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FAQs ABOUT RESTRUCTURING

With the pandemic continuing to impact the economy, the "B" word is on the minds of many people. We thought it was a good time for a brief run down of some of the questions that we are asked most frequently about bankruptcy and insolvency. So, here we go:

When a tenant delivers a Notice of Intention ("NOI") to make a proposal under the Bankruptcy and Insolvency Act ("BIA"), can the landlord terminate for non-payment of rent?

Instead of filing for "liquidation-style" bankruptcy, an insolvent tenant may try to save its business by making a proposal under the BIA to its creditors (including its landlord). Creditors vote on the proposal and if it is accepted and approved by the Court, the proposal proceeds. If rejected, the tenant is deemed to have made an assignment in bankruptcy. Tenants usually start the process by filing a NOI. This results in an automatic 30-day "stay" period (which may be extended to 45 days). During a stay period, the landlord cannot distrain or terminate for arrears of rent; however, the tenant is required to pay current rent. Upon receiving a NOI the landlord should issue a rent invoice for the month, or part month, commencing on the date of the NOI. If the tenant fails to pay ongoing rent (for the period after the stay commences), then the landlord may take steps to terminate the lease (subject to the current moratorium on evictions in Ontario due to the pandemic, for CERS eligible tenants).

What is the difference between a BIA Proposal and a Plan under the Companies' Creditors Arrangement Act ("CCAA")?

The CCAA is more flexible than the BIA and is typically used by large companies. (A company must have debts exceeding $5,000,000 to qualify for CCAA proceedings.) A CCAA proceeding starts with an Initial Order that sets the ground rules including: a stay (similar to the automatic stay under a BIA proposal); priority for the financiers of the company during the CCAA proceedings (known as Debtor in Possession, or DIP, financing); the appointment of a monitor who oversees the business (but does not actually run the business) during the CCAA proceeding; and usually, requiring the payment of rent and providing a right to disclaim the leases. Aside from the right to disclaim, the Initial Order should not amend an existing lease. Recent changes to the CCAA reduced the maximum length of the initial stay period on an Initial Order from 30 days to 10 days.

After the expiry of the initial 10-day period, all concerned parties may return to Court for a "comeback hearing" in respect of the Initial Order where requests for more broad-sweeping relief may be considered, such as orders permitting the removal of fixtures, furniture and equipment, or the installation of signage advertising a liquidation sale.

What is the difference between a Court appointed receiver and a private receiver?

Security documents (such as mortgages or personal property security agreements) generally grant a secured creditor the right to appoint a receiver when their borrower defaults. Selected by a secured creditor pursuant to its security documents, a private receiver has no greater rights, vis-à-vis the landlord, than the tenant. In other words, the private receiver steps into the shoes of the tenant. A private receiver has no right to disclaim the lease or dictate a stay period. The appointment of a receiver is often an event of default for which a landlord may terminate the lease. By contrast, a Court-appointed receiver is Court supervised and may be given additional powers. A Court-ordered receivership is called an Interim Receivership Order ("IRO"). Typically, an IRO includes a stay order preventing landlords from terminating the lease during the receivership, so long as the rent is paid and the receiver otherwise complies with the lease.

Can a stay be lifted and the lease terminated?

One common feature of all restructuring cases is the "stay". While a company is restructuring under the BIA, the CCAA or an IRO, there will be a stay. The stay prevents landlords from terminating leases for past defaults. Landlords should not feel they are being treated unfairly, as the stay applies to all contracts. The debtor is required to pay ongoing obligations (e.g., rent), and comply with the lease during the restructuring period. Courts have discretion to lift or terminate a stay, to allow the claim of a particular creditor. This order may be granted where a landlord can prove to the Court that the tenant will suffer little prejudice and that the landlord will suffer significant prejudice if the order is not granted. However, the Ontario Court of Appeal has repeatedly made clear that lifting the stay is far from a routine matter and to be granted in exceptional cases only.

Can a tenant assign its lease and can a landlord object to an assignment of the lease?

Under the BIA and provincial landlord-tenant legislation (except in Quebec), a trustee in bankruptcy may elect to assign a lease following the tenant's bankruptcy. A trustee in bankruptcy can occupy the tenant's premises for up to 3 months following bankruptcy. During this time, the landlord cannot terminate the lease or distrain for arrears, and the trustee may elect to: retain, disclaim or assign the lease. If the trustee makes no election, then after 3 months the stay expires and the landlord may terminate the lease if there is a default (subject to the moratorium on

evictions in Ontario). In Quebec, a trustee in bankruptcy may remain in the premises, rent free, until the first meeting of creditors. If the lease contains an *ipso facto* termination on bankruptcy clause, the lease can be terminated after the creditors' meeting.

A landlord is not obliged to consent to a proposed lease assignment. The trustee in bankruptcy is permitted to make an application to the Court to seek approval of the assignment. The Court will approve the assignment where it is satisfied that the proposed tenant is a fit and proper person who will observe and perform all terms of the lease. Generally this gives the trustee in bankruptcy wide latitude in obtaining approval for an assignee.

Under CCAA, a debtor tenant may apply to the Court for an order assigning rights and obligations under any agreement, including a lease. Agreements may be assigned provided any financial defaults are remedied. In determining whether to make an assignment order, the Court will consider whether: (1) the person to whom the rights and obligations are assigned is able to perform the obligations; (2) it is appropriate to assign the rights and obligations to that person; and (3) the monitor approved the proposed assignment.

Are tenants able to disclaim their leases pursuant to either the BIA or CCAA?

Tenants may disclaim their leases under both the BIA and CCAA. An assignment in bankruptcy under the BIA allows the tenant's trustee in bankruptcy to disclaim a commercial lease pursuant to the BIA and the related provisions under landlord and tenant legislation in each of the provinces except Quebec. Typically, leases are not disclaimed until after the first creditors' meeting.

For the most part, disclaimer of a lease is effected similarly under both the CCAA and the BIA. However, under the CCAA, if the monitor does not approve the proposed disclaimer, the debtor tenant may apply for a Court order to disclaim the lease. Within 15 days of the debtor-tenant giving notice disclaiming a lease, the landlord may seek a declaration from the Court prohibiting the tenant from disclaiming. When deciding whether to allow the disclaimer, the Court will examine whether: (i) the monitor approved the proposed disclaimer; (ii) the disclaimer would enhance the prospects of a viable compromise or arrangement between the tenant and its creditors; and (iii) the disclaimer would likely cause financial hardship to the landlord. If approved by the monitor and unopposed by the landlord, the lease is disclaimed 30 days after the tenant gives notice of the disclaimer.

Is a landlord entitled to compensation when a lease is disclaimed?

The landlord's claim for a disclaimed lease in a "liquidation" bankruptcy is limited to a preferred rent claim. We are only exploring restructuring in this News ReLease, not liquidation. The BIA provides that under a proposal, a landlord of a disclaimed lease may claim for its actual loss or the lesser of: (i) 1 year's rent plus 15% of the rent payable over the remainder of the term, or (ii) 3 years' rent, as an unsecured creditor. Under the CCAA, there are no fixed rules and the compensation for a disclaimed lease depends on the terms of the Plan of arrangement as approved by the creditors and the Court. (NB: There also might be a subtenant in the picture, who may have the right to take over the premises.)

Are tenants who are restructuring under the CCAA required to pay rent post-filing when their ability to operate the premises is impeded by governmental COVID-19 restrictions?

Section 11 of the CCAA grants broad discretionary powers to the Court to make any order it considers appropriate; however, these powers are limited by restrictions set out in the CCAA. One of these restrictions is that no order can be made under section 11 that would prohibit a person from requiring immediate payment for goods, services, or the use of leased or licensed property. This ensures that any tenant that chooses to retain their lease while restructuring cannot seek an order from the Court to stop paying rent while under CCAA protection. In the recent decision of *Groupe Dynamite Inc v Deloitte Restructuring Inc*., the Court confirmed that even when tenants are forced to shut down their premises due to a government order, mere possession of the leased property and the landlord's consequent inability to rent it to anyone else constitutes "use of leased premises" within the meaning of section 11 of the CCAA. As such, tenants are not excused from paying rent despite their inability to operate their business during a COVID-19 shut down.

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