

# Financial Services Flash

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## Trustee Cannot Disclaim Bankrupt Landlord's Lease

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In *Aventura*<sup>2</sup>, a recent decision of the Ontario Superior Court of Justice (Commercial List) (the "Court"), the Honourable Justice Penny confirmed that a bankruptcy trustee does not have the authority, pursuant to section 30(1)(k) of the *Bankruptcy and Insolvency Act* (the "BIA"), to disclaim a lease on behalf of a bankrupt landlord. Rather, a trustee's authority to disclaim a lease is limited to situations where the bankrupt is the tenant. His Honour held that, where the bankrupt is the landlord and "[w]here the tenant is not in breach, neither the landlord, nor his trustee in bankruptcy, has the power to terminate the lease."<sup>3</sup>

Section 30(1)(k) of the BIA provides a trustee the authority, with the permission of the inspectors of the bankrupt estate, to elect "to disclaim or resiliate any lease of, or other temporary interest or right in, any property of the bankrupt." At issue in *Aventura* was whether this authority extended beyond the trustee of a bankrupt tenant, giving the trustee of a bankrupt landlord the power to terminate a lease.

In *Aventura*, the owners of an indoor sports complex (the "Debtors") ran into financial trouble. A court-appointed receiver (the "Receiver") was appointed over the Debtors' property, and the Receiver assigned the Debtors into

bankruptcy and became their bankruptcy trustee (the "Trustee"). The Debtors' property included the sports complex and certain leases in relation thereto, including a five-year lease with Kendal Aquatics Swim Program Ltd. (the "Tenant") for the pool facility, which lease was set to expire on December 31, 2015 (the "Lease").

An agreement of purchase and sale was entered into between the Receiver and an arm's-length party (the "Purchaser") for the acquisition of the Debtors' property, which agreement was approved by the Court by way of a standard Approval and Vesting Order (the "AVO"). Amongst other things, the AVO vested all the purchased assets in the Purchaser, which purchased assets included the Lease. After the Court issued the AVO, the Purchaser claimed that it became aware of additional information causing it to conclude that the Lease was uneconomic. The Purchaser refused to close the transaction unless it received a substantial reduction in purchase price, or the Receiver disclaimed the Lease pursuant to section 30(1)(k) of the BIA. The Receiver complied with the latter request, and on the day the sale transaction closed, delivered a Notice of Termination to the Tenant such that the Tenant was essentially given 12 days' notice to vacate the premises (the "Notice").

The Tenant brought a motion under section 37 of the BIA to reverse the Trustee's decision to disclaim the Lease, which motion was allowed. In surveying the jurisprudence, His Honour noted that "[t]he settled authority, since 1960, on

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<sup>2</sup> 2015 ONSC 5026, 28 C.B.R. (6th) 157 [*Aventura*].

<sup>3</sup> *Ibid* at para. 27.

*this point has consistently been that the authority granted to a trustee under 30(1)(k) does not extend to the disclaimer of a lease on behalf of a landlord, unless such authority is specifically granted by provincial law.”<sup>4</sup> As there is no basis in Ontario under the *Commercial Tenancies Act* for a landlord to terminate a lease unilaterally where its tenant is not in breach, His Honour held that the Trustee had no authority for having issued the Notice, such that it was void *ab initio* and the Lease remained in full force and effect. His Honour also held that, since the Purchaser received notice of the Lease prior to entering into the agreement of purchase and sale, the Purchaser therefore acquired the sports complex subject to the Lease.*

While costs were not awarded against the Trustee, the same may not hold true the next time a bankruptcy trustee purports to disclaim a lease on behalf of a bankrupt landlord, and trustees should therefore take note that the powers granted by section 30(1)(k) of the BIA only apply in respect of leases pursuant to which the bankrupt is a tenant. In *Aventura*, His Honour noted that the Purchaser opted to play “hard ball” and sought to manipulate the powers of the Trustee to its financial advantage. Therefore, His Honour awarded costs on a substantial indemnity basis against the Purchaser.

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<sup>4</sup> *Ibid* at para. 26.

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