

CANADA / JUDGMENT

## Quest University Canada (Re)

2020 BCSC 921

COURT

Supreme Court of British Columbia

DECIDED

19 June 2020

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2020 BCSC 921 Quest University Canada (Re)

IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation:

Quest University Canada (Re),

2020 BCSC 921

Date: 20200619

Docket: S200586

Registry: Vancouver

In the Matter of the COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, c. C-36, as amended

- and -

In the Matter of the SEA TO SKY UNIVERSITY ACT, S.B.C. 2002, c. 54

- and -

In the Matter of A PLAN OF COMPROMISE AND ARRANGEMENT OF QUEST UNIVERSITY CANADA

Petitioner

Before: The Honourable Madam Justice Fitzpatrick

Reasons for Judgment

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P.J. Reardon

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Place and Date of Hearing:

Vancouver, B.C.

June 10, 2020

Place and Date of Judgment:

Vancouver, B.C.

June 19, 2020

## **INTRODUCTION**

- [1] On January 16, 2020, this Court granted an initial order (the "Initial Order") in favour of the petitioner Quest University Canada ("Quest"), pursuant to the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36 (the "CCAA"). The Initial Order included a stay of proceedings to January 27, 2020.
- [2] On January 27, 2020, this Court granted an Amended and Restated Initial Order (ARIO). The ARIO provided for a further extension of the stay of proceedings to May 29, 2020 in order to allow Quest to continue with its restructuring efforts. In addition, the ARIO authorized Quest to obtain an interim credit facility of \$5.5 million, to allow continued operations. See Quest University Canada (Re), 2020 BCSC 318.

- [3] On May 28, 2020, the matter came back before me. By then, there was considerable support of Quest's efforts among the stakeholders, particularly given its tentative steps toward finding an academic partner. I granted an order extending the stay to August 10, 2020 (or September 30, 2020, if a transaction arises). In addition, I approved an increase of the interim lending facility to \$8.2 million. See *Quest University Canada (Re)*, 2020 BCSC 860.
- [4] At that time, Quest premised its request for an increase in the interim lending facility, to some extent, on it deferring rent payments on four of its University residence buildings (the "Residences") from June-August 2020. Southern Star Developments Ltd. ("Southern Star") is the owner of the Residences and Quest's landlord. Southern Star objected to any rent deferral, as did Southern Star's secured lender, Bank of Montreal (BMO).
- [5] This application is to determine whether it is appropriate to allow Quest to defer rent payments to Southern Star. As agreed between the parties, Quest has paid the June 2020 rent to the Monitor, who is holding the funds pending the result of this hearing.

## BACKGROUND FACTS

- [6] In the early 2000s, Quest was formed as a private, not-for-profit, post-secondary institution, pursuant to the Sea to Sky University Act, S.B.C. 2002, c. 54 (the "Sea to Sky Act").
- [7] In 2001, a foundation acquired a 240-acre property in Squamish, BC. The foundation subdivided the property and sold a portion of the lands. The proceeds funded construction costs for the university campus on the remaining lands. In 2006, the foundation transferred the remaining lands to Quest. Quest remains the owner of the campus lands and other yet undeveloped lands.
- [8] In 2007, Quest accepted its first class of 73 students.
- [9] One of the stated purposes of Quest under s. 3(e) of the Sea to Sky Act is to "incorporate residential experiences into the academic programs". Since 2011, consistent with that purpose, Quest and Southern Star have developed the Residences on Quest's lands (on Lots A, B, C and D). The Residences can accommodate 513 students. Tentative plans are in place for a further residence building on Lot E.
- [10] Quest has also developed another residence on the campus, known as "Riverside".
- [11] The arrangements in relation to the Residences, as between Quest, Southern Star and other parties, are complex. I will describe them more fully in the discussion below. For context at this stage, I will provide a general description.
- [12] Southern Star owns the Residences on lands held by Quest. Southern Star holds long-term ground leases granted by Quest, as landlord (the "Ground Leases"). In turn, Southern Star, as landlord, granted subleases of the Residences in favour of Quest, as tenant (the "Subleases"). The Subleases cover a period of time during which the parties anticipated the repayment of the financing obtained to construct the Residences, through the rent payments made by

Quest. At present, the monthly rent amount payable by Quest for the Residences is about \$240,000.

- [13] When this restructuring began, all students attending Quest were required to reside on campus in the Residences. This arrangement was integral to the educational experience that Quest offered to the students. A significant number of those students (some 75%) were from international locations. In addition, some faculty members resided in the Residences.

#### COVID-19 PANDEMIC

- [14] Consequences arising from the pandemic, as experienced in BC, across Canada and around the world, are well known.
- [15] On March 12, 2020, Quest's board of governors directed the closure of Quest's campus to the public and students. Quest requested that students leave campus and complete the spring and summer terms online. Students and most faculty vacated the Residences. A small number of staff stayed behind for security purposes.
- [16] On March 18, 2020, the BC government issued Ministerial Order No. M073 by which it declared a state of emergency under the Emergency Program Act, R.S.B.C., 1996, c. 111 arising from the COVID-19 pandemic.
- [17] On March 26, 2020, the federal government prohibited the entry of foreign nationals into Canada, save from the United States, pursuant to s. 58 of the Quarantine Act, S.C. 2005, c. 20: Order in Council, PC Number 2020-0184. On May 21, 2020, government extended this prohibition to the US: Order in Council, PC Number 2020-0370.
- [18] Many BC government and Provincial Health Officer orders followed to address the COVID-19 pandemic. These include the May 22, 2020 order of the Provincial Health Officer under the Public Health Act, S.B.C. 2008, c. 28 with respect to "mass gathering events", prohibiting gatherings of more than 50 patrons.
- [19] The timing of the pandemic and its severe consequences could not have been worse for Quest in terms of its restructuring efforts. Prior to March 2020, Quest was in exploratory discussions with 12 potential academic or financial partners.
- [20] After closure of Quest's campus, Quest's Restructuring Committee (the "Committee") adapted to running Quest's programs online. They also significantly reduced operating costs of the university and accessed whatever government programs were available. Throughout all this, the Committee continued to advance negotiations with potential partners, including by:
- a) Working with a private education consultant, Halladay Education Group Inc. ("Halladay") to find a prospective academic partner for Quest;
  - b) Engaging Colliers Macaulay Nicolls Inc. ("Colliers") to find prospective purchasers or developers for Quest's real property assets; and

- c) Engaging with the BC government and academic post-secondary representatives to pursue public partnerships.
- [21] Despite the pandemic and its far-reaching consequences, several parties remained in negotiations with Quest. Unsurprisingly, discussions proceeded at a slower pace given the uncertainty during the early stages of the pandemic regarding its length, severity and economic impact.
- [22] Since mid-March 2020, and despite these challenges, Quest has advanced its pursuit of a variety of potential restructuring options:
  - a) On April 30, 2020, Quest entered a non-exclusive Letter of Intent (LOI) with an internationally based private academic institution (the "Academic Partner"). Quest identified this potential opportunity at the May 28, 2020 hearing.

Quest and the Academic Partner are currently in negotiations and working towards finalizing definitive documents by July 31, 2020, with a view to concluding a transaction by September 30, 2020. The LOI is conditional upon Quest maintaining its operations and continuing to operate as a post-secondary institution. In addition, the LOI provides for the funding necessary for Quest to address its secured debt, fund a plan to its unsecured creditors and obtain working capital;

- b) Quest is also pursuing several other possible partnership opportunities. Colliers has identified several proponents with a strong interest in Quest. Quest is currently negotiating the terms of a letter of intent with one proponent and it is expected that further letters of intent will be received into June 2020; and
- c) Quest has also spent considerable time in negotiations with a development group that works independently of Colliers and Halladay. That group's intent is toward a tripartite educational institution/developer partnership that would result in the development of Quest's surplus lands, while running academic institutions on the campus.
- [23] Potential partners (both academic and development wise) have indicated that a functioning post-secondary educational institution operating on Quest's current lands greatly enhances their view of the value of Quest's assets. Significantly, these potential partners have also indicated that the availability of the Residences is integral to their interest in pursuing a transaction with Quest.
- [24] Quest is now facing the challenge of determining how it will offer the fall term programming to students under current health and safety guidelines. Quest is well positioned to respond quickly in offering more in-person instruction as it becomes safe to do so. Quest also intends to allow students to return to campus as government orders and guidelines permit.

- [25] However, Quest anticipates that, due to COVID-19 and Quest's on-going restructuring efforts, student enrollment numbers for fall 2020 will be lower than originally forecasted a year ago. There remains significant uncertainty about students physically returning to the campus in the fall. As noted above, a large number of international students have historically attended the university. Quest does not know if those students will be able to attend Quest in the fall, given the current policies and restrictions on international travel and border closures.
- [26] Quest's intention is that, when it is able to return to full on-campus operations, it will again offer students the experience of residing in the Residences.

## THE APPLICATION

- [27] When Quest closed the campus, almost all students vacated the Residences. Quest continued to pay rent to Southern Star into April and May 2020.
- [28] On May 18, 2020, Quest advised Southern Star that Quest would not be making rent payments for the Residences beginning in June 2020 "pending positive developments in the CCAA". Quest cited the ongoing restructuring proceedings, the closure of on-campus learning and the uncertainty of what academic instruction it would offer in fall 2020 as reasons for the deferral. By this time, the Court had approved the interim financing to allow operations to continue to late May 2020.
- [29] Quest offered to negotiate a rent deferral agreement with Southern Star over the next several months, hopeful that Southern Star would be accommodating given their lengthy business relationship and the COVID-19 pandemic.
- [30] Southern Star immediately indicated its unwillingness to do so. On May 27, 2020, Michael Hutchison, president of Southern Star, stated in his Affidavit #1 that, without receipt of rent payments from Quest, Southern Star will not be able to make its mortgage payments to BMO. For obvious reasons, that is not an attractive situation for Southern Star, nor of course, BMO.
- [31] Quest's application, filed late May 2020, is to amend para. 9 of the ARIO to allow Quest to defer rent payments to Southern Star. Paragraph 9 tracks from BC's Model CCAA Initial Order and requires that Quest pay rent under its real property leases after the filing date. Paragraph 9 reads:

Until such time as a real property lease is disclaimed in accordance with the CCAA, the Petitioner shall pay all amounts constituting rent or payable as rent under real property leases (including, for greater certainty, common area maintenance charges, utilities and realty taxes and any other amounts payable as rent to the landlord under the lease) based on the terms of existing lease arrangements or as otherwise may be negotiated between the Petitioner and the landlord from time to time ("Rent"), for the period commencing from and including the Order Date, twice-monthly in equal payments on the first and fifteenth day of the month in advance (but not in arrears). On the date of the first of such payments, any Rent relating to the period commencing

from and including Order Date shall also be paid.

[32] Quest seeks to add the following wording to para. 9 of the ARIO:

Notwithstanding the foregoing, the Petitioner, as tenant, may forego any and all rent payments owing to Southern Star Developments Ltd., its successors or assigns, as landlord, in respect of real property leases for the Quest University Canada residence buildings on the Petitioner's lands during or for the months of June, July and August 2020, subject to further order of this Court.

[33] In late May 2020, as above, Quest sought and obtained an increase in the approved interim financing by \$3 million. The cash flow forecast that accompanied that application, attached to the Monitor's Second Report, did not reference any rent payments by Quest to Southern Star until October 2020. Accordingly, the approved interim financing is not sufficient to fund Quest's rent payments over the summer months and appears to contemplate an even longer rent deferral period than Quest proposes on this application.

[34] Quest contends that it is imperative to maintain the Subleases and its long-standing partnership with Southern Star, in terms of its future prospects as a post-secondary institution and its ability to pursue restructuring options.

[35] Quest explains its plans to address any unpaid rent owing to Southern Star:

Quest is optimistic that a transaction that permits Quest to remain as a post-secondary institution and valuable member of the Squamish community is achievable based on the opportunities currently before Quest. Upon closing of such a transaction, Quest anticipates it will be in a position to make the June, July and August payments to Southern Star Developments, or otherwise enter into suitable arrangements with Southern Star Developments, and that the delay in doing so will not unduly prejudice Southern Star Developments.

[36] Southern Star, supported by BMO, strongly disagrees with Quest's statement that they will not be prejudiced. Both remain adamant that Quest must pay the rent.

## STATUTORY FRAMEWORK

[37] The Initial Order imposed a stay in respect of Quest and its Business and Property (as defined in the Initial Order), as is typical in these proceedings: CCAA, s. 11.02(1). As stated many times before, the stay had the salutary effect of maintaining the status quo as between Quest and its stakeholders: *Woodward's Ltd. (Re)* (1993), 77 B.C.L.R. (2d) 332 (S.C.).

[38] Quest sought and obtained that relief, however, based on its stated intention to continue to operate as a university during its restructuring process, all with the supervision of the Monitor and the Court. Indeed, a continuation of Quest's operations through the means of a restructuring proceeding is the hoped for result.

- [39] While the stay addresses actions by pre-filing creditors, those persons who continue to do business with an insolvent company in CCCA proceedings are often (and understandably) concerned about how their ongoing business relationship will go forward and, if appropriate, how they will be paid for post-filing services provided. A company will usually address that issue immediately to quell any concerns and avoid disruption of the supply of those goods and services.
- [40] Generally speaking, a company in CCAA proceedings will consider a variety of ways to pay for (or rid itself of) these post-filing services. A company may:
- a) Confirm the agreement of the supplier to continue with the previous arrangements or alternatively, negotiate new payment terms, typically as demanded by the supplier (for example, COD or shortened payment deadlines);
  - b) Obtain interim financing to allow for ongoing operations and payments, all as reflected in cash flow statements (CCAA, s. 11.2);
  - c) Obtain a critical supplier designation to compel further supply on terms (CCAA, s. 11.4). In that event, the Court must order a security or charge in favour of that supplier (CCAA, s. 11.4(3)); and
  - d) Deliver a notice of disclaimer of executory contracts to avoid ongoing obligations (CCAA, s. 32).
- [41] The Initial Order sought by Quest (and later confirmed in the ARIO) reflected many of these strategies to deal with post-filing obligations that were expected to arise:
- a) Quest was entitled to pay expenses reasonably incurred in carrying on the Business in the ordinary course (ARIO, para. 7);
  - b) Quest was entitled to pay amounts for goods and services (both pre- and post-filing) if the supplier was deemed (with consent of the Monitor) to be critical to the Business and its ongoing operations and to ensure ongoing supply (ARIO, paras. 5(c) and 6);
  - c) Quest was required to pay rent under its real property leases based on the existing lease agreements or as may otherwise be negotiated (ARIO, para. 9); and
  - d) Quest was able to disclaim any executory contracts to avoid ongoing obligations (CCAA, s. 32). The ARIO addressed the consequences of any disclaimer of real property leases (paras. 12 and 13).
- [42] Contrary to Quest's position on this application, the mandated payment of rent under its real property leases in the ARIO was distinct from other provisions in the ARIO that did not allow Quest to make payments in respect of "financing leases which create security interests" (ARIO, para. 10(b)).

- [43] I agree with Quest that there is no specific CCAA provision that requires a company to make payment to persons who supply good and services in the post-filing period (including a landlord for post-filing rent).
- [44] However, fundamentally, the Initial Order and the ARIO reflect the common understanding in CCAA proceedings that, as Quest continued in the process, it would continue its operations substantially in the ordinary course and would pay for those operations. It is unsurprising that counterparties to those arrangements would expect payment as a matter of fairness. It would clearly be unattractive for a post-filing supplier to allow Quest, an insolvent company, to run up substantial obligations that might or might not be paid at the end of the day, depending on the outcome of the restructuring process: *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.*, 2007 SKCA 72 at paras. 41-42.
- [45] Section 11.01(a) of the CCAA circumscribes the discretion of the Court to impose an order or stay in respect of payment for post-filing supply of goods and services. In my view, Parliament's intention in enacting this provision is to balance the interests of a debtor company and its stakeholders and post-filing suppliers. Section 11.01 reads:

**No order made under section 11 or 11.02 has the effect of**

- (a) prohibiting a person from requiring immediate payment for goods, services, use of leased or licensed property or other valuable consideration provided after the order is made; or
  - (b) requiring the further advance of money or credit.
- [46] In *Air Canada (Re)*, [2004] O.J. No. 576 (S.C.J.), Justice Farley addressed an application by aircraft lessors to obtain post-filing rent for a plane that was not returned until months after the lease was repudiated. At para. 6, Farley J. noted that the above CCAA provision (then s. 11.3) meant that the lessor could require payment for use of the plane on the contract terms. The court ordered Air Canada to make payment.
- [47] Similarly, in *Boutiques San Francisco Inc. (Re)*, [2004] Q.J. No. 2886, Justice Gascon (as he then was) dealt with the right of unpaid suppliers to repossess their goods, in this case display units, from a CCAA debtor. At paras. 103-105, Gascon J. consider the CCAA provision (then s. 11.3). He held that, if the debtor wished to continue using the display units, it had to abide by the terms of the agreement and pay for them.
- [48] In *Cosgrove-Moore Bindery Services Ltd. (Re)*, [2000] 48 O.R. (3d) 540 (S.C.J.), the same reasoning was applied in the context of a proposal under the Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3 (the "BIA"). The BIA, s. 65.1 contains similar provisions to those in the CCAA imposing restrictions on counterparties but also not allowing the stay to prevent a post-filing supplier or lessor from demanding payment. Justice Ground stated:

- [10] I have come to the conclusion that the purpose of s. 65.1 is to provide a commercial enterprise with the opportunity to continue operations while working toward a reorganization but at the same time to give creditors obligated to continue to supply goods, services or the use of leased property some protection that payments ordinarily due during the proposal period will not be wiped out or reduced to pro rata unsecured claims in the event of an ultimate bankruptcy.
- [49] Consistent with the above authorities, and the common approach in CCAA proceedings, the ARIO required payment of the rent to Southern Star (as proposed by Quest).
- [50] I conclude that, even if I were to grant Quest the ability to "forego" the rent payments (the proposed addition to para. 9 of the ARIO), nothing would change. Quest already has that general ability under para. 7 of the ARIO, which says that Quest is only "entitled" to make such payments.
- [51] If s. 11.01 of the CCAA applies here, upon any default by Quest, the stay in the ARIO would not prohibit Southern Star from demanding immediate payment of the rent for the Residences. It is common ground that, if Southern Star (and perhaps even BMO) wished to take further action to address the default (under the Subleases and BMO's mortgage), they may be required to seek to lift the stay to allow them to proceed further. I will make no further comment in that respect as the issue is not before me.
- [52] Quest has no illusions that this issue must be resolved in some fashion, and resolved soon, so that it can go forward on some basis, hopefully toward a successful restructuring. I consider that, in essence, Quest is seeking a determination that, if the Court allows Quest to "forego" paying the rent payments, Southern Star or BMO are not allowed to make demand under s. 11.01(a) and seek to lift the stay.
- [53] With this background, Quest argues that s. 11.01(a) of the CCAA does not apply to negate the effect of the general stay (s. 11.02) to allow Southern Star to proceed in the event of default under the Subleases. Quest argues:
- a) The Subleases are, in substance, financing leases, which are not included within s. 11.01; and
  - b) Quest is not "using" the Residences, as required by s. 11.01.
- [54] The right of a supplier to proceed under s. 11.01 is an exception to the application of the general stay under s. 11.02. The purpose of the general stay is to further the remedial purposes of the CCAA. In that context, courts have consistently interpreted s. 11.01 narrowly: *Sproule v. Nortel Networks Corporation*, 2009 ONCA 833 at para. 17; *Smith Brothers Contracting Ltd. (Re)*, [1998] B.C.J. No. 728 (S.C.) at para. 41; and *Royal Bank of Canada v. Cow Harbour Construction Ltd.*, 2012 ABQB 59 at para. 20.

#### ARE THE SUBLEASES AKIN TO FINANCING LEASES?

- [55] Quest argues that s. 11.01(a) only applies to "true leases" and not financing leases. Quest argues that the nature of its arrangements with Southern Star goes well beyond rent payments for "use of leased . . . premises"; rather, Quest says those arrangements were, in essence, financing agreements which are subject to the general stay.
- [56] The "true lease" versus "financing lease" distinction often arises in insolvency proceedings, but in relation to personal property. This arises from requirements of personal property security legislation across Canada which "deem" even true leases exceeding one year to be a "security interest" requiring registration in order to maintain priority: in BC, the Personal Property Security Act, R.S.B.C. 1996, c. 359, ss. 3, 20 (the "PPSA"). Even so, the deeming provision in the PPSA does not affect the true nature of a lease: *Connacher Oil and Gas Limited (Re)*, 2017 ABQB 769 at para. 17.
- [57] In *Smith Brothers Contracting*, this Court first discussed the interplay between the nature of the lease and the application of s. 11.01 (then s. 11.3) of the CCAA. As noted in *Integris Credit Union v. Mercedes-Benz Financial Services Canada Corporation*, 2016 BCCA 231 at para. 45, *Smith Brothers Contracting* stands for the proposition that, under s. 11.01(a), creditors with "true leases" are entitled to continuing payments in CCAA proceedings while those with financing leases are not. What governs the application of s. 11.01 is the substance of the transaction, not simply the form: *Smith Brothers Contracting* at para. 26.
- [58] In *Smith Brothers Contracting*, the leased property in question was personal property, namely trucks. Justice Bauman (as he then was) considered the terms of the leases. Of particular importance were clauses that allowed acceleration of the debt upon default. The lessors could repossess the trucks to recover the debt owing under the entire lease term (not just to default). Upon later sale of the trucks, proceeds were applied to the debt, which inherently recognized amounts that would have been paid by the lessee to that time (i.e. the lessee's equity).
- [59] Justice Bauman found that the truck leases were, in substance, financing leases. Accordingly, they were not covered by s. 11.01(a) of the CCAA:
- [56] What I take from all of this is that by preserving a limited remedy for lessors, that is, "payment for use", in a field of commercial transactions which, as I have shown with these leases, encompasses a variety of arrangements with much broader remedies on default, s. 11.3(a) can be interpreted as restricting itself to the type of arrangement which is characterized by the narrower bargain. More simply: this analysis suggests that s. 11.3(a) does not cover all leases. Rather, it covers traditional true leases where the essential bargain is payment for use.
- [57] To put the matter in a slightly different way: Ford Credit's lease does not simply require "payment for . . . use of leased or licenced property", clause 21 secures payments when the property will clearly not be used by the lessee after a default and a retaking by the lessor.

[58] Further, can one say that the leases here contemplate payments by the lessee only for the use of the vehicles? That after all is the epitome of a true lease -- that is, a contract of bailment. Once again, clause 21 assists. On a default, the lessee is liable for the lease payments for the unexpired term. However, it is contemplated that the dealer will sell the vehicle and:

. . . will subtract from the amount owed sums received from the sale of the Vehicle in excess of what Dealer would have had invested in the Vehicle at the end of the lease term.

[59] I can only conclude that by crediting the lessee in these circumstances with the excess sum defined in clause 21, the document is implicitly (and fairly) ensuring that even a defaulting lessee will enjoy whatever equity he or she has effectively built up in the vehicle.

[60] From this perspective one can say that the lessee under these leases is not simply paying for use of the vehicle. He or she is potentially acquiring, as well, equity therein.

[61] It is only payments for the use of leased property that are excepted from a s. 11 stay order under s. 11.3(a). Payments for use and equity are not. Similarly payments for use and equity and an option to purchase are not. This is another reason to conclude the s. 11.3(a) is not inclusive of all forms of lease.

[60] Courts across Canada have consistently applied the reasoning in Smith Brothers Contracting in the interpretation of s. 11.01 with respect to personal property leases (see discussion in Cow Harbour Construction). No Canadian court has extended the Smith Brothers Contracting reasoning to real property leases.

[61] At this point, I will return to a more fulsome description of the arrangements between Quest, Southern Star and other persons with respect to the Residences.

[62] The commercial relationships relating to the financing, ownership and use of the Residences is governed by a complex set of agreements, as follows:

- a) Letter of Intent: On November 3, 2011, Quest, Mr. Hutchison and Mr. Hutchison's company entered into a letter of intent with respect to the proposed arrangement for development of student housing on Quest's lands;
- b) Limited Partnership: On June 5, 2012, the parties formed the Southern Star Developments Limited Partnership (the "LP"). Under the agreement, Southern Star is the LP's general partner (the "GP"); Quest is the sole limited partner. The stated business and purpose of the LP (s. 2.3 of the agreement) is:
  - a) To cause the [LP] to hold as its sole asset the Property and the profits and proceeds therefrom;
  - b) To develop the Property for use as student and university related housing leased to [Quest] to be used as an integral part of its academic community.

In July 2014, the purposes of the LP and the general nature of the LP's business was restricted to:

2(a) the acquisition, development, ownership, rating, maintenance, leasing, holding for investment and otherwise realizing economic benefits from land located in the District of Squamish to be used as student and university related housing to be lease to [Quest];

- c) Southern Star: Ownership of Southern Star (the GP of the LP) is held among various persons: Attu Holdings Ltd. ("Attu") is the sole shareholder of the Class A Preference shares; and, Southern Star Holdings Ltd. ("Holdings"), as trustee of the Southern Star Trust, is the sole shareholder of the Class C and E Common shares;
- d) Ground Leases: Commencing in August 2012, Quest and Southern Star entered into long-term leases of the lands (i.e. the Ground Leases) to allow Southern Star to construct the Residences. Quest, as owner, leased the lands to Southern Star for 99 years at a nominal rate (\$1). The Grounds Leases expressly acknowledge that Southern Star would seek financing for the cost of constructing the Residences and would be entitled to mortgage its leasehold interest under the Ground Leases in respect of Quest's lands and the Residences (referred to as the "Buildings"). Under the Ground Leases, use of the lands and Buildings was restricted to that consistent with zoning and "as an integral part of the operation of [Quest]";
- e) BMO Mortgage: Southern Star and the LP, jointly and severally, obtained construction financing of approximately \$38.1 million from BMO. Both granted a demand mortgage in favour of BMO to secure the financing. The BMO mortgage secured Southern Star and the LP's real property interests under the Ground Leases and the Subleases. The mortgage was registered against the Lots A-D titles. The current balance outstanding is approximately \$34.4 million;
- f) Subleases: Commencing in August 2012, Quest and Southern Star entered into the Subleases for each of the Residences over a 25-year period (subject to certain renewal rights). Arising from the Subleases:
  - i. Southern Star, as landlord (through the Ground Leases), subleases the Premises to Quest, as tenant. "Premises" are defined as the Residences as built on the lands;
  - ii. Quest's "rent" is calculated as the greater of:
    - 1) A set monthly amount (this varied depending on the Residence to which the sublease applies), or
    - 2) A monthly amount equivalent to the blended principal and interest (BMO's prime rate plus 2% per annum) on the principal amount (essentially, the cost of the construction financing owed to BMO under the mortgage);
  - iii. "Use of the Premises" is restricted to providing student residential housing "to be used as an integral part of [Quest's] academic community and endeavours . . .";

- iv. In typical fashion, Quest covenants to pay rent; Southern Star covenants to provide "quite enjoyment" of the Premises to Quest;
- v. Southern Star can terminate the Subleases and re-enter upon default. The Subleases require that Quest pay rent on the leases for each of the Residences for 25 years and maintain the leases in good standing for the 25-year term;
- g) Deed of Gift: Attu and Holdings, as trustee, delivered to Quest a deed of gift regarding the shares held by them in Southern Star. The express purpose of the gift was to grant Quest the value of the interest in the Residences after Quest paid rent under the Subleases for 25 years. As part of these arrangements, Attu and Holdings delivered their Southern Star shares into escrow. Attu and Holdings agreed that they would, commencing on the 13th year of each Sublease, transfer a portion of the Class A (Attu) and Class C and E (Holdings) shares to Quest. Three points of interest arise here:
- i. Presently, Attu and Holdings have not yet transferred any Southern Star shares to Quest since the first Sublease has not yet reached its 13th year. Accordingly, Attu and Holdings retain full ownership of Southern Star (the GP);
- ii. The obligations of Attu and Holdings to transfer their shares in Southern Star to Quest are conditional upon:
- 1) Quest being in good standing at the time of the gift (subject to some contradictory language in the Amended Deed of Gift about whether that "good standing" was required over the entire Sublease terms); and
- 2) Quest's issuance of a charitable donation receipt for fair market value of the Class C shares;
- iii. The escrow agreement between Attu, Holdings, Southern Star and Quest and the Escrowholder, address possible default by Quest. Upon Quest's default under the Subleases, the Escrowholder must deliver back Attu and Holdings' shares in Southern Star.
- [63] By the interplay between these agreements, the parties anticipated that, if Quest paid rent over the 25-year terms of the Subleases, it would receive the value of the interests in the Residences, through increasing ownership of Southern Star shares commencing in the 13th year of each Sublease. Effectively, after 25 years, Quest would hold all interests in the LP, being its existing limited partnership interests, and it would own all the shares in the LP's GP, Southern Star.
- [64] Quest submits that the Subleases, both themselves and as part of the entire suite of transactions between the parties, are much more than "payments for use" of the Residences, as being indicative of a "true lease".
- [65] I am unable to agree.

- [66] The Subleases only reflect normal real property lease terms; use in exchange for rent. There is no reference to financing or even the possibility of Quest acquiring equity in Southern Star through the means of paying rent. The only possible underpinning for this argument is that the amount of rent is linked to the cost of the BMO financing. However, this only means that rent is calculated by reference to the cost of that financing. The basis for the rent calculation, either on its own or in the context of the entire document, does not elevate the Subleases, whether in form or substance, to something they clearly are not.
- [67] I do not read or interpret the Subleases as amounting to Southern Star, as landlord, providing financing to Quest.
- [68] Essentially, Quest argues that the Court should read all of these various agreements together, so as "interpret" the Subleases. This argument also fails. The parties intended that the Subleases would operate within the overall arrangements. However, if there is any "financing" aspect through those arrangements, that aspect is found in the Deed of Gift agreements, not the Subleases. Although the Deed of Gift agreements reference the Subleases, the gifting is subject to terms and conditions that are entirely separate and distinct from the Subleases.
- [69] Importantly, the giftors of the Southern Star shares under the Deed of Gift agreements are not Southern Star, Quest's landlord. It is apparent that the giftors, Attu and Holdings, are related to Southern Star in some fashion. However, accepting Quest's arguments would amount to the Court ignoring the separate legal existences of Attu and Holdings, when there is absolutely no basis upon which I might do so.
- [70] I agree that, effectively, under these arrangements, the parties intended that Quest would eventually acquire all of the Southern Star ownership interests. However, that intent is accomplished by the interplay between the separate agreements. Each of those agreements created separate legal relationships and the agreed upon terms and conditions reference the accompanying rights and obligations that arise within those legal relationships. The legal relationships that arise are not only between Quest and Southern Star, but between others as well.
- [71] I also agree that the agreements other than the Subleases form part of the factual matrix in terms of any interpretation of the Subleases. However, as stated in *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53 at para. 57, surrounding circumstances or the factual matrix must never be allowed to "overwhelm the words of [an] agreement". Of paramount importance are clear words used by the parties in defining their relationship and setting out the parties' respective rights and obligations.
- [72] Here, the Subleases are clear in their terms. Southern Star granted Quest the right to use and occupy the Premises in exchange for rent. I cannot read or interpret the Subleases as characterizing rent as payment for both use and equity: *Smith Brothers Contracting* at para. 61.

- [73] As matters stand, Quest is in default under the Subleases. The rights of Southern Star, as landlord under the Subleases, are clear: the Subleases can be terminated and Southern Star can retake possession. Quest has not acquired any ownership interest in Southern Star, although I do not consider that as particularly relevant. More importantly, given the default, entirely separate persons, Attu and Holdings, are in a position to demand that the Escrowholder deliver the entirety of the Southern Star shares back to them.
- [74] I do not intend the above discussion as endorsing, as a matter of the interpretation of s. 11.01(a), that real property leases are within its purview. As stated above, no Canadian court has interpreted s. 11.01 in that fashion. Only one recent Ontario decision seems to have addressed s. 11.01(a) in the context of real property leases: Comark Holdings Inc. (Re) (June 3, 2020), Toronto CV-20-00642013-00CL (Ont. S.C.J.). However, the Ontario court did not issue any reasons so there is no indication that the court grappled with this issue.
- [75] Quest does not rely on Comark in respect of the "true lease versus financing lease" analysis, which I agree is appropriate. Quest relies on the Comark order in respect of the "use" issue, as I will discuss below.
- [76] Section 11.01(a) has been applied in the context of personal property leases only. Here, I need not decide whether real property leases also come within the purview of s. 11.01(a) and I would leave that for later determination. I conclude that, if s. 11.01(a) applies to real property leases, I do not interpret the Subleases as "financing leases" for the above reasons. I make this determination having regard to the need to interpret s. 11.01 narrowly, as discussed above.

#### ARE THE RESIDENCES BEING "USED"?

- [77] Currently, the Residences are unoccupied, save for three Quest staff members who are there mainly for security reasons. They are provided these accommodations as taxable benefits as part of their incomes.
- [78] Leaving aside the issue of whether s. 11.01(a) applies to real property leases, Quest submits that s. 11.01(a) is not engaged as Quest is not currently using the Residences (i.e. there is no "use of leased . . . property"). As a result, Quest says Southern Star is not exempt from the general stay and it is prevented from demanding the rent payments from Quest.
- [79] Quest argues that it vacated the Residences (i.e. the "Premises" under the Subleases) due to safety concerns and provincial health orders relating to the COVID-19 pandemic. Quest says that, as set out in the Subleases, it is only entitled to use the Premises for student residential housing and it cannot do so.

- [80] Quest relies on the recent initial order granted in the Comark proceedings on June 3, 2020 as supportive of its interpretation of s. 11.01(a) in these circumstances. Comark operated a number of retail stores in shopping malls across Canada. Comark was prohibited from operating these stores because of government orders issued to address the COVID-19 pandemic.
- [81] In Comark, Justice Hainey ordered that Comark was not required to pay rent for these stores until it was legally entitled to open the stores to the public for its ordinary course business operations. In granting that order, Hainey J. considered Comark's notice of application and factum and the monitor's report dated June 2, 2020. Comark argued that, since it could not legally operate the stores, there was no "use" of those stores by Comark that required rent to be paid under s. 11.01(a). Comark submitted that in the "exceptional circumstances", it was just and appropriate to grant rent relief for these stores. As stated above, unfortunately, I do not have the benefit of the court's reasoning in respect of s. 11.01(a) in granting that relief.
- [82] Very unusual circumstances were faced by Comark - and the court - at the time the initial order was granted, even beyond the effect of the Ontario government orders. It does not appear that landlords of these stores had notice of the hearing. The monitor indicated that this relief was sought for only a very limited time to allow Comark to address the issue of rent relief with the landlords.
- [83] On June 12, 2020, by the time of the comeback hearing, the landlords had weighed in and the landscape had changed substantially. The initial order was amended along the lines of the Ontario Model Order, and required payment of rent, although the landlords had agreed to a rent deferral on conditions.
- [84] In my view, at its highest, the Comark initial order must be viewed as granted under extraordinary circumstances and, apparently, on a "without notice" basis in respect of the affected parties (i.e. the landlords). I can not conclude from the order itself that the court accepted Comark's arguments with respect to s. 11.01(a). In any event, the circumstances here are distinguishable.
- [85] I do not quarrel with Quest's decision to move to online learning in mid-March 2020. However, as the BC government's counsel points out, Quest made that decision even before the BC government announced the state of emergency.
- [86] Quest has not referred me to any BC government or health officer order that would have prevented Quest's students from remaining in the Residences from that time. The reason why most students left is clear: Quest decided to move to online learning that did not require students to be physically present in the Residences to attend classes. Quest's counsel concedes that no BC government or health officer order precluded Quest from using the Premises.

[87] In addition, even accepting that the clearing out of the Residences in March 2020 arose from the COVID-19 pandemic, Quest's "use" of the Residences over the summer months (June-August) has not materially changed from years past. The evidence is that, over the summer, some Quest students remain on campus (while paying rent) and Quest rents out some accommodations to third parties. I am not aware of any reason why students - or third parties - could not reside in the Residences now.

[88] In addition, I do not equate a lack of physical occupation of the leased premises by students with a lack of "use".

[89] Dictionary definitions of "use", both as a noun and verb, are instructive and indicate an expansive meaning:

Black's Law Dictionary (10th ed.):

Noun: The application or employment of something; esp., a long-continued possession and employment of a thing for the purpose for which is adapted, as distinguished from a possession and employment that is merely temporary and occasion

Verb: To employ for the accomplishment of a purpose; . . .

Oxford English Dictionary (6th ed.):

Noun: 1 The action of using something; the fact or state of being used; application or conversion to some purpose ... 5 The opportunity, right or power of using something 7 Make use of (a thing), esp. for a particular end or purpose, utilize, turn to account :

[90] I conclude that Quest is "using" the Residences within the meaning of s. 11.01(a):

- a) Quest is allowing some staff members to reside there;
- b) Quest is asserting, as against Southern Star, its landlord, sole possession of the Residences, in accordance with its right to quiet enjoyment of the Residences under the Subleases. In other words, Quest is exercising its right to "use" the Residences, as intended;
- c) Certainly as early as June 2020, Quest was more than able to populate the Residences with students or other persons, just as they have done in past summers; I do not view this use over the summer months as being inconsistent with the stated and permitted use of the Premises under the Subleases;
- d) As of June and continuing into July and August 2020, the principal reason why the Residences are vacant is no different from previous summers. In previous summers, Quest continued to pay rent to Southern Star since it was still "using" the Residences under the terms of the Subleases; and

- e) Quest has not seen fit to disclaim the Subleases. To the contrary, Quest's evidence is that the Residences are very important and it must maintain them to further the possible restructuring options available to them, as discussed above. The existence of the Residences, and Quest's rights under the Subleases, remain a key selling point in relation to potential partners.
- [91] With respect to the latter point above, Southern Star's reliance on Allarco Entertainment Inc. (Re), 2009 ABQB 503 is apt. In the CCAA proceedings, the debtor applied for an order imposing different payment terms for certain TV programming. The debtor sought payment terms tied to its "use" of the programming based on what was actually played by its customers, contrary to the licensing terms.
- [92] In Allarco, Justice Veit declined to order different payment terms. At paras. 36 and 55, the court noted that the debtor continued to advertise the availability of the programming; therefore, the debtor was using the licensed property. The court declined to vary the payment terms agreed to by the parties, citing Boutiques San Francisco: paras. 50-54.
- [93] In my view, similar reasoning applies in the present case. Residing on campus is an integral part of Quest's program that Quest continues to market. While students are not physically occupying units in the Residences over the summer months, Quest continues to utilize or "use" the Premises under the Subleases over that time, in a fashion just as the parties intended. To allow this rent deferral would amount to the Court imposing different payment terms on Southern Star, which is inappropriate.

## CONCLUSION

- [94] I acknowledge that, to date, Quest has attempted, in good faith, to resolve its funding issues. I also accept, without hesitation, that by deferring rent payments to Southern Star, Quest's cash flow needs would lessen and enhance the prospects of a successful restructuring.
- [95] Efforts on Quest's part have included seeking out whatever governmental assistance was available arising from the COVID-19 pandemic. At one point, the Canada Emergency Commercial Rent Assistance program seemed a promising solution; however, Quest did not qualify since the rental amounts for each of the Residences exceeded \$50,000 and tenants in CCAA proceedings were disentitled from receiving any rent relief.
- [96] What remains a somewhat open question, however, is the matter of the financing of Quest's operations during the restructuring. Quest has known since the outset that it required interim financing to continue in the restructuring. It sought further funding as required, including the increase approved in late May 2020. It is unclear to me whether Quest has sought further financing that would allow payment for the rent amounts. Quest's evidence is silent on the point. The Monitor also does not address that issue, beyond noting that the cash flow does not include those rent payments because Quest "suspended" the monthly payments.

- [97] Fairness is a common touchstone in CCAA proceedings. In *Century Services Inc. v. Canada (Attorney General)*, 2010 SCC 60, the Court stated:
- [70] . . . 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.
- . . .
- [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.
- [98] As stated above, it is commonly considered "fair" that a person continuing to supply an insolvent debtor or allow the debtor to continue using its property during the restructuring should also be compensated for that supply or use, consistent with Model Orders in place across Canada: *Cow Harbour Construction* at para. 16.
- [99] In my view, significant indicia of unfairness arise by allowing the rent deferral.
- [100] Quest's request is not for a very short time (like *Comark*); rather, it is for a longer period (three months) and with no real end date. The result of this deferral would be to require that Southern Star become an unsecured creditor of Quest through the means of this restructuring. The resulting debt is large - some \$720,000 (subject to receipt of the funds held by the Monitor for June). The deferral would mean significant negative consequences to Southern Star, likely BMO taking default proceedings under its security. There are other participants who are supporting Quest in this restructuring proceeding by provided financing and ongoing supply; however, Quest has offered these participants protection in relation to any resulting debt - and the Court has granted that protection - in respect of that accommodation. No such protection - or even compensation for the delay in payment - has been offered to Southern Star; effectively, a deferral would expose Southern Star to significant risk and loss if the CCAA restructuring should fail.
- [101] There is a definite benefit to the stakeholders by allowing the rent deferral. No doubt, Vanchorverve Foundation, a major secured creditor, recognized this in indicating its support for Quest on this application. I fail to see why Southern Star (and indirectly, BMO) should bear substantial risk and loss to allow all of the other stakeholders to enjoy this benefit. It is, in my view, manifestly unfair.
- [102] I accept that I have the discretion to allow Quest to choose or not choose to pay the rent. However, I do not have the discretion to prevent Southern Star from demanding payment and taking steps to address any default. In light of Quest's true aim in bringing this application, it is appropriate that the ARIO continue to require that Quest pay the rent payments to Southern Star.
- [103] In all the circumstances, I do not consider that the rent relief sought is appropriate. Quest's application is dismissed.

"Fitzpatrick J."

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