose of which is to ensure remittance to Her Majesty in right of the province of amounts deducted or withheld under a law of the province where

(a) that law of the province imposes a tax similar in nature to the tax imposed under the *Income Tax Act* and the amounts deducted or withheld under that law of the province are of the same nature as the amounts referred to in subsection 227(4) or (4.1) of the *Income Tax Act*, or

(b) the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan*, that law of the province establishes a "provincial pension plan" as defined in that subsection and the amounts deducted or withheld under that law of the province are of the same nature as amounts referred to in subsection 23(3) or (4) of the *Canada Pension Plan*,

and for the purpose of this subsection, any provision of a law of a province that creates a deemed trust is, notwithstanding any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as the corresponding federal provision.

18.4 (1) Status of Crown claims — In relation to a proceeding under this Act, all claims, including secured claims, of Her Majesty in right of Canada or a province or any body under an enactment respecting workers' compensation, in this section and in section 18.5 called a "workers' compensation body", rank as unsecured claims.

...

(3) Operation of similar legislation — Subsection (1) does not affect the operation of

(a) subsections 224(1.2) and (1.3) of the *Income Tax Act*,

(b) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(c) any provision of provincial legislation that has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

and for the purpose of paragraph (*c*), the provision of provincial legislation is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as subsection 224(1.2) of the *Income Tax Act* in respect of a sum referred to in subparagraph (*c*)(i), or as subsection 23(2) of the *Canada Pension Plan* in respect of a sum referred to in subparagraph (*c*)(ii), and in respect of any related interest, penalties or other amounts.

...

20. [Act to be applied conjointly with other Acts] — The provisions of this Act may be applied together with the provisions of any Act of Parliament or of the legislature of any province, that authorizes or makes provision for the sanction of compromises or arrangements between a company and its shareholders or any class of them.

***Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (as at September 18, 2009)**

11. General power of court — Despite anything in the *Bankruptcy and Insolvency Act* or the *Winding-up and Restructuring Act*, if an application is made under this Act in respect of a debtor company, the court, on the application of any person interested in the matter, may, subject to the restrictions set out in this Act, on notice to any other person or without notice as it may see fit, make any order that it considers appropriate in the circumstances.

...

11.02 (1) Stays, etc. — initial application — A court may, on an initial application in respect of a debtor company, make an order on any terms that it may impose, effective for the period that the court considers necessary, which period may not be more than 30 days,

(a) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under the *Bankruptcy and Insolvency Act* or the *Winding-up and Restructuring Act*;

(b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(c) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.

(2) Stays, etc. — other than initial application — A court may, on an application in respect of a debtor company other than an initial application, make an order, on any terms that it may impose,

(a) staying, until otherwise ordered by the court, for any period that the court considers necessary, all proceedings taken or that might be taken in respect of the company under an Act referred to in paragraph (1)(*a*);

(b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(c) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.

(3) Burden of proof on application — The court shall not make the order unless

(a) the applicant satisfies the court that circumstances exist that make the order appropriate; and

(b) in the case of an order under subsection (2), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

...

11.09 (1) Stay — Her Majesty — An order made under section 11.02 may provide that

(a) Her Majesty in right of Canada may not exercise rights under subsection 224(1.2) of the *Income Tax Act* or any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, in respect of the company if the company is a tax debtor under that subsection or provision, for the period that the court considers appropriate but ending not later than

(i) the expiry of the order,

(ii) the refusal of a proposed compromise by the creditors or the court,

(iii) six months following the court sanction of a compromise or an arrangement,

(iv) the default by the company on any term of a compromise or an arrangement, or

(v) the performance of a compromise or an arrangement in respect of the company; and

(b) Her Majesty in right of a province may not exercise rights under any provision of provincial legislation in respect of the company if the company is a debtor under that legislation and the provision has a purpose similar to subsection 224(1.2) of the *Income Tax Act*, or refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, and the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

for the period that the court considers appropriate but ending not later than the occurrence or time referred to in whichever of subparagraphs (*a*)(i) to (v) that may apply.

(2) When order ceases to be in effect — The portions of an order made under section 11.02 that affect the exercise of rights of Her Majesty referred to in paragraph (1)(*a*) or (*b*) cease to be in effect if

(a) the company defaults on the payment of any amount that becomes due to Her Majesty after the order is made and could be subject to a demand under

(i) subsection 224(1.2) of the *Income Tax Act*,

(ii) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(iii) any provision of provincial legislation that has a purpose similar to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, and the sum

(A) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(B) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection; or

(b) any other creditor is or becomes entitled to realize a security on any property that could be claimed by Her Majesty in exercising rights under

(i) subsection 224(1.2) of the *Income Tax Act*,

(ii) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(iii) any provision of provincial legislation that has a purpose similar to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, and the sum

(A) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(B) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection.

(3) Operation of similar legislation — An order made under section 11.02, other than the portions of that order that affect the exercise of rights of Her Majesty referred to in paragraph (1)(*a*) or (*b*), does not affect the operation of

(a) subsections 224(1.2) and (1.3) of the *Income Tax Act*,

(b) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts, or

(c) any provision of provincial legislation that has a purpose similar to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, and the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

and for the purpose of paragraph (*c*), the provision of provincial legislation is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as subsection 224(1.2) of the *Income Tax Act* in respect of a sum referred to in subparagraph (*c*)(i), or as subsection 23(2) of the *Canada Pension Plan* in respect of a sum referred to in subparagraph (*c*)(ii), and in respect of any related interest, penalties or other amounts.

37. (1) Deemed trusts — Subject to subsection (2), despite any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as being held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

(2) Exceptions — Subsection (1) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* (each of which is in this subsection referred to as a "federal provision"), nor does it apply in respect of amounts deemed to be held in trust under any law of a province that creates a deemed trust the sole purpose of which is to ensure remittance to Her Majesty in right of the province of amounts deducted or withheld under a law of the province if

(a) that law of the province imposes a tax similar in nature to the tax imposed under the *Income Tax Act* and the amounts deducted or withheld under that law of the province are of the same nature as the amounts referred to in subsection 227(4) or (4.1) of the *Income Tax Act*, or

(b) the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan*, that law of the province establishes a "provincial pension plan" as defined in that subsection and the amounts deducted or withheld under that law of the province are of the same nature as amounts referred to in subsection 23(3) or (4) of the *Canada Pension Plan*,

and for the purpose of this subsection, any provision of a law of a province that creates a deemed trust is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as the corresponding federal provision.

***Excise Tax Act*, R.S.C. 1985, c. E-15 (as at December 13, 2007)**

222. (1) [Deemed] Trust for amounts collected — Subject to subsection (1.1), every person who collects an amount as or on account of tax under Division II is deemed, for all purposes and despite any security interest in the amount, to hold the amount in trust for Her Majesty in right of Canada, separate and apart from the property of the person and from property held by any secured creditor of the person that, but for a security interest, would be property of the person, until the amount is remitted to the Receiver General or withdrawn under subsection (2).

(1.1) Amounts collected before bankruptcy — Subsection (1) does not apply, at or after the time a person becomes a bankrupt (within the meaning of the *Bankruptcy and Insolvency Act)*, to any amounts that, before that time, were collected or became collectible by the person as or on account of tax under Division II.

...

(3) Extension of trust — Despite any other provision of this Act (except subsection (4)), any other enactment of Canada (except the *Bankruptcy and Insolvency Act)*, any enactment of a province or any other law, if at any time an amount deemed by subsection (1) to be held by a person in trust for Her Majesty is not remitted to the Receiver General or withdrawn in the manner and at the time provided under this Part, property of the person and property held by any secured creditor of the person that, but for a security interest, would be property of the person, equal in value to the amount so deemed to be held in trust, is deemed

(a) to be held, from the time the amount was collected by the person, in trust for Her Majesty, separate and apart from the property of the person, whether or not the property is subject to a security interest, and

(b) to form no part of the estate or property of the person from the time the amount was collected, whether or not the property has in fact been kept separate and apart from the estate or property of the person and whether or not the property is subject to a security interest

and is property beneficially owned by Her Majesty in right of Canada despite any security interest in the property or in the proceeds thereof and the proceeds of the property shall be paid to the Receiver General in priority to all security interests.

***Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (as at December 13, 2007)**

67. (1) Property of bankrupt — The property of a bankrupt divisible among his creditors shall not comprise

(a) property held by the bankrupt in trust for any other person,

(b) any property that as against the bankrupt is exempt from execution or seizure under any laws applicable in the province within which the property is situated and within which the bankrupt resides, or

(b.1) such goods and services tax credit payments and prescribed payments relating to the essential needs of an individual as are made in prescribed circumstances and are not property referred to in paragraph (*a*) or (*b*),

but it shall comprise

(c) all property wherever situated of the bankrupt at the date of his bankruptcy or that may be acquired by or devolve on him before his discharge, and

(d) such powers in or over or in respect of the property as might have been exercised by the bankrupt for his own benefit.

(2) Deemed trusts — Subject to subsection (3), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a bankrupt shall not be regarded as held in trust for Her Majesty for the purpose of paragraph (1)(*a*) unless it would be so regarded in the absence of that statutory provision.

(3) Exceptions — Subsection (2) does not apply in respect of amounts deemed to be held in trust under subsection 227(4) or (4.1) of the *Income Tax Act*, subsection 23(3) or (4) of the *Canada Pension Plan* or subsection 86(2) or (2.1) of the *Employment Insurance Act* (each of which is in this subsection referred to as a "federal provision") nor in respect of amounts deemed to be held in trust under any law of a province that creates a deemed trust the sole purpose of which is to ensure remittance to Her Majesty in right of the province of amounts deducted or withheld under a law of the province where

(a) that law of the province imposes a tax similar in nature to the tax imposed under the *Income Tax Act* and the amounts deducted or withheld under that law of the province are of the same nature as the amounts referred to in subsection 227(4) or (4.1) of the *Income Tax Act*, or

(b) the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan*, that law of the province establishes a "provincial pension plan" as defined in that subsection and the amounts deducted or withheld under that law of the province are of the same nature as amounts referred to in subsection 23(3) or (4) of the *Canada Pension Plan*,

and for the purpose of this subsection, any provision of a law of a province that creates a deemed trust is, notwithstanding any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as the corresponding federal provision.

86. (1) Status of Crown claims — In relation to a bankruptcy or proposal, all provable claims, including secured claims, of Her Majesty in right of Canada or a province or of any body under an Act respecting workers' compensation, in this section and in section 87 called a "workers' compensation body", rank as unsecured claims.

...

(3) Exceptions — Subsection (1) does not affect the operation of

(a) subsections 224(1.2) and (1.3) of the *Income Tax Act*;

(b) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution, as defined in the *Canada Pension Plan*, or an employee's premium, or employer's premium, as defined in the *Employment Insurance Act*, and of any related interest, penalties or other amounts; or

(c) any provision of provincial legislation that has a similar purpose to subsection 224(1.2) of the *Income Tax Act*, or that refers to that subsection, to the extent that it provides for the collection of a sum, and of any related interest, penalties or other amounts, where the sum

(i) has been withheld or deducted by a person from a payment to another person and is in respect of a tax similar in nature to the income tax imposed on individuals under the *Income Tax Act*, or

(ii) is of the same nature as a contribution under the *Canada Pension Plan* if the province is a "province providing a comprehensive pension plan" as defined in subsection 3(1) of the *Canada Pension Plan* and the provincial legislation establishes a "provincial pension plan" as defined in that subsection,

and for the purpose of paragraph (*c*), the provision of provincial legislation is, despite any Act of Canada or of a province or any other law, deemed to have the same effect and scope against any creditor, however secured, as subsection 224(1.2) of the *Income Tax Act* in respect of a sum referred to in subparagraph (*c*)(i), or as subsection 23(2) of the *Canada Pension Plan* in respect of a sum referred to in subparagraph (*c*)(ii), and in respect of any related interest, penalties or other amounts.

Footnotes

1 Section 11 was amended, effective September 18, 2009, and now states:

11. Despite anything in the *Bankruptcy and Insolvency Act* or the *Winding-up and Restructuring Act*, if an application is made under this Act in respect of a debtor company, the court, on the application of any person interested in the matter, may, subject to the restrictions set out in this Act, on notice to any other person or without notice as it may see fit, make any order that it considers appropriate in the circumstances.

2 The amendments did not come into force until September 18, 2009.

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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

Court File No. C66626

ONTARIO
COURT OF APPEAL

PROCEEDING COMMENCED AT
TORONTO

BOOK OF AUTHORITIES
OF THE RESPONDENT

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