Court File No. CV-14-10518-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE - COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF THE CASH STORE FINANCIAL SERVICES INC., THE CASH STORE INC., TCS CASH STORE INC., INTSALOANS INC., 7252331 CANADA INC., 5515433 MANITOBA INC., 1693926 ALBERTA LTD. DOING BUSINESS AS "THE TITLE STORE"

APPLICANTS

BOOK OF AUTHORITIES OF THE MOVING PARTY, 0678786 B.C. LTD. (FORMERLY THE MCCANN FAMILY HOLDING CORPORATION)
(returnable June 11, 2014)

VOLUME 1 OF 2

Dated: May 30, 2014

BENNETT JONES LLP
One First Canadian Place
Suite 3400, P.O. Box 130
Toronto, Ontario
M5X 1A4

Robert W. Staley (LSUC #27115J)
Raj Sahni (LSUC #42942U)
Gannon Beaulne (LSUC #63948V)

Tel: 416-777-4856
Fax: 416-863-1716

Lawyers for the 0678786 B.C. Ltd.

TO: THE SERVICE LIST

Party/Counsel	**Telephone**	**Facsimile**	**Party Represented**
Lax O'Sullivan Scott Lisus LLP Suite 2750, 145 King Street West Toronto, ON M5H 1J8 Canada Eric R. Hoaken Email: ehoaken@counsel-toronto.com **JJS Barristers** Suite 800, The Lancaster Building 304 - 8 Avenue SW Calgary, Alberta T2P 1C2 Canada Robert Hawkes, Q.C. Email: hawkesr@jssbarristers.ca	416.598.1744 416.645.5075 403.571.1544	416.598.3730 403.571.1528	Counsel for DirectCash Bank, DirectCash ATM Processing Partnership, DirectCash ATM Management Partnership, DirectCash Payments Inc., DirectCash Management Inc. and DirectCash Canada Limited Partnership ("DirectCash") who are co-defendants with The Cash Store Financial Services Inc. and The Cash Store Inc. (the "Cash Store") in class action (Court File No. 7908/12CP)
Osler Hoskin & Harcourt LLP P. O. Box 50, 1 First Canadian Place Toronto ON M5X 1B8 Marc Wasserman Email: mwasserman@osler.com Jeremy Dacks Email: jdacks@osler.com Patrick Riesterer Email: priesterer@osler.com Karin Sachar Email: ksachar@osler.com	416.362.2111 416.862.4908 416.862.4923 416.862.5947 416.862.5949	416.862.6666	Counsel to the Chief Restructuring Officer ("CRO")
Rothschild Neil Augustine Email: nycprojectoilers@rothschild.com Bernard Douton Email: nycprojectoilers@rothschild.com	212.403.3500 212.403.5411 212.403.5254	212.403.3501	Financial Advisors to the CRO

Party/Counsel	Telephone	Facsimile	Party Represented
Cassels Brock & Blackwell LLP 2100 Scotia Plaza, 40 King Street West Toronto, Ontario M5H 3C2 Wendy Berman Email: wberman@casselsbrock.com Ryan C. Jacobs Email: rjacobs@casselsbrock.com	416.869.5300 416.860.2926 416.860.6465	416.640.3107 416.640.3189	Counsel to the Applicants
FTI Consulting Canada Inc. TD Waterhouse Tower 79 Wellington Street West Suite 2010, P.O. Box 104 Toronto ON M4K 1G8 Greg Watson Email: greg.watson@fticonsulting.com Jeff Rosenberg Email: jeffrey.rosenberg@fticonsulting.com	416.649.8077	416.649.8101	Monitor
McCarthy Tétrault Suite 5300, TD Bank Tower Box 48, 66 Wellington Street West Toronto ON M5K 1E6 James Gage Email: jgage@mccarthy.ca Heather Meredith Email: hmeredith@mccarthy.ca	416.362.1812 416.601.7539 416.601.8342	416. 868.0673	Counsel to the Monitor
Goodmans LLP Bay Adelaide Centre 333 Bay Street, Suite 3400 Toronto ON M5H 2S7 Robert J. Chadwick Email: rchadwick@goodmans.ca Brendan O'Neill Email: boneill@goodmans.ca	416. 979.2211 416.597.4285 416.849.6017	416. 979.1234	Counsel to Ad Hoc Noteholders
Norton Rose Fulbright Canada LLP Suite 3800, Royal Bank Plaza, South Tower 200 Bay Street, P.O. Box 84 Toronto, ON M5J 2Z4 Orestes Pasparakis Email: orestes.pasparakis@nortonrosefulbright.com	416.216.4000 416.216.4815 416.216.4805 416.216.4853 416.216.2419	416.216.3930	Counsel to Coliseum Capital Management

Party/Counsel	Telephone	Facsimile	Party Represented
Alan Merskey Email: Alan.Merskey@nortonrosefulbright.com Virginie Gauthier Email: virginie.gauthier@nortonrosefulbright.com Alex Schmitt Email: alexander.schmitt@nortonrosefulbright.com			
McMillan LLP Brookfield Place, 181 Bay Street, Suite 4400 Toronto, ON M5J 2T3 Adam C. Maerov Email: adam.maerov@mcmillan.ca Brett Harrison Email: brett.harrison@mcmillan.ca	403.531.4700 403.215.2752 416.865.7932	416.865.7048	Counsel to Trimor Annuity Focus LP #5
Computershare Trust Company of Canada and Computershare Trust Company, NA 100 University Avenue, 11th Floor, North Tower Toronto, ON M5J 2Y1 Patricia Wakelin, Corporate Trust Officer Email: patricia.wakelin@computershare.com Shelley Bloomberg, Manager, Corporate Trust Email: Shelley.Bloomberg@computershare.com Mohanie Shivprasad, Associate Trust Officer Email: mohanie.shivprasad@computershare.com Tina Vitale, Senior VP, Corporate Trust Email: tina.vitale@computershare.com John Wahl, Corporate Trust Officer Email: john.wahl@computershare.com	416.263.9317 416.263.9322 212.805.7345 646.334.3350 (C) 303.262.0707	416.981.9777 514.981.7677	Collateral Trustee under the Collateral Trust and Intercreditor Agreement
Dickinson Wright LLP 199 Bay Street, Suite 2200 Commerce Court West Toronto, ON M5L 1G4 Michael A. Weinczok Email: mweinczok@dickinsonwright.com David P. Preger Email: Dpreger@dickinsonwright.com	416.777.4026 416.301.4883 (C) 416-646-4606	416-865-1398	Canadian Counsel to Computershare
Perkins Coie LLP 30 Rockefeller Plaza 22nd Floor New York, New York 10112-0085 United States of America Tina N. Moss Email: TMoss@perkinscoie.com Ronald T. Sarubbi	212.262.6910 212.262.6914	212.977.1648 212.977.1644	US Counsel to Computershare

Party/Counsel	Telephone	Facsimile	Party Represented
Email: RSarubbi@perkinscoie.com			
Borden Ladner Gervais Centennial Place, East Tower 1900 520 – 3rd Ave SW Calgary, AB, T2P 0R3 Josef G.A. Kruger Email: jkruger@blg.com Patrick T. McCarthy Email: PMcCarthy@blg.com	403.232.9500 403.232.9563 403.232.9441	403.266.1395	Counsel to the Trustee in Bankruptcy for Assistive Financial Corp.
Duncan Craig LLP 2800 Scotia Place 10060 Jasper Avenue Edmonton, Alberta T5J 3V9 Darren R. Bieganek, Q.C. Email: dbieganek@dcllp.com	780.428.6036 780.441.4386	780.428.9683 780.969.6381	Counsel to Mr. Cameron Schiffner
Harrison Pensa LLP 450 Talbot Street London, ON N6A 5J6 Jonathan Foreman Email: jforeman@harrisonpensa.com **Koskie Minsky LLP** Barristers & Solicitors 20 Queen Street West, Suite 900 Toronto, ON M5H 3R3 Andrew J. Hatnay Email: ahatnay@kmlaw.ca	519. 679.9660 519.661.6775 416.595.2083	519.667.3362 416.204.2872	Counsel to the Plaintiff in the class action of Timothy Yeoman v. The Cash Store Financial Services Inc. et al. (Court File No. 7908/12CP) Agent to Plaintiff's Counsel in class action (Court File No. 7908/12CP)
Siskinds LLP 100 Lombard Street, Suite 302 Toronto, ON M5C 1M3 Canada Charles M. Wright Email: charles.wright@siskinds.com Serge Kalloghlian Email: serge.kalloghlian@siskinds.com Alex Dimson Email: alex.dimson@siskinds.com	416.362.8334	416.362.2610	Lawyers for an Ad Hoc Committee of Purchasers of the Applicant's Securities, including the Representative Plaintiff in the Ontario Class Action against the Applicant

Index

Court File No. CV-14-1051800CL

ONTARIO
SUPERIOR COURT OF JUSTICE - COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF THE CASH STORE FINANCIAL SERVICES INC., THE CASH STORE INC., TCS CASH STORE INC., INTSALOANS INC., 7252331 CANADA INC., 5515433 MANITOBA INC., 1693926 ALBERTA LTD. DOING BUSINESS AS "THE TITLE STORE"

INDEX

---

9. *Verdellen v Monaghan Mushrooms Ltd*, 2011 ONSC 5820, 207 ACWS (3d) 553 (Sup Ct).

10. *Re Dilollo*, 2013 ONSC 578, 97 CBR (5th) 182 (Sup Ct), aff'd 2013 ONCA 550, 117 OR (3d) 81.

11. *Keith G Collins Ltd v Canadian Imperial Bank of Commerce*, 2011 MBCA 41, 268 Man R (2d) 30.

12. *Re Holt Motors Ltd* (1966), 57 DLR (2d) 180, 56 WWR 182 (Man QB).

13. *Thorne Riddell v Fleishman,* 47 CBR (NS) 233, 1983 CarswellOnt 201 (Sup Ct).

14. *Touche Ross Ltd v Weldwood of Canada Sales Ltd*, 48 CBR (NS) 83, 1983 CarswellOnt 214 (SC).

15. *Re AR Colquhoun & Son Ltd*, [1937] WWR 222, 18 CBR 124 (Sask KB).

16. *Re Norris* (1994), 23 Alta LR (3d) 397, 28 CBR (3d) 167 (QB), rev'd on other grounds (1996), 45 Alta LR (3d) 1, 193 AR 15 (CA).

17. *Skalbania (Trustee of) v Wedgewood Village Estates Ltd* (1988), 31 BCLR (2d) 184, 70 CBR (NS) 232 (SC), aff'd (1989), 37 BCLR (2d) 88, 60 DLR (4th) 43 (CA), leave to appeal to SCC ref'd (1989), 40 BCLR (2d) xxxiii (note), 62 DLR (4th) viii (note) (SCC).

18. *Conte Estate v Alessandro*, 2002 CarswellOnt 4507, [2002] OJ No 5080 (Sup Ct).

19. *Re Fancy* (1984), 46 OR (2d) 153, 8 DLR (4th) 418 (SC).

20. *Boudreau v Marler*, 18 RPR (4th) 165, 48 CBR (4th) 188 (CA).

VOLUME 2

21. *Montor Business Corp (Trustee of) v Goldfinger*, 2013 ONSC, 237 ACWS (3d) 296.

22. *Robinson v Countrywide Factors Ltd* (1977), [1978] 1 SCR 753, 72 DLR (3d) 500.

23. *Re Garrett*, 30 CBR (NS) 150, 1979 CarswellOnt 195 (SC).

24. *Indcondo Building Corp v Sloan*, 2010 ONCA 890, 103 OR (3d) 445.

25. *Oliver v McLaughlin*, 24 OR 41, [1893] OJ No 11 (CA).

26. *Bank of Montreal v Peninsula Broilers Ltd*, 177 ACWS (3d) 405, 2009 CarswellOnt 2906 (Sup Ct).

27. *Dapper Apper Holdings Ltd v 895453 Ontario Ltd* (1996), 38 CBR (3d) 284, 11 PPSAC (2d) 284 (Gen Div).

28. *Burton v R & M Insurance Ltd* (1977), 5 Alta LR (2d) 14, 9 AR 589 (SC TD).

29. *Alberta (Director of Employment Standards) v Sanche*, 134 AR 149, 5 Alta LR (3d) 243 (QB).

30. *Dwyer v Fox*, 190 AR 114, 43 Alta LR (3d) 63 (QB).

31. *Taylor & Associates Ltd v Louis Bull Tribe No 439*, 2011 ABQB 213, 46 Alta LR (5th) 182.

32. *Maki Megbiz, KFT v Osprey Energy Ltd*, 2006 ABQB 630, 405 AR 165 (Master).

33. *Re Canwest Publishing Inc/Publications Canwest Inc*, 2010 ONSC 222, 184 ACWS (3d) 684.

Tab 1

1911 CarswellOnt 733
Supreme Court of Canada

Clarke v. Baillie

1911 CarswellOnt 733, 45 S.C.R. 50

Rose A. Clarke (Plaintiff), Appellant and Frank W. Baillie and others (Defendants), Respondents

Sir Charles Fitzpatrick C.J. and Davies, Idington, Duff and Anglin JJ.

Judgment: November 24, 1910
Judgment: October 3, 1911

Proceedings: affirming *Clarke v. Baillie* (1910), 1910 CarswellOnt 134, 20 O.L.R. 611, 15 O.W.R. 691 ((Ont. C.A.)); refused leave to appeal *Clarke v. Baillie* (1911), 45 S.C.R. vii ((Ontario P.C.))

Counsel: *Nesbitt K.C.* and *Wood* for the appellants.
Hellmuth K.C. and *Long* for the respondents.

Subject: Securities; Property; Contracts; Corporate and Commercial

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bailment and Warehousing --- Pledge or pawn — Relationship between pledgor and pledgee — Rights of pledgor — Miscellaneous rights

Where pledgee has repledged.

Where the pledgee repledges the security for a larger amount than his loan to the pledgor, before the loan is due, the pledgor is not entitled to reclaim the security pledged by him until he has paid the debt to the pledgee, notwithstanding the pledgee's violation of his duty.

Securities and Commodities --- Broker and customer — Contract — Custom and usage

Use of American sources as to laws, custom and usage.

Per Anglin J.: "It is common knowledge that the business of stockbrokers in this country is conducted in a manner more closely resembling that which prevails in the United States, and particularly in the State of New York, than that which

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

obtains in England. Many customs and usages of English brokers are unknown in Canada; and many practices prevalent in our markets, which have come to us from the United States, would not be recognized on the London Stock Exchange. For this reason, and also because of a dearth of English authority (see R. 70 of the London Stock Exchange, Stutfield, 3rd ed., p. 45) I have drawn for authorities, perhaps more freely than is usual in our Courts, upon American sources.".

Securities and Commodities --- Margin transactions — Pledging of customer's securities — Conversion

A broker has the right to hypothecate his client's stock for an amount not in excess of what is owing on that stock. Where the stock is pledged for a greater amount but the broker is at all times able to deliver the stock to the client upon payment of the amount due, in accordance with the usage and custom of brokers, known to the client, he may not be liable for conversion. Plaintiff instructed defendant broker to buy certain stocks for her on margin. Defendant carried out these instructions, and, while holding the stocks pending the payment of the amount remaining due on the price, pledged the stocks together with other stocks, for a sum larger than that owing by plaintiff. Subsequently plaintiff paid the amount remaining due, and her stocks were promptly delivered to her. Upon learning of defendant's dealing with her stocks, plaintiff brought an action for conversion. Held, plaintiff could not succeed. She was well aware of the custom of brokers to pledge stocks held by them on margin, and defendant had done nothing not permitted by the tacit contract between the parties. Even assuming there had been a conversion, plaintiff had suffered no damage thereby. Per Fitzpatrick C.J. : "The purchase of stock on margin through a broker necessarily involves an advance by the latter of a sum which added to the amount of the margin put up by the customer will be sufficient to enable the broker to pay for the stock. It is proved beyond doubt that to procure this money the broker is entitled, according to the well established usage of the stock exchange both in Toronto and New York, to re-pledge en bloc the stock bought by him on margin." Per Duff J.: "In each of the bought notes sent to her [appellant] there is an intimation in these words: `When carrying stocks for customers, we reserve the right of pledging the same or raising money upon them in any way most convenient to us.' This, she says, was not brought to her attention, but, I think, a person who, having instructed a broker to buy stocks and carry them, receives a notice of this kind and does not read it, must be taken in respect of subsequent dealings to assent to any reasonable terms it may contain to the same extent as if he had read it and taken no exception to it. Now, in my view, this intimation is a plain warning that the arrangement with the broker involves the right to use the stocks purchased as security in accordance with the reasonable practice in such transactions among reputable brokers in Toronto and New York; and I do not see how after reading it and acquiescing in it the client could be heard to object to the use of them in the same way in which stocks carried `on margin' were being generally dealt with. I do not think ordinary people reading such a notice would take it to refer only to the broker's interest as mortgagee; that I think is too much of a lawyer's refinement. I think most people would assume that it meant something more than the mere statement of the fact that the broker would exercise the legal right to hypothecate his own interest in the securities referred to.".

***The Chief Justice*:**

1 I have no doubt that this appeal should be dismissed. The appellant brought an action to recover from the respondents damages for breach of an agreement to purchase for her certain shares of stock in these circumstances: —

2 The appellant is a spinster admittedly familiar with the usages and practice of the stock market and the respondents are brokers and members of the Toronto stock exchange. Instructions to purchase on margin a certain number of shares of Sao Paulo and of Louisville and Nashville stock were given verbally by the appellant and when the orders were executed a notice called a bought note was sent to her in each case to inform her that her order was executed and setting forth the conditions subject to which the purchase was made.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

3 The purchase of stock on margin through a broker necessarily involves an advance by the latter of a sum which added to the amount of the margin put up by the customer will be sufficient to enable the broker to pay for the stock. It is proved beyond doubt that to procure this money the broker is entitled, according to the well established usage of the stock exchange both in Toronto and New York, to re-pledge *en bloc* the stock bought by him on margin. To enable this repledging to be done in a way most advantageous for both parties and to avoid all misunderstanding as to the authority of the broker, this term was inserted in all the bought notes: —

> When carrying stocks for clients, we reserve the right of pledging the same or raising money upon them in any way most convenient to us.

4 It is admitted that the broker did in the case of each purchase make the necessary advances for his customer, the appellant; but the latter contends that while the broker had the stocks in his possession they were pledged by him to raise a sum of money in excess of what was then due to him by her with respect to each block of stock and that such a dealing constituted a conversion of the stocks to his own use and that he must account for their full value at that date notwithstanding that he acted in perfect good faith.

5 There can be no doubt, as both parties admit, that the broker had the right to hypothecate the stock of his client so long as he did not pledge it for an amount in excess of what was due him by the client in connection with the purchase and the trial judge finds as a fact

> that the stock which was for a good deal of the time unpledged was never at any time pledged by the respondents beyond the amount due them by the appellant for that portion of the purchase made which they had advanced.

6 If not sufficient to justify this finding which, of course, puts an end to the plaintiff's claim the evidence is very conclusive that the brokers had at all times control over the stock and could deliver it to the appellant, as they did on her first demand, on payment of the amount due on each purchase. When she did ask for delivery of the stocks the certificates were partly in respondents' vaults and partly in the possession of their agents in New York, subject to their order; and her directions with respect thereto were immediately complied with and the stocks were never at any time dealt with by the brokers to the damage of the appellant and to the profit of the respondents. On the contrary it is clear on every line of the evidence that the brokers acted with the utmost good faith, in strict accordance with the usages and customs known to the appellant and with reference to which she is properly presumed to have made her contract.

7 I would dismiss with costs.

***Davies J.*:**

8 I am of opinion that this appeal should be dismissed upon the ground that there was no evidence whatever that the plaintiff (appellant. had sustained any loss by reason of the alleged conversions of her stock of which she complains.

9 The respondents were brokers and had purchased stock for the appellant on the margins advanced for the purpose by the appellant. They had pledged this stock so purchased together with other stock of other clients with one of the banks not only to raise the difference between the margins put up by the appellant and the purchase price of the stocks, but also to cover their

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

general indebtedness to the banks which was, of course, much greater than the sum owing to them upon the appellant's stock. The appellant contends that the manner in which the pledge was made constituted in law a conversion of her stock and entitled her to recover the damages she claimed.

10 The facts proved shewed that the alleged conversion was in accordance with the ordinary practice of the respondent brokers in their dealings with the banks respecting the hypothecation by them of stocks of their customers, and that although they had hypothecated the appellant's stock or shares together with other stocks for a sum of money greatly in excess of the amount owing by the plaintiff on her stock, the moment she demanded her stock her demand had been complied with and her stock duly transferred to her, accepted by her and then sold by her. The alleged conversion by the improper manner of hypothecating the shares brought no profit to the brokers nor any loss to the appellant. It was not till long afterwards that plaintiff brought her action.

11 On the ground, therefore, that although the brokers were not under the terms of their contract with the appellant as I construe it justified in pledging her shares in the manner they did, yet as they delivered the shares to the appellant immediately she demanded them and that she did not suffer any damage whatever from the alleged impropriety I think this action cannot be sustained.

12 Owing to some observations made in the reasons for judgment of the Court of Appeal I think it desirable to say that further argument of the question of the legal meaning of the foot-note to the bought and sold notes of the brokers under which they claimed the right to hypothecate these shares for a larger sum than was due to them upon the shares by their owner has not tended to weaken or alter the opinion I expressed with regard to its meaning in the case of *Conmee v. Securities Holding Co.*[1] , namely, that its language does not justify the broker in pledging the shares for a sum greater than that due from the customer to him.

13 I would dismiss the appeal with costs.

***Idington J.*:**

14 The respondents contracted with the appellant to purchase and carry for her certain stocks. In the course of the business she claims they had pledged or hypothecated such stocks in such a way that she is entitled to charge against them the then market value of said stocks, though much depreciated in value when she received a transfer to her of said stocks or the like stocks and disposed of them, and hence suffered loss.

15 I am somewhat at a loss to know exactly on what legal grounds the claim is put.

16 If we are to treat the stocks in question as transferable in such a way that they can be looked upon as chattels susceptible of conversion for which an action of trover would lie and this as if such an action, we are met with the legal difficulty that it has always been competent for the court in an action of trover to stay the proceedings for damages upon a delivery up of a chattel.

WestlawNext® CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

17 That is what has happened by the act of the parties, and how can damages rest on that ground?

18 It has sometimes been competent for the owner of the chattel wrongfully converted, to waive the tort and sue for price or proceeds of goods and recover. This option could only be exercised upon the complete abandonment of any right to, or interest in, the chattel, which is impossible on the facts here.

19 In either of such alternatives as I present, the property in the thing in question is presumed in law to have become by the judgment of recovery, vested in the wrongdoer or party meddling with another's property. Hence no such ground of action is conceivable here.

20 Again, trusteeship is spoken of as a possible ground. How it can be invoked in such a case or made to operate is unexplained. Even if so a trustee having power of disposal pretending to exercise it by a circuitous method so that he ultimately becomes apparent owner as result of such transactions, has been held bound at the option of the *cestui qui trust* to account upon the footing of his alleged sale or whilst being tentatively held thereto to have the property put up for sale and the chances of a better bid being got given the *cestui que trust* . See *Ex parte Hughes*[2] (1802), and *Ex parte Lacey*[3] (1802).

21 Short of some such situation as that, I know of no legal principle upon which the courts have ever acted to charge a trustee or agent improperly dealing with the trust estate with the value thereof; unless same or part thereof, debited has been lost as the result of such improper dealing.

22 The evidence in this case falls short of anything in any of these conceivable cases.

23 I am also unable to understand how our decision in the *Conmee Case*[4] has any bearing on the issues raised herein.

24 I would not for a moment say a word to weaken what we held in so plain a case as that was. Yet even if appellant had before accepting delivery to her of the stocks in question, made her alleged discovery of the facts herein relative to the pledging or hypothecation of the stocks in question and sought to make respondents responsible therefor, I would not be quite sure that she had brought herself within the said decision.

25 The hypothecation or pledging of the property of another beyond what that other authorizes, may have in many ways serious results that are not apparent in this case where no damages are shewn to have in fact resulted from the act complained of.

26 Again it is claimed as to the stock bought in New York that in fact there never was a purchase of that stock. The learned trial judge found that there was in fact such a purchase. The Divisional Court in appeal therefrom, also found there was such a purchase.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

27 Though not expressly dealing with the point the Court of Appeal for Ontario must also be taken to have held the same way.

28 It is too late for us to reverse such findings of fact on such conflicting evidence as exists herein.

29 The utmost that can be said with a full assurance that we are not infringing upon the rule as to concurrent finding of fact by courts below is this, that the stock alleged to have been purchased in New York, passed by reason of some sort of understanding between the respondents and their New York agents, into a body of mingled securities pledged or hypothecated for a very large balance due from respondents to their New York agents in respect of similar transactions.

30 Now I am not at all prepared to hold that a broker in Toronto retained to buy stocks in New York, has completely executed the business entrusted to him, when he has by the same act of buying so called, so bound the alleged purchase as to subject it to the common charge (exceeding his advance in the purchase) covering it and many others.

31 It is idle to speak of the other securities being ample, or the personal credit of the broker in New York being ample, so long as the charge exceeds the value of the stock presumed to have been bought.

32 Nor am I disposed to stretch the implied authority, which may exist as suggested in the Court of Appeal, even if known and so recognized amongst brokers in Toronto, as to be binding upon each other or members of the Stock Exchange, to cover the duty arising towards a person ignorant thereof, when the broker is retained merely to purchase in New York, even when coupled with an agreement to advance part of the price.

33 I think this case must be disposed of by strict attention to the nature of the contract between the parties and the consequences of some breach thereof. In doing so I desire not to be misunderstood as accept ing without limitation either what has been held in the court below, or been contended for here and probably there, and hence my taking trouble to explain (by what I have said) in advance, what I am about to say.

34 The contract seems accurately stated in the following evidence of one of the respondents: —

> 249. Q. — The contract was that she was to pay 15% or 20% of the par value of the stock, and you were to pay the balance to purchase it, and the stock was to be pledged to you for the amount you put up, and she was to keep her margin up according to the fluctuations of the market, — was that the contract between you? A. — Yes, that is the contract; there was no written contract.

35 I do not think such a contract warrants the broker acting upon it either pledging or hypothecating the stock purchased pursuant thereto, for any greater sum than he has advanced together with the interest and commission due him.

36 Nor, to guard myself by repeating what I have said already relative to New York, do I think that if the purchase and

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

this unwarranted pledging or hypothecating are, as they may be in a given case such as that of the dealing in Sao Paulo stock in question, part and parcel of the same transaction, that the broker has executed his contract to purchase.

37 It is not clear exactly how that was in this case. It is tolerably clear, however, that in the many changes involved here there must have been a time when the contract of purchase was executed by the terms of the pledge or hypothecation having been so expressed as to enable the shares in question to have been as of right withdrawn upon payment of the sum due from appellant to respondent.

38 It is, moreover, absolutely clear that the stocks were on demand of the appellant freed from any charge and immediately transferred to her upon her paying the amounts due.

39 The purchase the respondents were retained to make must then at all events have been fully executed, and I fail to see how thereafter she can, under the circumstances, now be heard to say the contrary, especially in the absence of any tender back of that which she got.

40 Now assume for argument's sake, that the respondents exceeded in any way by unauthorized pledging or hypothecating the limits of their legal rights, and even have thereby improperly jeopardized the appellant's property and her interests in question relative thereto, how can she on the facts claim she was damnified? No damage is shewn. No case is made shewing such damages. If her pleadings might cover nominal damages that is not what has been thrashed out in the long drawn out contest.

41 And if it ever was open to the appellant to rest upon such a case, the facts have been so held by the courts below, and the nature of the contest has been throughout so entirely distinct from such a consequence, that I do not think we can now reverse on such technical grounds, all that has passed in the courts below.

42 Although a case may be conceivable of transactions of such magnitude as to effect by such methods as in question the value of the stocks in the market, no evidence here shews such results to have taken place.

43 I may remark that though I have used purposely in order to cover briefly all points of view, the terms pledging or hypothecating as possibly conceivable relative to what was done, I by no means overlook the widely different legal meanings of the words, and in some cases, legal results, of improperly dealing with property subject thereto, or made the subject thereof.

44 In common parlance, and as used for convenience sake in argument the terms are loosely treated as interchangeable, though not so.

45 It so happens here I simply have to solve a legal problem arising in this case which must be solved in the same way, whether or not the thing known as stocks herein, or the evidence thereof, can be properly spoken of as subject matter of a pledge.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

46 In the absence of fraud and having regard to the good faith of respondents, however mistaken in my view of their legal rights, I see no conceivable ground of action beyond breach of contract.

47 One question yet remains and that is the minor one of the one-half per cent. interest charged beyond the rate the brokers were paying. The contract is not clear, but the conduct of the parties makes it clear. She was told from time to time what interest was being charged. Unless the relation of principle and agent excludes the right to charge more than paid, the contract, or that and the conduct of the parties, forbids complaint.

48 The relation created by this contract is not one purely of principal and agent. It involves much more and thereby to my mind excludes in the absence of any countervailing facts and circumstances reducing it to that simple relation the application of the principles of law prohibiting an agent from making a profit unassented to by the principal.

49 I think the appeal must be dismissed with costs.

Duff J.:

50 I think the appeal should be dismissed. I should not have thought it necessary to add anything to the reasons given by the learned judges who have dealt fully with the questions involved in the court below were it not for the difference of opinion in this court and the circumstance that the decision of the Court of Appeal (it is argued) is in some way inconsistent with the decision of this court in *Conmee v. The Securities Holding Co.*[5] .

51 There are several grounds upon which I think the plaintiff's action must fail.

52 The evidence shews very clearly, I think, that both in New York and Toronto there is a well understood and well defined usage among brokers who buy and carry stocks for customers "on margin" to repledge or hypothecate such stock *en bloc* for the purpose of raising the funds necessary to meet the obligations incurred by them in the transactions they have executed or undertaken to execute.

53 It was stated at the trial by Mr. E.B. Osler that this practice is advantageous to the customer because it enables the broker to borrow money at a lower rate. That it is a reasonable practice is shewn, first, by the fact of its general adoption in the two places mentioned, and secondly, by the circumstance that in the State of Massachusetts almost without exception and on the London Stock Exchange in the vast majority of cases such transactions are treated as executory agreements for the sale by the broker to the customer at the price at which the stocks are purchased plus a charge for interest and the broker so long as he carries the stocks is entitled to deal with them as owner. In *Bentinck v. London Joint Stock Bank*[6] the subject was dealt with by North J. who sums up the evidence given in that case at pp. 140 and 141 thus: —

> Now the evidence as to "contango" transactions is this — I am only giving a short *résumé* so far as it is now material — when a client directs a broker to buy stock for which the client is not himself finding the money to pay at the time, the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> money is provided by the broker, and he borrows the money for the purpose. This is done sometimes, no doubt, by a pure and simple loan; but in a very large majority of cases, amounting, according to the evidence of Mr. Grant, the official assignee of the Stock Exchange, to sixteen-twentieths of the whole business on the Stock Exchange, and, according to Mr. Powell's evidence, to nineteen-twentieths of the whole business, the thing is done by the broker finding the money on "contango," and then what happens is this: he is treated, not as the mortgagee or pledgee of the shares for the money which he advances, but he becomes by contract the purchaser of the shares out and out, and they become his own property. The shares are not yet transferred to him — he does not acquire any legal interest in them; but, as between the client on whose account he has bought them on the one hand, and himself on the other, when he finds the money on "contango" he becomes the absolute owner of the property, subject, however, to a contract made at the same time, or part of the same contract, that he is to re-sell to the client a like amount, not the same identical shares, but a like amount of similar shares, usually on the next account day, although a later day may be fixed by arrangement, at a price larger than that for which he gave his client credit on the first occasion; because the enhanced price is to cover interest upon the money in the meantime. Therefore, in fact, these "contango" transactions, although they are constantly treated as loans of money, even by persons who are thoroughly familiar with the business, although they are popularly spoken of, even on the Stock Exchange and by members of the Stock Exchange, when they come before the Court, as loans, yet, when the transaction is regarded from a legal point of view, it is not a loan on the client's security, but is a sale by which the broker becomes entitled to the security as his own, although he is subject to a contract to re-sell to the client, not the same, but an equal amount of similar shares or stocks at a future date. In all these transactions, therefore, when money is borrowed from a stockbroker on "contango" or "continuation," whether the money is obtained from the dealer or from other stockbrokers, or from bankers, the result is the same: the arrangement is one by which the broker becomes, as between himself and his client, the owner of the shares in question, although he is under a contract to provide an equal amount of similar shares at a future date. This being the nature of the business between the parties, the reason why these "contangos" or "continuations" are often called loans is quite clear; but this does not alter the legal position of the parties con cerned in them, or prevent the shares held by the brokers under such circumstances from being their own and available by them.

54 According to the practice among brokers in Toronto and New York with reference to stocks so carried the powers of the broker over the stocks are much more restricted than those thus indicated. The evidence of Mr. Osler makes it plain that while the broker may pledge his securities *en bloc* he is, according to the practice in Toronto, bound to do so in such a way — that is to say, he is bound so to maintain the ratio between the loan and the value of the securities lodged — as to be able at any time on payment of the amount owing by a particular customer to procure delivery of any pledged shares which may be the property of that customer. His primary obligation, in a word, is to maintain such control over his hypothecated securities as to enable him at any time to carry out his contract with his customer; but subject to that he may pledge his customer's security with others *en bloc* for the purpose of getting the necessary funds to carry out his obligations. It appears to me to be a question of fact whether or not the agreement between the plaintiff and the defendants was entered into with reference to this practice. I do not think the law assigns such legal incidents to an arrangement by a broker to carry stocks "on margin" for a speculator as to exclude such a practice. I am quite willing to concede that in the absence of any such custom and in the absence of any express agreement to the contrary the relation between the customer and broker in such transactions would be in substance that of mortgagor and mortgagee subject to some modifications necessary to suit the peculiar necessities of the case. Here, however, we have such a cus tom, and I think the effect of the evidence is that in Toronto at all events it would be impracticable for brokers to carry out such transactions without resorting to the methods mentioned. There are some observations of Parke B. in *Foster v. Pearson*[7] , at pages 858, 859 and 860, not without a bearing upon the point.

> The judgment in the case of *Haynes v. Foster*[8] is treated in the argument for the defendant as establishing that it is a sort of *legal incident* to the character of a bill-broker that he is to pledge the bills of each customer separately; but we think that such is not the fair meaning of the judgment, but that it is to be taken in connection with the evidence, and that all that was intended was this, that, in the absence of evidence as to the nature of such an employment, a bill-broker must be taken to be an agent to procure the loan of money on each customer's bills separately, and that he had therefore no right to mix bills together and pledge the mass for one entire sum. In truth, *a bill-broker is not a character known to the law with certain prescribed duties; but his employment is one which depends entirely upon the course of dealing* . It may differ in different parts of the country, it may have powers more or less extensive in one place than in another; what is the nature of its powers and duties in any instance is a question of fact, and is to be determined by the usage and course

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> of dealing in the particular place. A great body of evidence was adduced in the present case to prove that it was the course of dealing in the city of London for bill-brokers to raise money for their employers, by pledging the bills of different proprietors for one entire advance; and there is nothing unreasonable in such a practice.
>
> It remains to consider whether there is any difference between the case of *Foster v. Pearson* and that of *Stevens v. Foster* .
>
> The question was not left to the jury in the same way in the latter as in the former case. It was put on the ground that the jury might infer from the usage proved, and its general notoriety, that the customer employed the bill-brokers with reference to that usage, and therefore authorized them to deal with the bills as they in fact did; and the jury were satisfied with the evidence, and did draw the inference that Messrs. Wood & Poole had authority as between them and their employers to pledge the bills in the manner in which it appears that they did.
>
> So far as the usage tends to shew an authority to pledge bills in a mass, and not separately, its reasonableness is hardly disputed; and that question has also been already disposed of. It was proved to be the prevailing practice, and it is enough for us to say the jury were warranted in drawing the inference which they did, especially as the plaintiff was himself a bill-broker.

These observations were in effect adopted in *London Joint Stock Bank v. Simmons*[9] , by Lord Macnaghten at page 225, and by Lord Field at page 228.

55 It is then, I repeat, a question of fact whether the contract was or was not entered into with reference to the usages referred to. I agree with the Court of Appeal that the proper inference is that it was. The appellant was, admittedly, familiar with transactions in the stock market. In each of the bought notes sent to her there is an intimation in these words: —

> When carrying stocks for customers, we reserve the right of pledging the same or raising money upon them in any way most convenient to us.

56 This, she says, was not brought to her attention, but, I think, a person who, having instructed a broker to buy stocks and carry them, receives a notice of this kind and does not read it, must be taken in respect of subsequent dealings to assent to any reasonable terms it may contain to the same extent as if he had read it and taken no exception to it. Now, in my view, this intimation is a plain warning that the arrangement with the broker involves the right to use the stocks purchased as security in accordance with the reasonable practice in such transactions among reputable brokers in Toronto and New York; and I do not see how after reading it and acquiescing in it the client could be heard to object to the use of them in the same way in which stocks carried "on margin" were being generally dealt with. I do not think ordinary people reading such a notice would take it to refer only to the broker's interest as mortgagee; that I think is too much of a lawyer's refinement. I think most people would assume that it meant something more than the mere statement of the fact that the broker would exercise his legal right to hypothecate his own interest in the securities referred to.

57 But assuming the plaintiff's rights to be regulated by the rules governing the relations between mortgagor and mortgagee, without reference to any special course of dealing, I cannot understand upon what ground she can recover in this action. The proposition upon which her case rests must be this: that a mortgagee of shares in an incorporated company making a sub-mortgage to secure a sum larger than the actual amount of his mortgage debt comes *ipso facto* under an obligation to pay the mortgagor the full market value of the shares at the time, and this although the mortgagor has acted in entire good faith and without profit to himself or loss to the mortgagor. I do not know upon what legal principle any such liability can be based. If the mortgagee makes a sale or as in *Ex parte Dennison*[10] hands over the stocks to somebody else to make a sale or does that which is equivalent to a sale he must, of course, account for what he receives or ought to have received; if he improperly uses the mortgaged property in such a way as to make a profit out of it he may be accountable for

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

the profit. But if a mortgagee holding land under an absolute conveyance subject to a collateral agreement for redemption should submortgage or otherwise encumber the property (without disclosing the mortgagor's interest) for a larger amount than the mortgage debt, would anybody argue that the mortgagee must account for the full value of the land at the date of the sub-mortgage? If so, upon what principle could the contention be based? If one take the case of a pledge of chattels, that case is covered by distinct authority. It has long been settled that a repledge for more than the debt of the pledgor does not expose the pledgee to an action for conversion. Even a trustee using the property of his *cestui que trust* is accountable, generally speaking, only for the property or for the profits he has made or for the loss occasioned by his breach of trust. I do not think it has ever been suggested that a trustee in good faith leasing property he had no power to lease or mortgaging property he had no power to mortgage assumes *ipso facto* the obligation of a purchaser of the property at the option of his *cestui que trust*.

58 A very different question arose in *Conmee v. Ames*[11] , and I refer to it only because some language of mine has been cited as shewing that the memorandum on the bought note was not to be given effect to. In that case it appeared to me there was no evidence of any general practice which would affect the transaction under consideration. The point upon which it appeared to me, rightly or wrongly, that the decision must turn was that the plaintiffs, the brokers (who were suing the principal for a payment alleged to have been made on his account), had on the facts proved failed to establish that they had executed his mandate. I thought also that the memorandum in the bought note (on the same terms as that referred to above) not having been brought to the defendant's notice could not be held to govern the rights of the parties in respect of transactions completed before the bought note was despatched by the broker. That view has no possible bearing upon the questions arising in this case.

***Anglin J.*:**

59 The plaintiff sues to recover moneys paid by her to the defendants — her brokers — on account of the purchase price of certain shares of stock and interest thereon and for commissions; also for damages for breach of duty as her agents and for misrepresentation and deception and for the conversion of her shares.

60 The transactions were what is known as purchases on margin. The understanding, as deposed to by the defendant Wood, was that the brokers should take transfers of the stocks in such manner that, while the property of the plaintiff, they would be under the broker's control, *Caswell v. Putnam*[12] ; and that they should carry them for the plaintiff, having the right, however, at any time to call upon her to pay the balance due upon them and to take them over. As an incident to such a contract the brokers had the right to re-pledge the plaintiff's stock, always preserving, however, her legal right upon payment of the balance owing by her to obtain delivery of her securities. *Conmee v. Securities Holding Co.*[13] , at pages 609, 613; *Rothschild v. Allen*[14] . Shares were eventually delivered by the defendants to the plaintiff on her de mand which corresponded in number and demonination with her orders to them. When she demanded and received these shares, however, she was ignorant of the brokers' dealings with her property in the interval which form the basis of her present action.

61 She prefers her claim on allegations that the defendants never bought for her the shares for which she paid them; that, if they were bought for her, at least some of such shares were re-sold by the brokers' agents without authority; and, if this be so, that all of them were pledged by the defendants for their own general indebtedness, much greater in amount than what was owing to them by her, and without any provision for the release of her property on payment of the balance which she owed in respect of it; and that the amount charged her for interest was greater than the brokers themselves paid for the moneys which they borrowed and was a secret profit to which, as agents, they were not entitled.

62 I am not satisfied that the plaintiff has established her charge that the brokers did not buy for her all the shares she ordered them to purchase. The purchases of Sao Paulo stock are fully proven. There is some confusion in regard to the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

purchase of the Louisville & Nashville Railway stock. The evidence of it is decidedly halting, and, had the finding been that this stock had not been bought for the plaintiff, I would have thought it at least equally satisfactory; but I am unable to say that there is no evidence to support the holding of the provincial courts that 100 L. & N. shares were purchased for the plaintiff in New York by the defendants' agents, the Randolphs.

63 It is no doubt the case that the identical shares of L. & N. which were so bought were not kept on hand by the defendants or their agents. But they were not bound to keep these identical shares on hand. *Nourse v. Prime*[15] . Subject to the question of hypothecation, with which I shall presently deal, their obligation would have been fulfilled if they kept on hand a sufficient number of L. & N. shares to answer the claims upon them of the plaintiff and of all other persons entitled to receive such stock from them. *Caswell v. Putnam*[16] ; *Conmee v. The Securities Holding Co.*[17] . Upon the evidence in the record, however, the finding that this obligation was fulfilled in regard to the L. & N. stock cannot, in my opinion, be sustained.

64 It is admitted that, on the day on which they received the certificates for the 100 shares of L. & N. said to have been bought by them for the plaintiff, the Randolphs delivered it through the clearing house to Gates & Co. in part fulfilment of a contract previously made for a sale to them of 400 shares of L. & N. After this delivery the Randolphs held either 450 or 550 shares of L. & N. (it is not very clear which is the correct figure) — all of them under hypothecation to various lenders for large sums of money. The defendants failed to produce the Randolphs' "box-book" which alone would have shewn any other unpledged shares. There is no evidence that any of the pledged shares belonged to the Randolphs themselves or could have been appropriated by them to the defendants' account without disregarding prior rights of some of their other customers. When it appeared that the L. & N. shares alleged to have been so purchased for the plaintiff were not held for her but were immediately delivered to a purchaser from the Randolphs — if it were not so with out that evidence — the burden was upon the defendants to shew, as something peculiarly within their knowledge, that they or their agents had on hand or under their control other L. & N. shares which they could rightly appropriate to the plaintiff's account. *Dickson v. Exans*[18] , at pages 59, 60; *The King v. Turner*[19] , at pages 210-211; *Elkin v. Janson*[20] , at page 661; Taylor on Evidence, 10th ed., p. 292. There is no such evidence in the record. The witness Abrey, Randolphs' representative, very carefully refrained from committing himself to this statement. He, no doubt, indicated the position correctly when he said, not that the defendants actually had 100 L. & N. shares in the hands of the Randolphs, but that "they were *long* by the records." The transfer to Gates & Co. of the shares said to have been bought for the plaintiff was, upon the evidence before us, unjustifiable. It was a distinct appropriation of them which rendered the defendants liable to account to her for their value; and to that liability it is no answer that a like number of similar shares was subsequently acquired by the defendants and was accepted from them by the plaintiff in ignorance of what had taken place. *Langton v. Waite*[21] . As to the 100 L. & N. shares the plaintiff's case is, in this aspect of it, if anything, stronger than was that of the defendant (appellant) in *Conmee v. The Securities Holding Co.*[22] .

65 It is fully established — in fact it is admitted — that the defendants hypothecated all the plaintiff's shares for their own general indebtedness, much greater in amount than the balance due by the plaintiff in re spect of such shares, and that at certain times they had not on hand shares available to answer her claim without resorting to those so hypothecated. They had no stipulation or agreement with their lenders under which they had a legal right to the release of the plaintiff's stock on payment of the amount she owed to them or of any smaller sum. They endeavoured to establish by evidence of brokers and others that it is the invariable custom of banks and trust and loan corporations from which such loans are procured by brokers to release the stock of a client pledged by his broker at any time upon payment of the amount of the balance due in respect of such stock by the client to the broker.

66 In the case of the pledges of the Sao Paulo shares the agreements between the lenders and the brokers were in writing. They contain no such term and in my opinion as to them this evidence of usage or custom was not admissible. It would vary written agreements or add to them a term inconsistent with the rights which they purport to give the lender.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

67 In the case of the L. & N. shares, assuming that they were bought and carried for the plaintiff, the terms of the hypothecation of them are not in evidence. It does not appear whether the arrangement for it was verbal or in writing. But the pledge was for general indebtedness and there is no evidence that there was any stipulation which would give either to the defendants or to the plaintiff a legal right to the release of her shares on payment of the amount which she owed.

68 I am not satisfied that the evidence in the record establishes such an invariable custom or practice as the defendants contend for on the part of the lenders from whom they borrowed. But if such a usage were established it would fall short of a reservation in favour of the plaintiff of the legal right to redeem her stock on payment of the amount due by her in respect of it; and to that legal right and nothing short of it she was entitled. The brokers could not require her to rely upon any loose understanding or mere obligation of honour between themselves and their lenders. Neither could they require her to rely upon their own personal security. She was entitled to have her shares in such a position that they would be her security and would be at all times available to her on payment of the amount which she owed in respect of them. *Douglas v. Carpenter*[23] , at pages 333-4. See also the remarks of Lord Wynford in *Rothschild v. Brookman*[24] , at pages 195-6.

69 It is common knowledge that the business of stock-brokers in this country is conducted in a manner more closely resembling that which prevails in the United States, and particularly in the State of New York, than that which obtains in England. Many customs and usages of English brokers are unknown in Canada; and many practices prevalent in our markets, which have come to us from the United States, would not be recognized on the London Stock Exchange. For this reason, and also because of a dearth of English authority (see R. 70 of the London Stock Exchange, Stutfield, 3rd ed., p. 45), I have drawn for authorities, perhaps more freely than is usual in our courts, upon American sources.

70 The hypothecation of the plaintiff's stocks for the brokers' general indebtedness, in the absence of auth ority for it from her, was in my opinion unjustifiable, and, so far as such intangible property can be the subject of conversion, should be deemed a conversion of it. It was an exercise of dominion over the shares — the assertion of an interest in them inconsistent with the right of the plaintiff, consistent only, in the absence of authorization from the plaintiff, with ownership of the shares by the defendants.

71 Either because the securities should be regarded as negotiable; *Baker v. The Nottingham and Nottinghamshire Banking Co.*[25] ; *Colonial Bank v. Cady*[26] , at pages 277-8; *London Joint Stock Bank v. Simmons*[27] ; or because, as against the pledgees, whose good faith is not questioned, the plaintiff was estopped from denying the authority of the brokers to pledge the securities as their own; *Bentinck v. London Joint Stock Bank*[28] ; *McNeil v. Tenth National Bank*[29] ; the hypothecation gave to the pledgees an enforceable lien or a special property in the stock greater than that which the brokers had authority to confer. The evidence in the record and the position taken by the defendants sufficiently establish a custom of stock-brokers and bankers to deal with securities such as those in question as transferable by delivery when indorsed in blank. The elements necessary to establish an estoppel against the plaintiff appear to be present. It has not been even suggested on behalf of the defendants that their pledgees would not have been legally entitled to hold the plaintiff's securities as against her for the full amount of the loan as collateral to which they were hypothecated, or for so much of it as they pleased, unless a right of redemption on payment of the balance due by her to the defendants was a provision of the loan implied by custom. On the contrary, they assert a right to so deal with the plaintiff's stocks, based either on a special contract with her evidenced by a memorandum at the foot of the "bought note" sent to her, or upon an alleged custom, which they sought to prove, and which they contend confers on brokers carrying stocks on margin this extraordinary privilege.

72 I adhere to the views which I expressed in *Ames & Co. v. Conmee*[30] , at pages 168 *et seq.* , that the hypothecation of a client's stock by a broker for his general indebtedness without authority from the client is unjustifiable, and that the memorandum at the foot of the "bought note" given to the plaintiff — which is the same as that considered in *Conmee's* case — is not evidence of such authority. This note was in the following terms: —

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

When carrying stock for clients, we reserve the right of pledging the same or raising money upon them in any way most convenient to us.

73 It is clear that nothing was said about any such provision when the brokers took the plaintiff's orders. Miss Clarke denies that this memorandum ever came to her notice. But assuming that it did and that the brokers might thus add a term to the contract, upon a proper construction of the memorandum having regard to the fact that it was prepared by the brokers themselves, while it might authorize them to pledge the plaintiff's stock for an amount not greater than that due by her in any way most convenient to them selves, there is nothing in it to confer on them a right to pledge it for a greater amount or to mingle it with other securities in a bulk pledge. *Conmee v. The Securities Holding Co.*[31] . Neither is there anything in it to warrant the broker giving to his pledgee the right to dispose of the stock without notice either to himself or to his client. Yet we find that this was a stipulation in the pledge of the plaintiff's Sao Paulo shares to the National Trust Company; and there is a similar provision in the draft form of pledge used by the Dominion Bank with which the Sao Paulo shares were also hypothecated. It does not appear whether in the pledge of the L. & N. stock there was or was not a similar provision.

74 Failing to establish an express agreement by the plaintiff authorizing such pledges of her stocks as the defendants and their agents made and the attempted inference of such an authority from the memorandum on the "bought note" above alluded to being also unsuccessful, the defendants sought to establish that there is a universal custom of members of the Toronto Stock Exchange to so deal with their clients' stocks held on margin without express authority from the clients and that this custom was binding upon the plaintiff either because she was actually aware of it, or because, though not so aware, having employed members of the Toronto Stock Exchange, she should be deemed to have contracted subject to it. In the first place the evidence in my opinion falls short of what would be necessary to establish the custom. But, assuming that it was sufficiently proved, the attempt to bring home actual knowledge of it to the plaintiff absolutely failed. Without such knowledge it is not a custom which would bind her. *Kirchner v. Venus*[32] , at page 399. It "is so entirely in favour of (the brokers') side that it is fundamentally unjust to the other side," and, "if sought to be enforced against a person ignorant of it," would be held "unreasonable, contrary to law, and void"; its effect, if admitted, would be to change the intrinsic nature of the plaintiff's contract. *Robinson v. Mollett*[33] , at pages 818, 836-8; *Johnson v. Kearley*[34] , at page 530; *Lawrence v. Maxwell*[35] . It follows that the hypothecation of the plaintiff's stocks by the defendants and their agents for their general indebtedness was a distinct breach of the defendants' contract with the plaintiff and also of their fiduciary duty to her. *Conmee v. The Securities Holding Co.*[36] , at page 609-10. It was a "conversion" of her property; *Strickland v. Magoun*[37] , at page 116.

75 It is well established that where a broker, who is under agreement to purchase and carry stock for a client, sells that stock without authority, leaving himself without other stock of the same kind available to satisfy his client's claim upon him, he becomes liable in equity, at the option of his client, to account to him for the proceeds of the sale, or the value of the shares as upon a conversion thereof to his own use, and he cannot escape that liability by purchasing and tendering to the client the same number of similar shares. *Langton v. Waite*[38] , at page 173; *Taussig v. Hart*[39] , at page 429.

76 Where a broker lends his client's stock to another broker he will in equity be held guilty of a similar conversion of it and the rights of the client are the same as if the stock had been sold, the broker being held accountable for its value at the time of the conversion. *Ex parte Dennison*[40] .

77 The broker, who, without authority so to do, mingles his customer's securities with others and rehypothecates them for a greater amount than the customer's indebtedness to him, neither reserving the customer's right to obtain his securities on payment of that indebtedness nor retaining in his own possession a like amount of similar securities, available for delivery to his client, is in my opinion likewise guilty of a "conversion" of such securities. *Douglas v. Carpenter*[41] ; *Strickland v. Magoun*[42] ; *Rothschild v. Allen*[43] .

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

78 The broker in such a transaction appropriates the client's stocks for his own purposes and pledges them as his own. I can see no difference in principle between such an appropriation and that which takes place upon the wrongful sale or loan of stocks similarly held.

79 It is urged, however, that the recovery of the client should be confined to the actual damage which he can shew that he has sustained as the result of the wrongful hypothecation of his stock, and that, where such stock, or a like amount of other stock of the same kind is delivered to him upon his demand, he has suffered no damage and can at best have but a nominal recovery. No doubt this would be the case if the sole right of the client were to maintain a common law ac tion of trover and conversion. *Hiort v. London and North Western Ry. Co.*[44] .

80 At common law, and if the relationship of the client to the broker should be regarded merely as that of pledgor and pledgee, re-hypothecation by the pledgee for a larger amount than that of his claim against the pledgor, though unlawful, is deemed not so repugnant to the contract as to be equivalent to a renunciation of it and an extinguishment of the pledgee's right of detainer; and the pledgor cannot maintain an action of detinue without having paid or tendered the amount of the pledgee's claim against him. *Donald v. Suckling*[45] , at page 616. It is to be noted, however, that, in this case, as stated by Mellor and Blackburn, JJ. the re-pledging would be inoperative as against the original owner, and would confer upon the defendant no greater right than the original pledgee had: pp. 610, 611. If such an action were maintained at common law, it would be on the ground that the contract had been terminated and the pledgee would thus lose his security or its value, although not in a position to recover his advances.

81 A premature sale by a mere bailee or pledgee was also held at common law not to terminate the bailment nor to destroy the interest or special property of the bailee in the goods pledged, and, therefore, although a conversion, to be insufficient without tender to the bailee of the amount of his claim to support an action of detinue; and for the conversion only actual damages could be recovered, and, if there were not such damages, only nominal damages — if indeed the action would lie at all. *Halliday v. Holgate*[46] ; *Johnson v. Stear*[47] .

82 But even at common law, an action in assumpsit for money had and received would lie for the proceeds of securities wrongfully sold by the bailee or agent (not a pledgee), the owner electing to treat the wrongdoer as his agent in the transaction, and adopting the sale and claiming its proceeds as money had and received to his use. *Marsh v. Keating*[48] , at page 600. In *Bonzi v. Stewart*[49] , it was held that the principal of a factor, who had raised money on the security of his principal's goods without authority, might claim it as money had and received to his own use. Tindal C.J. said: —

> Messieurs Bonzi were at liberty, *at any time when they found their factors had wrongfully raised money on their goods* , in taking the account between themselves and their factors, to abandon their goods altogether, and to treat the money so wrongfully borrowed by the factors on the pledge of the goods, as money had and received to the use of themselves.

83 The Chief Justice adds that this is but an application of the principle laid down by the House of Lords in *Marsh v. Keating*[50] .

84 A stock-broker buying on margin and carrying stock for a client is something more than a mere pledgee; he is also his client's broker or fiduciary agent. His position is not dissimilar to that of a factor who, in the ordinary course of business, is entrusted with the possession of his principal's goods or the documents of title thereto.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> Now as between principal and factor, there is no question whatever that that description of case *** has always been held to be within the jurisdiction of a court of equity, because the party partakes of the character of a trustee. Partaking of the character of a trustee, the factor — as the trustee for the particu lar matter in which he is employed as factor — sells the principal's goods, and accounts to him for the money. The goods, however, remain the goods of the owner or principal until the sale takes place, and the moment the money is received the money remains the property of the principal. So it is with regard to an agent dealing with any property; he obtains no interest himself in the subject-matter beyond his remuneration; he is dealing throughout for another, and though he is not a trustee according to the strict technical meaning of the word, he is *quasi* a trustee for that particular transaction for which he is engaged; and therefore in these cases the courts of equity have assumed jurisdiction. *Foley v. Hill*[51] .

85 The stock-broker holding the stocks of a client, bought by him upon margin, as collateral security for moneys advanced by him to make the purchase, is neither merely a broker, nor merely a pledgee of the stock. He holds towards his client a fiduciary relation similar to that which exists between the factor and his principal; in his capacity as a pledgee he cannot divest himself of his character as an agent; having assumed the position of a quasi-trustee, the client is in equity entitled to hold him to it and to the consequent obligation to account on that footing. *Haight v. Haight & Freese Co.*[52] ; see also *Marvin v. Brooks*[53] , at page 81. Indeed an accounting on this basis seems to be exigible in equity from a broker-pledgee although no fiduciary relationship existed in regard to the securities in question. *Ex parte Dennison*[54] . Where there is a relation of quasi-trusteeship between the parties, the equitable jurisdiction to compel an accounting undoubtedly attaches.

86 It is familiar law that if a trustee's breach of trust consists in a sale of stock, the *cestui que trust* may in bankruptcy proceedings at his option prove for the proceeds of the sale or for the value of the stock at the date of bankruptcy. *Ex parte Gurner*[55] . So, in an action against a trustee who has wrongfully sold real property, the *cestui que trust* has the option of compelling the trustee to purchase other lands of equal value to be settled upon the like trusts, or of taking the proceeds of the sale with interest, or the present estimated value of the lands sold after deducting any increase of price by subsequent improvements. Lewin on Trusts, 11th ed, p. 1138.

87 In the case of a wrongful sale of his stock by his broker, if the client, who had intended to hold it, upon demand receives from the broker shares of the same kind and to an equal amount at par value, though he did so in ignorance of the broker's misconduct, he cannot shew that he is any worse off than he would have been had the shares been kept for him by the broker always ready for delivery. From that point of view he has sustained no damage, and were it not for the fiduciary position of the broker he might have no redress. But in equity his right, upon learning of the wrongful sale, to hold the broker accountable for its proceeds or for the value of the securities at the time of sale, as upon a conversion thereof to his own use, appears to admit of no doubt. Like results follow where the broker lends the client's stock. Why should the consequences not be the same where he appropriates the securities by hypothecating them for his own indebtedness to an amount greater than is due him from his client? Certainly not merely because, on demand by the client, ignorant of what has transpired, he has de livered to him shares of the same kind and of a like amount at par value. If that would suffice to discharge the broker guilty of wrongful hypothecation, it should also suffice where he has effected a wrongful loan or sale. Nor is the fact that the client has not shewn that the broker has made a profit by his misdeed a sufficient reason for his not being held so accountable.

88 Where a broker entrusted with his client's securities sells or lends them, the authorities establish that in equity he must account for their value at the date of the "conversion." Where he appropriates them by unauthorized hypothecation, the client should have the same remedy. In each case alike the personal responsibility of the broker has been unlawfully substituted as the client's security in lieu of the property with which the broker has wrongfully dealt. In each case, instead of fulfilling his mandate, which required him to hold the stock or shares for his client, or, if he parted with their possession, to do so only in such manner that upon payment of the amount due by him the client could obtain them as of legal right from the holder, the broker, using them for his own purposes, has put them out of his control. In the one case the client is asked to trust to the broker buying in shares to replace those with which he has parted; in the other, to his doing that, or redeeming the shares which he has pledged. In each case the client is subjected to the risk of the broker's insolvency.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

89 The broker, who hypothecates his client's stock for his own purposes for a sum larger than that due by the client, substitutes as security to the latter, at least to the extent of the excess, his personal responsibility in lieu of the stock to which the client is en titled. If the broker, remaining solvent, by redeeming the stock and delivering it to the client on demand, could fully discharge himself, the temptation to commit the breach of duty involved in so dealing with stocks in his hands might, in many cases, be irresistible; can he but succeed in concealing his wrongdoing until the client applies for and takes over the stock or directs its sale, he escapes all liability for his misdeed. On the other hand, should he become bankrupt, and disaster to the client ensue, the broker will probably be little troubled by the claim of the latter for damages against what will in many cases be a practically worthless estate.

90 In wrongful sale — in wrongful loan — in wrongful hypothecation, there is involved an appropriation by the broker of his client's property for his own use.

91 While I appreciate the distinction which is drawn between a disposition of a pledge by a bailee effected wholly without authority, which suffices to terminate the contract of bailment and to disentitle the bailee to repayment of his advances, and a disposition merely in excess of the bailee's authority to do an act of the same class — such as a sale effected prematurely or without requisite notice, or a repledge for a greater amount than is due to the original pledgee — which is not so repugnant to the contract of bailment that it puts an end to it; *Halliday v. Holgate*[56] ; *Donald v. Suckling*[57] ; and is, therefore, held not to destroy the bailee's right to repayment of his advances or, in the case of the broker-pledgee, to indemnity; *Minor v. Beveridge*[58] ; the difference ends there. Its hypothe cation for a larger amount by a broker, holding with a right to repledge to cover his own advances, imperils the security of his client and involves an appropriation of it by the broker for his own use quite as much as would its pledge merely for the amount of the excess if the broker had no right to pledge at all; indeed, in the former case the title of the broker's pledgee, if dependent on estoppel, will probably be more readily established. The vital distinction, however, between the repledge by a broker holding a client's securities as the defendants held those of the plaintiff and the repledge by a mere common law pawnee is that in the former case the broker confers on his pledgee a good title for the whole amount of his advances as against the broker's client, whereas in the latter, the title of the sub-pledgee is limited to the interest of the original bailee.

92 In a case of sale the broker may directly take advantage of the rise and fall in the stock market to make illicit profit; indeed, he may use his client's stocks to help to bring about fluctuations in prices for his own benefit at his client's expense. In a case of hypothecation the opportunities for direct advantage may not be the same. But, although on a loan of the client's stock the broker has not this advantage, he is held accountable for the market value of the stock at the time he wrongfully lends it. *Ex parte Dennison*[59] . Moreover, by pledging his client's stocks in bulk with securities of his own or of other clients, the broker may be enabled to raise a much larger sum of money than if all these stocks were pledged separately. With the additional moneys so obtained — moneys part, or it may be the whole, of which rightfully belong to the client — the broker may be enabled to reap advantages and to make profits which it would be difficult to estimate and almost impossible to trace directly to their source. He may be enabled on his own account to deal, to an extent not otherwise possible, in marketable securities, profiting by their fluctuations in value, and perhaps affecting the market price of his client's securities to his detriment. Upon principle as well as for reasons of policy I think that, in the case of the stock-broker, the wholesome rule which entitles the client to hold him accountable for the market value of his securities at the time of their conversion should be held equally applicable to the cases of a wrongful hypothecation, a wrongful sale and a wrongful loan of such securities. I know of no situation in which a quasi-trustee has greater opportunities, if so inclined, to derive improper advantage from the possession and control of the property of his *cestui que trust* , than that in which the broker carrying stocks on margin for a client finds himself. In order, as far as possible, to protect their customers against the risks to which they would be exposed, were brokers at liberty with practical impunity to deal with their securities as those of the plaintiff were dealt with in this case — in order to protect brokers themselves against the temptation of making, it may be, large illicit gains by committing such a wrong with a minimized risk of personal loss, I think that the drastic but salutary rules which govern the relation of trustee and *cestui que trust* should be applied in all their rigour.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

93 The very difficulty — amounting to a practical impossibility — of an accounting on the basis of the profits which the defendants may have made by the use of the money obtained by their illegal hypothecation of the plaintiff's securities affords another and a cogent reason for treating them as having become purchasers of those securities when they so dealt with them and for holding them accountable for their fair value at that time. "This seems to me to be a simple mode of effectually doing justice between the parties." Having used the plaintiff's securities as proprietors, the defendants' "proceedings, I think, entitled (her) to elect, and (she) has elected, to treat them as purchasers." *Marriott v. The Anchor Reversionary Co.*[60] , at pages 186, 188.

94 Having regard to the fact that the financial result to the plaintiff would in all likelihood have been the same as it is had her stocks not been wrongfully pledged by the defendants, it may seem a hardship to hold them so accountable. But this observation is equally applicable where the broker sells and afterwards replaces his client's stock. "This is the risk to which such transactions are subject," *Ex parte Dennison*[61] , at page 553; and the law applicable to them is "a law of jealousy," *Rothschild v. Brookman*[62] . I cannot but think it deplorable that it should be held to be the law of Canada that if a broker, carrying stock on margin without authority, uses his client's shares as his own — pledges them for his general indebtedness — substitutes for them his personal responsibility as security to his client, the latter has not the right, upon discovering the facts, to elect to adopt his agent's appropriation of his property and to hold him chargeable with its value at the time of its con version. The effect of such a decision must be greatly to encourage breaches of duty by these quasi-trustees and to foster amongst an important body of fiduciary agents a disregard of the fundamental distinction between *meum* and *tuum* in dealing with the property of their principals.

95 In the case of a sale the proceeds usually represent the value of the securities; but, if not, the client's right is to an account of the actual market value. *Taussig v. Hart*[63] . In the case of an hypothecation, as in that of a loan, the value must be determined by the market price at the time. If, as in the factor's case (*Bonzi v. Stewart*[64]), the right of the client adopting the broker's misappropriation should be restricted to claiming credit for the moneys raised upon his securities as against the broker who has so mingled these securities with others that it is not possible to determine how much of the moneys lent to him have been obtained on the pledge of them, it may fairly be held that a portion of the advances equal in amount to the full value of the client's securities was obtained by their hypothecation. In my opinion, therefore, the defendants and their agents by pledging the plaintiff's shares for their general indebtedness without providing for their release on payment of the balance owing by her, and without holding under their own control other shares of the same description available to answer her claim, made themselves accountable to her for the market value of such shares at that time.

96 That right the plaintiff did not lose by her subsequent acceptance of the shares tendered to her by the brokers in satisfaction of her claim, or by her dealing with them as owner, in ignorance of what had transpired. Without knowledge there cannot be ratification or condonation. *Johnson v. Kearley*[65] , at page 524. The defendants are, of course, entitled in an equitable accounting to credit for the value of the shares at the time they were so accepted. But they cannot insist on the plaintiff's returning, or tendering a return of such shares before suing for such accounting. If, in circumstances such as those of this case, a broker had this right, he might put a client, who had innocently parted with shares so taken over, in a position of serious difficulty; he might effectually deprive him of his right of action. The broker, whose misconduct has led to such a difficulty, cannot complain if his client elects to retain the securities giving him credit in the accounting for their market value when received.

97 This case may also be dealt with on the basis which commended itself to Magee J. in *Hutchinson v. Jaffray & Cassels*[66] . Concealing the facts which entitled the plaintiff to take the position that her indebtedness was wiped out and that she was in fact their creditor, and falsely representing to her that they held and were carrying her stocks according to her mandate, the defendants obtained from her several payments of large sums of money and eventually of the entire residue of

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

the purchase price of the stocks, with interest on the balance from time to time unpaid. Moneys so obtained by misrepresentation — paid in mistake of material facts concealed by the payee from the payer — are recoverable. The law will not permit persons holding a fiduciary position to retain them.

98 The brokers receive the full benefit to which they are entitled in respect of their claim for indemnity by having the balance of the original purchase price unpaid by the client offset in the accounting against the value of the converted property for which the client receives credit. To that they have an equitable right (*Minor v. Beveridge*[67]), but to nothing more.

99 The present action concerns 50 shares of Sao Paulo stock bought on the 26th of April, 1906 — (all the S.P. stock held by the defendants except 10 shares was hypothecated for their general indebtedness on the 30th of April); 50 shares of S.P. stock bought on the 26th September, 1906 — (all the defendants' S.P. stock was hypothecated for their general indebtedness on the 29th September); and 100 shares of L. & N. railway stock said to have been bought on the 25th August, 1906, and hypothecated in like manner, if it was not wrongfully sold, as I think it was, on the very day of its purchase. As to the latter stock the defendants are accountable for the full price charged to the plaintiff for it. The market prices of the S.P. stock on the 30th April and 29th September are not in evidence, but there are general statements that, when the plaintiff's Sao Paulo shares were hypothecated, the market prices did not differ materially from the prices at which they were purchased for her. The defendants having failed to prove that at the respective dates of their conversion the market prices of these shares were lower than at the respective dates of purchase, they are accountable in the case of these stocks also for the full prices charged to the plaintiff. For these sums she should be given credit — in respect of the first lot of S.P. shares on the 30th April, 1906, and in respect of the second lot, on the 29th September, 1906. She is chargeable with interest on the balance of the purchase price of the first lot unpaid between the 26th and the 30th April, and in respect of the second lot on a like balance from the 26th to the 29th September, at the rates shewn in the defendant's accounts in which she appears to have acquiesced. No interest is chargeable against her in connection with the L. & N. transaction. She is chargeable with the purchase price of these several stocks and is entitled to credit for all moneys paid by her to the defendants for principal, interest and commissions, including the original marginal payments and the final payment of the 3rd of June, 1907. Upon the sale of the first lot of Sao Paulo she was credited with the proceeds. That credit must stand. She took delivery from the brokers on the 3rd of June, 1907, of 50 shares of Sao Paulo and 100 shares of L. & N. The defendants are entitled to credit for the market value of these shares at that date. The plaintiff is entitled to interest at 5% on any balance from time to time standing to her credit on such accounting and upon the final balance, which would stand to her credit after the payment of the 3rd of June, 1907, from that date until this action was brought; and to interest on her claim thus ascertained until judgment.

Appeal dismissed with costs.

Solicitors of record:
Solicitor for the appellant: *W.C. Mackay.*
Solicitors for the respondents: *Malone, Malone & Long.*

Footnotes

1 38 Can. S.C.R. 601.

2 6 Vesey 617.

3 6 Vesey 625.

4 38 Can. S.C.R. 601.

5 38 Can. S.C.R. 601.

6 [1893] 2 Ch. 120 .

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

7 1 C.M. & R. 849.

8 2 C. & M. 237.

9 [1892] A.C. 201 .

10 3 Ves. 552.

11 38 Can. S.C.R. 606.

12 120 N.Y. 153.

13 38 Can. S.C.R. 601.

14 90 App. Div. N.Y. 233.

15 4 Johns. Chy. 490; 7 Johns. Chy. 69.

16 120 N.Y. 153.

17 38 Can. S.C.R. 601.

18 6 T.R. 57.

19 5 M. & S. 206.

20 13 M. & W. 655 .

21 L.R. 6 Eq. 165, at p. 173.

22 38 Can. S.C.R. 601.

23 17 App. Div. N.Y. 329.

24 5 Bli. N.S. 165.

25 60 L.J.Q.B. 542.

26 15 App. Cas. 267 .

27 [1892] A.C. 201 .

28 [1893] 2 Ch. 120 .

29 46 N.Y. 325.

30 10 Ont. L.R. 159.

31 38 Can. S.C.R. 601, at p. 609.

32 12 Moo. P.C. 361 .

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

33 L.R. 7 H.L. 802.

34 [1908] 2 K.B. 514 .

35 53 N.Y. 19.

36 38 Can. S.C.R. 601.

37 119 App. Div. N.Y. 113.

38 L.R. 6 Eq. 165.

39 58 N.Y. 425.

40 3 Vesey 552.

41 17 App. Div. N.Y. 329.

42 119 App. Div. N.Y. 113.

43 90 App. Div. N.Y. 233.

44 4 Ex.D. 188.

45 L.R. 1 Q.B. 585 .

46 L.R. 3 Ex. 299.

47 15 C.B.N.S. 330 .

48 1 Mont. & Ayr. 592.

49 4 Man. & Gr. 295 at pages 303-4, 325; 5 Scott, N.R. 1, 26.

50 1 Mont. & Ayr. 592.

51 H.L. Cas. 28, at pp. 35-6.

52 112 App. Div. N.Y. 475; 190 N.Y. 540.

53 94 N.Y. 71.

54 3 Vesey 552.

55 1 Mont. D. & DeG. 497.

56 L.R. 3 Ex. 299.

57 L.R. 1 Q.B. 585 .

58 141 N.Y. 399.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

59 3 Ves. 552.

60 3 DeG. F. & J. 177.

61 3 Ves. 552.

62 5 Bli. N.R. 165, at p. 190.

63 58 N.Y. 425, at p. 429.

64 4 M. & Gr. 295, at pp. 303-4, 325; 5 Scott N.R. 1, at p. 26.

65 [1908] 2 K.B. 514 .

66 1 Ont. W.N. 481.

67 141 N.Y. 399.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 2

2003 CarswellOnt 168
Ontario Superior Court of Justice

Metropolitan Toronto Police Widows & Orphans Fund v. Telus Communications Inc.

2003 CarswellOnt 168, 30 B.L.R. (3d) 288, 6 P.P.S.A.C. (3d) 307

Metropolitan Toronto Police Widows and Orphans Fund et al, Plaintiffs and Telus Communications Inc., Defendant

Ground J.

Heard: September 9, 10, 12, 13, 16-18, 2002
Judgment: January 21, 2003
Docket: 99-CL-003317

Counsel: *Michael E. Barrack*, *Mark Polley*, *Jefferson J. Roppell*, for Plaintiff
David S. Stockwood, *Johanna Braden*, for Defendant

Subject: Corporate and Commercial

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Corporations — Borrowing — Bonds and debentures — Miscellaneous issues

Securitization transaction between company and special purpose trust was established by agreement for purchase of company's receivables by trust — Company redeemed bonds through application of proceeds of securitization transaction — On redemption date, market price per bond was greater than redemption price paid by company pursuant to trust deed resulting in loss to bondholders — Bondholders brought action for damages and for relief from oppression — Action dismissed — Redemption of bonds was not refunding operation by company through direct application of borrowed funds in that securitization transaction was in law true sale and not secured borrowing — Wording of receivables purchase agreement clearly indicated intention of parties that transaction be true sale and conduct of parties did not negate that intention — Both parties could only get full benefit of transaction if it was true sale — Recourse available to trust under agreement was not full recourse with respect to collectibility and was not economic recourse in sense of guarantee of repayment and did not preclude determination that transaction was sale — Absence of right of trust to retain surplus from collection of receivables was not fatal to determination that transaction was sale — Purchase price under transaction was not uncertain — Subject matter of sale of receivables was ascertainable and fact that agreement contemplated that particular receivable may under certain circumstances be reconveyed to company did not derogate from fact that original conveyance of receivable to trust was true sale — Provisions of agreement relating to collection of purchased receivables by company on behalf of trust were not inconsistent with sale transaction — Agreement did not grant company any right of repurchase or redemption of accounts receivable at its option so as to lead to conclusion that transaction was not true sale.

WestlawNext® CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Conditional sales --- Nature of conditional sale — General

Ultimate test to be applied to determine whether particular transaction is secured loan or true sale is right of borrower, upon repayment of debt, to require lender to reassign to it all of lender's interest in assets secured to pay debt — In case of true sale, vendor has no right to require title to assets sold to be reassigned to it.

Corporations --- Borrowing — Rights and obligations of security holders — Redemption

Securitization transaction between company and special purpose trust was established by agreement for purchase of company's receivables by trust — Company redeemed bonds through application of proceeds of securitization transaction — On redemption date, market price per bond was greater than redemption price paid by company pursuant to trust deed resulting in loss to bondholders — Bondholders brought action for damages and for relief from oppression — Action dismissed — Redemption of bonds was not refunding operation by company through direct application of borrowed funds in that securitization transaction was in law true sale and not secured borrowing — Wording of receivables purchase agreement clearly indicated intention of parties that transaction be true sale and conduct of parties did not negate that intention — Both parties could only get full benefit of transaction if it was true sale — Recourse available to trust under agreement was not full recourse with respect to collectibility and was not economic recourse in sense of guarantee of repayment and did not preclude determination that transaction was sale — Absence of right of trust to retain surplus from collection of receivables was not fatal to determination that transaction was sale — Purchase price under transaction was not uncertain — Subject matter of sale of receivables was ascertainable and fact that agreement contemplated that particular receivable may under certain circumstances be reconveyed to company did not derogate from fact that original conveyance of receivable to trust was true sale — Provisions of agreement relating to collection of purchased receivables by company on behalf of trust were not inconsistent with sale transaction — Agreement did not grant company any right of repurchase or redemption of accounts receivable at its option so as to lead to conclusion that transaction was not true sale.

Table of Authorities

Cases considered by *Ground J.*:

Canada Trustco Mortgage Corp. v. Port O'Call Hotel Inc., (sub nom. *Pigott Project Management Ltd. v. Land-Rock Resources Ltd.)* 38 Alta. L.R. (3d) 1, (sub nom. *Pigott Project Management Ltd. v. Land-Rock Resources Ltd.)* 11 P.P.S.A.C. (2d) 1, (sub nom. *Pigott Project Management Ltd. v. Land-Rock Resources Ltd.)* [1996] 1 C.T.C. 395, (sub nom. *Minister of National Revenue v. Alberta (Treasury Branches))* 196 N.R. 105, (sub nom. *Minister of National Revenue v. Alberta (Treasury Branches))* 184 A.R. 1, (sub nom. *Minister of National Revenue v. Alberta (Treasury Branches))* 122 W.A.C. 1, (sub nom. *Alberta (Treasury Branches) v. Minister of National Revenue)* 133 D.L.R. (4th) 609, (sub nom. *Alberta (Treasury Branches) v. Minister of National Revenue)* [1996] 1 S.C.R. 963, (sub nom. *R. v. Alberta Treasury Branches)* 96 D.T.C. 6245, 39 C.B.R. (3d) 157, 27 B.L.R. (2d) 147, (sub nom. *Pigott Project Management Ltd. v. Land-Rock Resources Ltd.)* [1996] 5 W.W.R. 153, [1996] G.S.T.C. 17, (sub nom. *R. v. Province of Alberta Treasury Branches)* 4 G.T.C. 6103, 1996 CarswellAlta 366, 1996 CarswellAlta 366F (S.C.C.) — considered

Inglefield Ltd., Re, [1933] Ch. 1 (Eng. C.A.) — considered

Major's Furniture Mart Inc. v. Castle Credit Corp. (1979), 602 F.2d 538 (U.S. C.A. 3rd Cir.) — considered

Manufacturers Life Insurance Co. v. Dofasco Inc., 9 B.L.R. (2d) 203, 1993 CarswellOnt 175 (Ont. Gen. Div. [Commercial List]) — considered

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Pente Investment Management Ltd. v. Schneider Corp., 1998 CarswellOnt 4035, 113 O.A.C. 253, (sub nom. *Maple Leaf Foods Inc. v. Schneider Corp.)* 42 O.R. (3d) 177, 44 B.L.R. (2d) 115 (Ont. C.A.) — followed

Shenandoah Life Insurance Co. v. Valero Energy Corp. (June 1, 1988), Doc. Civ. A. 9032 (U.S. Del. Ch.) — considered

Welsh Development Agency v. Export Finance Co., [1992] B.C.L.C. 148 (Eng. C.A.) — considered

Westfair Foods Ltd. v. Watt, 79 Alta. L.R. (2d) 363, 115 A.R. 34, [1991] 4 W.W.R. 695, 79 D.L.R. (4th) 48, 5 B.L.R. (2d) 160, 1991 CarswellAlta 63 (Alta. C.A.) — considered

Statutes considered:

Canada Business Corporations Act, R.S.C. 1985, c. C-44
Generally — referred to

s. 241 — pursuant to

s. 241(2) — pursuant to

ACTION by bondholders for damages and relief from oppression.

***Ground J.*:**

1 This action arises out of the redemption by BC Tel., a predecessor of Telus Communications Inc., ("BC Tel"), of Series AL Bonds (the "Bonds") on December 30, 1997. The Bonds were redeemed through the application of the proceeds of a securitization transaction entered into between BC Tel and RAC Trust, a special purpose vehicle sponsored by CIBC/Wood Gundy ("RAC").

2 The Plaintiffs maintain that the redemption of the Bonds was a breach of the No Financial Advantage Convenant (the "NFAC") contained in a Deed of Trust and Mortgage between BC Tel and Montreal Trust Company dated as of March 1, 1946, (the "Trust Deed") pursuant to which the Bonds were issued. The Plaintiffs further maintain that the redemption of the Bonds effected a result that unfairly disregarded the interests of the Bondholders as referred to in Subsection 241(2) of the *Canada Business Corporations Act*, R.S.C. (1985), Ch. c-44, as amended, (the "CBCA"). It has been agreed to proceed with the claim of Sun Life Assurance Co. of Canada ("Sun Life") as to liability only. Sun Life was not an original purchaser of the Bonds but, as of the redemption date, held Bonds in the aggregate principal amount of $26,845,000 purchased by Sun Life at various times. On the redemption date, the market price of the Bonds was approximately $115.00 and, the redemption price paid by BC Tel pursuant to the Trust Deed was approximately $103.00 resulting in a loss to the Bondholders of approximately $12.00 per $100.00 principal amount of Bonds. The Bonds bore interest at the rate of 11.35% per annum and matured on November 15, 2005.

3 The NFAC in the Trust Deed provides as follows:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

The Company shall not, however, redeem any of the Series AL Bonds prior to November 15, 2000 other than for sinking and improvement fund purposes, as part of any refunding or anticipated refunding operation by the application, directly or indirectly, of funds obtained through borrowings, having an interest cost to the Company of less than 11.35% per annum

4 It is agreed that the redemption of the Bonds was effected through a refunding operation and that the redemption was not for sinking or improvement fund purposes. It is also agreed that the proceeds of the securitization transaction were deposited by BC Tel in a separate bank account and applied directly toward the redemption of the Bonds.

The Receivables Purchase Agreement

5 The securitization transaction between BC Tel and RAC was established by a Receivables Purchase Agreement between RAC and BC Tel made as of November 20, 1997 (the "Agreement"). The Agreement contains definitions of Eligible Receivables which must meet certain criteria set out in Schedule A to the Agreement and a definition of Purchased Receivables and provides that RAC purchases from BC Tel and BC Tel sells, assigns and transfers to RAC, all of BC Tel's right, title and interest in and to "the universality of all Eligible Receivables which, from time to time, constitute Purchased Receivables and all Related Security, all without the need of any formal or other instrument of assignment" (Section 2.01). There are some deficiencies in the drafting of the Agreement with respect to the definition of the purchase price of the Purchased Receivables but the only definition which is consistent with the balance of the Agreement is that the purchase price is comprised of the amounts advanced by RAC and not reduced pursuant to other provisions of the Agreement (defined as the "Outstanding Cash Payments") and the Deferred Amount. The Deferred Amount can only be calculated on the termination of the Agreement and is, in effect, the portion of the Reserve which is not required to be applied to compensate RAC for uncollectible Purchased Receivables.

6 The aggregate amount of Purchased Receivables which, as of any particular day, is sold to RAC, is determined by the Required Amount which is comprised of the Outstanding Cash Payments, the Reserve and the Purchase Discount. The Purchase Discount is determined monthly and is based upon RAC's adjusted cost of funds for the ensuing month. The Reserve is determined by a rather complex calculation but, for purposes of the transaction between BC Tel and RAC, is 5% of the Outstanding Cash Payments at any time. It is agreed that the historic bad debt ratio of BC Tel was between 1% and 2%.

7 It is agreed that the Outstanding Cash Payments and the Reserve may vary over the term of the Agreement and that the Purchase Discount will vary from month to month so that the Required Amount could vary on a day-to-day basis. It appears that, as of any particular day, one can determine exactly which Eligible Receivables are Purchased Receivables by applying the Trial Balance Sequence as defined in the Agreement which establishes an order in which Eligible Receivables are determined to be Purchased Receivables (Section 2.02). In simplified terms, the determination is made by starting with the obligor who owes the least amount of Receivables and proceeding through the obligors in ascending order of the aggregate amount of Receivables owed by each obligor. By following the Trial Balance Sequence, a particular Eligible Receivable may be a Purchased Receivable on day 1, may not be a Purchased Receivable on day 2, and may again be a Purchased Receivable on day 3.

8 The total amount advanced by RAC pursuant to the Agreement was $150,000,000. The Agreement provides that, on each day prior to the termination date, BC Tel shall automatically sell and RAC shall automatically purchase that amount of Eligible Receivables which will result in the Purchased Receivables equaling the Required Amount (Section 2.04). The Agreement also provides that BC Tel may, in effect, reduce the Outstanding Cash Payments by delivering to RAC a

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Cessation Request which has the effect of RAC ceasing to purchase Eligible Receivables until such time as the Outstanding Cash Payments has been reduced to the amount specified in the Cessation Request. The Cessation Request must be made in multiples of $1,000,000 and cannot reduce the Outstanding Cash Payments to less than $75,000,000 in total (section 2.05). The Agreement further provides that, on each day prior to the termination date, BC Tel shall be deemed to apply the collections from the Purchased Receivables first toward payment of the Purchase Discount for the relevant month to the extent that it has not been previously paid; second, on account of the Deferred Amount in an amount equal to 5% of the daily collections; and third, to the purchase of Eligible Receivables to be purchased by RAC on such a day so as to bring the aggregate amount of Purchased Receivables up to the Required Amount for such day (section 2.06).

9 The Agreement also appoints BC Tel as agent of RAC for the purpose of servicing the portfolio of Purchased Receivables purchased by RAC and sets out in detail the duties and obligations of BC Tel as servicer. No fee is payable by RAC to BC Tel for such services. BC Tel, as the servicer of the Purchased Receivables, is deemed to hold all payments to be applied toward payment of the Purchase Discount in trust for RAC and to remit such payments to RAC on the first day of the following month (section 2.06).

10 On termination, the Agreement provides that there shall be a Final Settlement Period following the termination date and that all collections after the termination date shall be held in trust for RAC and applied in payment to RAC of first, the Purchase Discount in respect of the Final Settlement Period; second, the Outstanding Cash Payments; and third, all other amounts owed to RAC under the Agreement (section 2.07). Following the payment of all such amounts to RAC, RAC shall, in satisfaction of its obligation to pay the Deferred Amount, at its option either pay the Deferred Amount in cash to BC Tel or sell, assign and transfer to BC Tel all of its right, title and interest in Purchased Receivables (section 2.07). The reference in section 2.07 to other amounts owed to RAC pursuant to the Agreement would appear to be a reference to a Program Fee payable to RAC of between .20% and .23% per annum of the Outstanding Cash Payments calculated on a daily basis pursuant to section 2.09 of the Agreement and reimbursement for legal costs up to $50,000 and for various other costs and expenses.

11 The Agreement also contains provisions for the reconveyance by RAC to BC Tel of any Purchased Receivable which ceases to be qualified as an Eligible Receivable or otherwise reduced or cancelled as a result of some action taken by BC Tel. BC Tel shall remit to RAC the amount of such Purchased Receivable or transfer to RAC additional Eligible Receivables to ensure that the Purchased Receivables are equal to the Required Amount (Section 2.08).

12 The Agreement also contains provisions relating to Events of Termination generally similar to events of default under a loan agreement and provides that, if an Event of Termination has occurred and is continuing, BC Tel shall hold all collections separate and apart from its general funds in a segregated trust account for the benefit of RAC and remit such collections to RAC as and when required by RAC. If an Event of Termination has occurred, RAC may designate a Replacement Servicer to replace BC Tel as servicer of the portfolio of Purchased Receivables and the fees of such Replacement Servicer shall be paid by BC Tel to RAC out of the proceeds of collection of Purchased Receivables (Sections 6.04 and 6.05).

13 The Agreement also provides that in the event that any change in any law, regulation or guideline of any governmental authority or any judgment, award or decree of any court results in the cost to RAC of the purchase of Purchased Receivables being increased or the rate of return to RAC in connection therewith being reduced, BC Tel shall from time to time upon demand by RAC, pay such increased costs or compensation for such reduction in rate of return to RAC (Section 7.06).

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

14 Although there is no specific provision that the Agreement is governed by the law of Ontario, the Agreement does provide that

> The Seller hereby irrevocably submits to the jurisdiction of any court sitting in Toronto in any action or proceeding arising out of or relating to this Agreement, and the Seller hereby irrevocably agrees that all claims in respect of such action or proceeding may be heard and determined in such Toronto court (Section 7.09).

Securitization

15 Corporate financing by way of securitization did not become prevalent in the Canadian market until the late 1980s or early 1990s. The basic concept of securitization is that a corporation raises cash by selling certain of its assets to a special purpose vehicle (an "SPV") which, in turn, issues securities, usually commercial paper, in the market to raise the purchase price of the assets purchased from the corporation.

16 The sale of the assets by the corporation to the SPV is structured in such a manner that it removes, to the extent practical, the assets from the estate of the corporation in the event of the bankruptcy or insolvency of the corporation. The assets are owned by the SPV and the realization or collection of those assets by the SPV services the commercial paper issued by the SPV. The holder of the commercial paper, therefore, looks to the cash flow from the assets and not to the credit of the corporation for repayment. The separation of the corporation from the assets themselves enables the corporation to raise funds less expensively through the commercial paper issued by the SPV, than it would cost the corporation to raise funds through securities issued directly by the corporation. There is also an "off balance sheet" advantage to the corporation in that the cash that is raised by the sale of the assets will not require an offsetting liability to be shown on the balance sheet of the corporation. The cash from the sale of the assets and the off-setting decrease in accounts receivable are reflected on the asset side of the corporation's balance sheet but there is no offsetting liability in that the commercial paper issued to raise such cash is a liability of the SPV and not of the corporation.

17 Securitization may have a further advantage to the corporation if it is restricted by trust deed or loan agreement covenants from incurring or securing debt. Securitization may enable the corporation to raise cash without breaching such covenants because the corporation is selling assets and is not incurring or securing debt. An article by Stephen L. Schwarcz "Structured Finance: The New Way To Securitize Assets": (1990) Cardozo Law Review, vol. 11, page 607, (the "Schwarcz Article") which contains a detailed history and analysis of securitization transactions states on page 608 "Whether a structured financing would violate particular covenants requires a case by case inquiry".

18 In the case of a sale of accounts receivable, the commercial paper issued by the SPV is not subject to the risk of the bankruptcy and insolvency or other downturn in the fortunes of the corporation selling its accounts receivable and is subject only to the risk of collectibility of the accounts receivable sold by that corporation to the SPV. This risk is covered by a reserve amount of receivables transferred to the SPV of at least 5% of the amount advanced by the SPV to the corporation and, in many cases, is further covered by a backup security and enhancement agreement entered into by the SPV with a financial institution. In the case of the BC Tel — RAC securitization, RAC negotiated a backup security and credit enhancement agreement with a Swiss bank to an amount of a further 10% of the Purchased Receivables sold to RAC.

History of the BC Tel — RAC Transaction

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

19 BC Tel was first approached by investment bankers with respect to the possibility of a securitization transaction in the early 1990s. It is clear from the evidence that, at that time, the officers of BC Tel considering these proposals had an imperfect understanding of securitization and had concerns with respect to the accounting and tax treatment of a securitization transaction. At that time, however, the regulatory environment in which BC Tel operated precluded BC Tel from reaping the full benefits of a securitization transaction and none of the proposals from the investment bankers was pursued at that time. The effect of the regulatory environment at the time was that redeeming debt would not permit BC Tel to earn additional income. BC Tel was limited to earning income equal to a percentage of equity on the basis of a 55/45 debt equity ratio.

20 In the period 1996 to 1997, the regulatory environment changed to a system based on certain caps on income as opposed to a limit tied into a percentage of equity and a particular debt equity ratio. It then became advantageous for BC Tel to enter into a securitization transaction and apply the proceeds from the sale of assets to the reduction of debt. BC Tel received a number of securitization proposals from investment bankers at this time and decided to proceed with the proposal from RAC which was sponsored by CIBC/Wood Gundy based upon the best pricing, lower program fees and the historic relationship between BC Tel and CIBC. A presentation was made to the Board of Directors of BC Tel on October 24, 1997, seeking the approval of the sale of up to $175,000,000 principal amount of accounts receivable to RAC. The Board gave its approval for the sale of $150,000,000 principal amount of accounts receivable. The Board, at that meeting, did not make any determination with respect to the use of the proceeds of the securitization but was advised that the most beneficial use of the proceeds would appear to be to redeem the Bonds.

21 The presentation to the Board indicates a net savings to BC Tel of $750,000 a year as a result of the reduction of capital tax after taking into account fees and costs relating to the securitization. BC Tel obtained, at that time, opinions from its outside counsel, its tax counsel and its external auditors addressing the legal nature of the transaction and its accounting and tax treatment. Following the Board's approval, on November 20, 1997, BC Tel entered into the Agreement with RAC. The sale of accounts receivable to RAC pursuant to the Agreement closed on November 20, 1997, and the proceeds of sale paid to BC Tel and deposited to a special bank account.

22 On November 26, 1997, a further presentation was made to the Board of Directors of BC Tel recommending the redemption of the Bonds out of the proceeds from the securitization transaction. The presentation indicates a net savings to BC Tel and, accordingly, a shareholders' gain, of $22,900,000 as a result of such transaction. The risks indicated in the presentation were the reaction of the holders of the Bonds and a risk of losing any legal challenge to the transaction although such risk was thought to be minimal as a result of the decision in *Manufacturers Life Insurance Co. v. Dofasco Inc.* (1993), 9 B.L.R. (2d) 203 (Ont. Gen. Div. [Commercial List]) and the lack of a legal challenge to a securitization transaction entered into by Hudson Bay Acceptance Co. in 1996. The Board of Directors approved the redemption of the Bonds out of the proceeds of the securitization transaction with RAC and the Bonds were redeemed on December 30, 1997.

23 During the currency of the Agreement, BC Tel issued two Cessation Requests resulting in the reduction of the Outstanding Cash Payments by $10,000,000 on January 31, 2002 and by a further $2,000,000 on February 28, 2002.

24 By letter dated August 1, 2002, Telus gave notice of the termination of the Agreement as of August 7, 2002 and proposed a Final Settlement Period ending September 22, 2002, which was agreed to by RAC. RAC proposed to pay the amount payable to Telus pursuant to the Agreement on the Final Settlement Date and to continue to collect Purchased Receivables rather than transferring Purchased Receivables back to Telus in satisfaction or partial satisfaction of the amount payable to Telus on the Final Settlement Date.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Findings of Fact

25 There are, in my view, very few facts in dispute in this action which are material to the issues to be decided by this court. The evidence did, however, establish the following facts which were relied upon to some extent by counsel in their submissions:

1. both BC Tel and RAC intended the securitization transaction to be a sale of the Purchased Receivables;

2. both BC Tel and RAC would obtain all of the benefits of the securitization transaction only if it was a sale;

3. the financial world recognizes that there is some risk that a securitization transaction may not be found to be a sale in law, particularly, in the case of a revolving type of securitization transaction; and

4. in the majority of securitization transactions, on termination, the seller buys back the Purchased Receivables in satisfaction or partial satisfaction of the amount, if any, payable to the seller on termination.

Issues

26 The three issues in this action may be broadly stated as follows:

1. was the redemption of the Bonds a refunding operation by BC Tel by the indirect application of borrowed funds having an interest cost to BC Tel of less than 11.35%?

2. was the redemption of the Bonds a refunding operation by BC Tel by the direct application of borrowed funds having an interest cost to BC Tel of less than 11.35%?

3. did the redemption of the Bonds by BC Tel effect a result that unfairly disregarded the interests of the holders of the Bonds?

Legal Analysis

Indirect Application of Borrowed Funds

27 It is not in dispute that the securitization transaction constituted a refunding operation in that the proceeds of the securitization were applied toward the redemption of the Bonds. It is also not in dispute that such refunding operation was not for sinking fund or improvement fund purposes.

28 The first issue then becomes whether the securitization transaction constituted the indirect application of funds obtained through borrowing having an interest cost to BC Tel of less than 11.35% per annum. It is agreed that the issuance of commercial paper by RAC to raise the funds advanced to BC Tel through the securitization transaction was a borrowing by RAC and that such borrowing during the relevant period had an interest cost of less than 11.35% per annum. The issue then becomes whether the securitization transaction was an indirect borrowing by BC Tel and whether there was an interest cost to BC Tel.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

29 On a straight reading of the wording of the NFAC, there is no requirement that the borrowing be by BC Tel, whereas the NFAC does require that the interest cost be an interest cost to BC Tel. In addition, the NFAC clearly contemplates the refunding operating being by the direct or indirect application of funds obtained through borrowing. In *Manufacturers Life Insurance Co. v. Dofasco Inc.* (1993), 9 B.L.R. (2d) 203 (Ont. Gen. Div. [Commercial List]), although the court determined that funds obtained by Dofasco pursuant to a financing arrangement with Mitsui & Co. Ltd. were not applied directly or indirectly by Dofasco to redeem the debentures issued under a trust indebenture containing an NFAC, the court did deal with the issue of indirect borrowings. Borins, J. cited with approval the decision of Chancellor Allen in *Shenandoah Life Insurance Co. v. Valero Energy Corp.* (U.S. Del. Ch., 1988) where he stated:

> ...suppose an issuer incorporated a subsidiary corporation and transferred sufficient assets to it to permit it to borrow money; and suppose that that subsidiary then did borrow low-cost funds and transferred them to its parent either pursuant to a high-interest note or as a capital contribution; and suppose, of course, that the issuer then used those nominally high-interest funds to redeem debentures to which a provision such as 4.02 pertained. Can there be any doubt that such a course would constitute the indirect application of low-cost borrowed funds in violation of a 4.02-type restriction? The reason that there appears so clearly to be the case is, again, that when the transaction has been completed, all that has occurred, from a realistic point of view, is the substitution of new (cheaper) debt for the higher interest debentures. *The borrowing has no economic purpose or reality other than that substitution.*
>
> While it is impossible to generalize perfectly concerning all of the situations in which the "indirectly" language of Section 4.02 might find application, *it does appear that the inclusion of that phrase is intended to reach situations in which the underlying economic reality of the completed transaction is the functional equivalent of a direct loan for purposes of effectuating a redemption and nothing more.* [emphasis in original]

30 The Plaintiffs submit that this analysis is applicable to the case at bar in that the underlying economic reality of the securitiziation transaction is the functional equivalent of BC Tel directly borrowing funds and applying the proceeds of the loan to the redemption of the Bonds and nothing more.

31 I have some difficulty with this submission. The evidence of the Defendant's witnesses was clear that the securitization transaction was approved by the Board of Directors of BC Tel separate and apart from the approval of the redemption of the Bonds. It was conceded that, at the time of the approval of the securitization, the possible application of the proceeds toward redemption of the Bonds was discussed but that the securitization was not approved strictly for the purpose of using the proceeds to redeem the Bonds. The evidence of the Defendant's witnesses was also undisputed that there were advantages to BC Tel in entering into the securitization transaction whether or not the proceeds were used for the redemption of the Bonds in that the transaction would have the effect of substantially reducing the capital tax paid by BC Tel and would have a positive impact on the presentation of the company's balance sheet. It was also the evidence of the Defendant's witnesses that BC Tel would have gone ahead with the securitization even if the proceeds were not available to redeem the Bonds in that there were other debts that BC Tel could have redeemed out of the proceeds of the securitization.

32 In the Dofasco case, unlike the case at bar, there was a tracing problem as to the source of the funds used to redeem the debentures. In the case at bar, there is no tracing problem; it is clear that the only monies used to redeem the Bonds were from the proceeds of the securitization transaction and, accordingly, the Plaintiffs submit that the source of the funds used to redeem the Bonds was an indirect borrowing using the facility provided by RAC. The Plaintiffs further submit that this indirect borrowing had an interest costs to the company of less than 11.35% per annum in that the interest cost to RAC was passed through to BC Tel by way of the Purchase Discount paid by BC Tel on a monthly basis which was determined by RAC's "actual pooled cost of funds allocated, on a weighted basis, to the cash proceeds relevant to the securitization transaction with BC Tel".

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

33 The Defendant attempted to draw a distinction between interest and the Purchase Discount payable pursuant to the terms of the Agreement in that the amount of interest paid is dependent upon the length of time that the loan is outstanding whereas the Purchase Discount is fixed for each month in advance and payable in arrears and presumably would be payable at the end of the month even if the total amount of Outstanding Cash Payments was reduced during that month and accordingly, is a discount in the sense of being a deduction from the purchase price of the receivables fixed once and for all at the time it is calculated. This reasoning appears to me to be a considerable stretching of the definition of discount in the authorities. The use of the phrase "Purchase Discount" is, in my view, a particularly inappropriate misdescription of the item. It is clearly not part of the purchase price of the Purchased Receivables and it is certainly not a discount from the purchase price of the Purchased Receivables. An analysis of the Agreement confirms that the Purchase Discount is strictly a flow through to BC Tel of the interest cost payable by RAC on borrowings made by it through the issuance of commercial paper. It is more analogous to consideration or compensation for the use of money than to a discount from the purchase price of assets. The Purchase Discount, in our case, is not described in the Agreement as a component of the purchase price of the Purchased Receivables and the obligation to pay the Purchase Discount is related in no way to the period that the Purchased Receivables are outstanding. It is clearly a mechanism to flow through to BC Tel the interest cost to RAC of monies borrowed by it and is payable so long as there are Outstanding Cash Payments as between RAC and BC Tel.

34 It is also the submission of the Defendant that, in order for a transaction held to be an indirect borrowing, the transaction must be a sham constructed to circumvent the NFAC and must have no independent economic function, as for example in the subsidiary situation postulated by Chancellor Allen in *Shenandoah Life Insurance Co., supra.* The Defendant submits that this is not applicable to the case at bar. The securitization transaction involved a non arm's length third party which received a financial benefit out of the transaction and the transaction also had an independent economic function for BC Tel in that it resulted in cash assets for BC Tel rather than accounts receivable which cash assets could be applied by BC Tel in a number of different ways including the ability of BC Tel to apply the proceeds from the sale of the receivables to the reduction of its indebtedness and accordingly realize considerable interest savings.

35 I am not satisfied that the fact that the Purchase Discount reflects the interest costs to RAC of funds borrowed by it is necessarily determinative of whether or not the transaction represents an indirect borrowing by BC Tel. If the transaction otherwise meets the criteria for a sale, in my view, it would not be fatal to that determination that the vendor had agreed to compensate the purchaser for the cost of raising funds to complete the purchase.

36 Further, I accept the submission of the Defendant that to find that the transaction was prohibited by the NFAC as being a refunding operation by the indirect application of funds obtained through borrowings, the transaction would have to have been constructed by BC Tel, specifically and exclusively, for the purpose of redeeming the Bonds and have no independent economic function either from the perspective of BC Tel or of RAC, neither of which criteria applies to the case at bar.

37 Accordingly, I conclude that the securitization transaction did not constitute an indirect borrowing of funds having an interest cost to BC Tel of less than 11.35% per annum and is not prohibited by the NFAC.

Direct Application of Borrowed Funds

38 The issue then becomes whether the Funds received by BC Tel through the securitization transaction and applied to the redemption of the Bonds were "borrowed funds". To determine whether the securitization transaction should be characterized as a sale or as a secured loan requires an analysis of the criteria which the courts have considered in determining whether a transaction is a sale. In interpreting a contract, the court must look to the intention of the parties as expressed by the language of the contract itself. The court may also look at the factual matrix or the circumstances existing at the time the contract was

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

entered into to determine which of two possible interpretations of the contract should be preferred. The court must also look to the substance of the transaction and not merely to the form. In *Inglefield Ltd., Re*, [1933] Ch. 1 (Eng. C.A.), Lord Hanworth, M.R. stated at page 17:

> It is old law, and plain law, that in transactions of this sort the Court must consider whether or not the documents really mask the true transaction. If they do merely mask the transaction, the Court must have regard to the true position, in substance and in fact, and for this purpose tear away the mask or cloak that has been put upon the real transaction. In *Helby v. Matthews* (1) Lord Herschell states the principle that we have to follow in the opening sentences of his speech (2):
>
> 'My lords, it is said that the substance of the transaction evidenced by the Agreement must be looked at, and not its mere words. I quite agree. But the substance must, of course, be ascertained by a consideration of the rights and obligations of the parties, to be derived from a consideration of the whole of the Agreement', and Lord Macnaghten and the other learned lords express the same opinion.

39 It is the function of the court to determine the real nature of the transaction by considering not only the intention of the parties as evidenced by the language of the contract but the evidence as to how the transaction in fact transpired and the conduct of the parties in the performance of the contract. Both the wording of the contract and the conduct of the parties in implementing the contract must be examined. In addition to the intention of the parties, the factors considered by the courts in determining whether a transaction constitutes a true sale are: the transfer of ownership risk and the level of recourse, the ability to identify the assets sold, the ability to calculate the purchase price and whether the return to the purchaser will be more than its initial investment and a calculated yield on such investment. In the case of a sale of receivables, other factors to be considered are the right to retain surplus collections, a right of redemption, the responsibility for collection of the accounts receivables and the ability of the vendor to extinguish the purchaser's rights from sources other than the collection of the receivables.

Intention of the Parties

40 The wording of the Agreement throughout clearly indicates the intention of both parties that the transaction be a true sale. The Agreement is clearly crafted to use the language of a sale throughout. There are no references to a loan or to security or to payments of principal or interest on a loan. The true nature of the transaction can be determined not only by the wording of the Agreement but can also be gleaned from an examination of how the relationship in fact transpired and the conduct of the parties. Although in certain cases, clear, unequivocal conduct of the parties may negate the intention as expressed by the wording of a contract, that would not appear to be applicable to the case at bar. The court must consider various aspects of the transaction to determine whether in law the transaction ought to be regarded as a sale or as a secured borrowing. That does not impact upon the express intention of the parties as demonstrated by the wording of the Agreement which clearly contemplates a sale. In addition, in looking at the factual matrix or context in which the transaction was entered into, it was clearly the intention of BC Tel that it be a sale in order to avoid any problems with breach of the NFAC contained in the Trust Deed under which the Bonds were issued. In the case of RAC, it was clearly the intention of RAC that the transaction be a sale in order to obtain the highest rating for the commercial paper issued by RAC to the public. It accordingly appears to me that both parties could only get the full benefit of the transaction if it was a true sale. It was the intention of both BC Tel and RAC that the transaction be a true sale and the conduct of the parties does not clearly and unequivocally negate that intention. If the court should determine that, in law, the transaction must be regarded as a secured borrowing, this would be a result not intended by the parties.

Ownership Risk and Recourse

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

41 In any true sale transaction, there must be a transfer of ownership risk to the purchaser. In the case of the sale of accounts receivable, the risk with regard to the non-payment of the receivable must pass to the purchaser subject to whatever forms of recourse the purchaser may have against the vendor. In *Major's Furniture Mart Inc. v. Castle Credit Corp.*, 602 F.2d 538 (U.S. C.A. 3rd Cir., 1979) the U.S. Court of Appeal (Third Circuit) stated at page 545:

> In the instant case the allocation of risks heavily favours Major's claim to be considered an assignor with an interest in the collectibility of its accounts. It appears that Castle required Major's to retain all conceivable risks of uncollectibility of these accounts. It required warranties that retail account debtors, e.g. Major's customers, meet the criteria set forth by Castle, that Major's performed the credit check to verify that these criteria were satisfied, and that Major's warrant that the accounts were fully enforceable legally and were "fully and timely collectible". It also imposed an obligation to indemnify Castle out of a reserve account for losses resulting from the customer's failure to pay, or for any breach of warranty, and an obligation to repurchase any account after the customer was in default for more than 60 days. Castle only assumed the risk that the assignor itself would be unable to fulfil its obligations. *Guarantees of quality alone, or even guarantees of collectibility alone, might be consistent with a true sale, but Castle attempted to shift all risks to Major's and incur none of the risks or obligations of ownership. It strains credulity to believe that this is the type of situation...in which there may be a "true sale of accounts...although recourse exists*". When we turn to the conduct of the parties to seek support for this contention, we find instead that Castle, in fact, treated these transactions as a transfer of a security interest.

42 It was the evidence of Mr. Edward Fujisawa, the former Director of the Securitization Group of CIBC World Markets Inc. with responsibility for RAC, that in reality RAC did not bear any of the risks of uncollectibility of the Purchased Receivables because of the requirement to replace defective receivables prior to termination and ineligible or defective receivables after termination of the Agreement and because of the size of the Reserve of 5% in contrast to BC Tel's historic bad debt ratio of between 1% and 2%.

43 It appears to me that for all practical purposes the only risk of uncollectibility assumed by RAC was the possibility of an insolvency of BC Tel and accordingly, the inability to be compensated by BC Tel in the event of Purchased Receivables in excess of the amount of the Reserve being uncollectible. Because of that possibility, however remote, RAC did assume some risk with respect to the collectibility of the Purchased Receivables.

44 The risks of ownership obviously decrease with the amount of recourse which the purchaser has, as against the vendor, in the event that the asset purchased is defective or subject to liens or encumbrances. In the case of the sale of accounts receivable, the recourse against the vendor would be with respect to uncollectibility of the accounts receivable. In the Schwarcz Article *supra*, the author states at page 621:

> The most significant factor appears to be the extent of recourse the transferee of the receivables has against the transferor. As the degree of recourse increases, the likelihood that a court will find a true sale decreases. The existence of some recourse does not by itself preclude characterization of the transaction as a true sale. If recourse is present, the issue is whether the nature of the recourse, and the true nature of the transaction, are such that the legal rights and economic consequences of the agreement bear a greater similarity to a financing transaction [that is, a secured loan] or to a sale.

45 In the case at bar, the Plaintiffs submit that, in addition to the right of RAC to have defective or ineligible receivables replaced both before and after termination, RAC is further protected by the overcollaterization provided by the Reserve in that the Reserve of 5% of the amount of Purchased Receivables is far in excess of the bad debt experience of BC Tel which was in the range of 1% to 2% during the years immediately prior to the date of the securitization transaction. The Plaintiffs

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

refer to the evidence of Mr. Fujisawa and submit that the only risk to which RAC was exposed is the insolvency of BC Tel under the provisions of section 2.08(5) of the Agreement which provide, in effect, that RAC will not receive less than the total amount of Outstanding Cash Payments, the Purchase Discount and the Program Fee unless there is an insolvency of BC Tel. The Plaintiffs, therefore, submit that the recourse available to RAC is not a recourse for collectibility but an economic recourse which is the equivalent of a warranty to the buyer of a return of its investment plus an agreed upon yield unrelated to the collectibility of the assets. The Plaintiffs concede that a resource for collectibility is consistent with a true sale of accounts receivable but that an economic recourse which ensures a return unrelated to the collectibility of the accounts receivable is indicative of a secured loan transaction where the receivables serve simply as collateral.

46 It is the submission of the Defendant that full recourse granted to a purchaser of an asset is not inconsistent with a true sale transaction and that warranties, representations and guarantees regularly provided by vendors of assets do not detract from the characterization of the transaction as a true sale of an asset. In both British and Canadian authorities it has been held that even full recourse is not incompatible with a concept of a legal sale. In *Welsh Development Agency*, *infra*, the purchaser was fully protected by way of recourse to the seller. Lord Justice Ralph Gibson, although concluding that no real risk passed from the seller to the purchaser, found that the transaction was nevertheless one of sale.

47 Purchasers regularly obtain recourse against vendors by way of representations, warranties and guarantees and, in the case of a sale of accounts receivable, a warranty or guarantee that the receivables are collectible. In an article co-authored by Stephen L. Schwarcz and others entitled "Rethinking the Role of Recourse in the Sale of Financial Assets" November, 1996, The Business Lawyer, Vol. 52, p. 159, the authors state at pages 160 to 161:

> Under contract law, parties generally are free to enter into and enforce any contract that is not illegal or against public policy; there is nothing about recourse, for example, that either is illegal or in violation of public policy... There is no legal or public policy which precludes a transferor from improving the value of an asset sold by adding its own guarantee. When a financial asset represented by a check or other draft is transferred, recourse is the common, accepted and sometimes mandatory consequence of transfer. Endorsement with recourse has never been viewed as precluding the existence of a sale ....
>
> In many cases involving the sale of financial assets, a true sale determination can be made even if the buyer were to have full or partial recourse to the seller for collectibility.

48 In the case at bar, the recourse given to RAC under the Agreement is that defective or uncollectible receivables will be replaced either by the transfer of further Eligible Receivables or by cash and the structure of the transaction is such that RAC will have recourse to such receivables or to cash to recoup the amounts advanced by it together with its cost of borrowing by way of the Purchase Discount and the agreed to Program Fee. It appears to me, however, that the effect of subsection 2.08(5) of the Agreement is that, after the termination date, if RAC determines that the Outstanding Purchased Receivables as of the termination date were less than the Required Amount, BC Tel may, as its option, either pay the difference in cash to RAC or transfer additional Eligible Receivables to RAC to ensure that as of the termination date the Outstanding Purchased Receivables equalled the Required Amount; however, if after the termination date, such Outstanding Purchased Receivables should become uncollectible to an amount in excess of the Reserve, RAC has no further recourse against BC Tel for the amount of such excess.

49 This recourse therefore appears to me to be clearly a recourse as to collectibility and not what the Plaintiffs have defined as an economic recourse which will guarantee a return on an investment regardless of the quality of the assets sold. The recourse available to RAC under the Agreement is not in all events a full recourse with respect to collectibility and is not an economic recourse in the sense of a guarantee of repayment of the Outstanding Cash Payments and a calculated yield thereon. The recourse available to RAC does not therefore preclude a determination that the securitization transaction was a

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

sale of the Purchased Receivables.

50 The fact that RAC had a backup credit enhancement arrangement with a Swiss bank to the extent of a further 10% of the Purchased Receivables does not, in my view, impact on an analysis of the Agreement with respect to assumption of risk and recourse as between RAC and BC Tel. I regard the credit enhancement arrangement as a type of insurance taken out by RAC in the event of uncollectible Purchased Receivables exceeding the amount of the Reserve.

Right to Surplus

51 An analysis of the Agreement leads to the conclusion that RAC is entitled to receive the amount of the Outstanding Cash Payments, the Purchase Discount and a Program Fee calculated as a percentage of the Outstanding Cash Payments, indemnification for legal costs up to $50,000 and for various other costs and expenses and nothing more. To the extent that collections of the Purchased Receivables exceeded that total, the surplus remains with BC Tel. Collections of Purchased Receivables are notionally held in trust by BC Tel for RAC. The Agreement provides that, once the total amount payable to RAC under the Agreement has been paid after the termination date, RAC shall either pay BC Tel the Deferred Amount outstanding or return excess Purchased Receivables in that amount to BC Tel. RAC does not have, therefore, the right to any amount collected on the Purchased Receivables beyond the repayment of amounts advanced by it, certain payments calculated as a percentage of such amounts and specific reimbursement of certain costs and expenses. If, on termination, RAC is paid all amounts payable to it pursuant to the Agreement and collections on the Purchased Receivables exceed that amount, RAC is required to pay the surplus either in cash to BC Tel and/or to return surplus Purchased Receivables to BC Tel.

52 The Schwarcz Article, *supra*, states at page 622:

> Several courts also have considered the existence of a transferor's right to any surplus collections, once the transferee has collected its investment plus an agreed yield, as indicative of secured loan. The right of the transferee of the receivables to retain all collections of transferred receivables for its own account, even after the transferee has collected its investment plus yield, would therefore be a factor in favour of characterization of the receivables transaction as a true sale.

53 It is the submission of counsel for the Plaintiffs that the fact that such surplus is returnable to BC Tel is conclusive of the issue as to whether the securitization transaction is a loan as opposed to a sale.

54 In leading English cases, the inability of the purchaser to retain surplus has not been found to be fatal to the characterization of a transaction as a true sale. In *Inglefield Ltd., Re*, [1933] Ch. 1 (Eng. C.A.), in analyzing a financing agreement, Lord Hanworth, M.R. stated at pages 19 and 20:

> Eve J. [the judge at first instance from whom the appeal was successfully taken] found in clause 18 a factor which was consistent, to his mind, only with the transaction being one of charge, but when the clause is examined and understood it seems impossible to attribute such an effect to it. It provides that after the discount company shall have received from the hirer, or the dealer (that is George Inglefield, Ltd.), in respect of all the hire purchase Agreements comprised in the assignment, sums amounting in the aggregate to the purchase price paid by the discount company under the terms of the assignment, that company is to allow the dealer to retain all the subsequent installments of rent, or other monies, if any,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> due from the hirer, and shall account to the dealer for such sums. If then one approaches clause 18 without any prejudice, either one way or the other, it really amounts to more than that when the discount company have been paid more than they are entitled to receive under the assignment to them of the benefit of the hire purchase agreement, they will pay the excess to George Inglefield, Ltd. That is because the discount company are not entitled to retain payments in excess of those to which they were entitled under the hire purchase agreement. I cannot find from that clause any sufficient ground for treating this assignment as a charge.

55 Similarly, in *Welsh Development Agency v. Export Finance Co.* ("Export"), [1992] B.C.L.C. 148 (Eng. C.A.), the English Court of Appeal was analyzing an agreement pursuant to which funding was provided by Export Finance Co. Ltd. ("Exfinco") to Parrot Corp. Ltd. ("Parrot") which carried on the business of exporting computer discs. The agreement was somewhat complicated but provided that, when Parrot entered into a transaction to sell goods to an overseas buyer, Exfinco made a standing offer to buy such goods and Parrot would sell the goods, as Exfinco's agent, to the overseas buyer. The agreement contained a termination provision which provided that on termination Parrot would satisfy all amounts owing to Exfinco by the overseas buyers and Exfinco would then transfer all interest it had in the goods to Parrot. The financing arrangements were such that Exfinco received only an amount related to the duration of the financing made available by Exfinco. In responding to the submission of Exfinco that the agreement nevertheless constituted a true sale of the goods as between Parrot and Export, Ralph Gibson L.J. stated at page 177:

> Nevertheless, I see no answer to Exfinco's contention that they were under our law entitled to enter into the agreement in the terms therein set out; that no principle of our law is apt to deprive them of the benefit of the rights and obligations thereby created; and that the fact that the provisions of the master agreement were designed to protect Exfinco from any commercial risk on the sale of Parrot's floppy discs, and to contain any commercial profit to a sum demonstrably related to the duration of the financial provisions made available, does not alter the nature of the rights and obligations created by the master agreement.

56 Accordingly, it does not appear to me that the absence of a right in RAC to retain the surplus from the collection of accounts receivable is fatal to a determination that the securitization transaction between BC Tel and RAC was a true sale of the Purchased Receivables.

Determination of Purchase Price

57 As stated above, "Purchase Price" is not a defined term in the Agreement. Subsection 2.01(3) of the Agreement provides that, in effect, the purchase price for any Purchased Receivables will be comprised of the immediate cash payment made by RAC on the purchase of any receivables and the "Deferred Amount". The "Deferred Amount" is not defined in the Agreement. It then becomes necessary to find a provision of the Agreement which would give meaning to the term "Deferred Amount". I accept the Defendant's submission that the only provision of the Agreement which could be referred to is Subsection 2.07(2) which in effect provides that, on termination of the Agreement and the completion of the liquidation of the Purchased Receivables, one can determine what portion of the Reserve is not required to be applied to compensate RAC for uncollectible Purchased Receivables and that the unused portion of the Reserve is the Deferred Amount as referred to in the definition of purchase price. Accordingly, it appears to me that, on any given day during the term of the Agreement, if the Agreement was terminated it would be possible to calculate the purchase price for the Purchased Receivables held by RAC as of that date.

58 I am also not satisfied that fluctuations in the amount of the Purchase Discount results in an indeterminable purchase price. The Agreement clearly indicates that the Purchase Discount is not part of the purchase price of the Purchased Receivables. The Purchase Discount is defined in the Agreement as an amount calculated for each settlement period

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(generally one month) based upon the weighted average Outstanding Cash Payments and the adjusted cost of funds to RAC. RAC will notify BC Tel of the Purchase Discount as soon as practicable after the first day of each settlement period. It is, in my view, beyond dispute that the Purchase Discount represents the reimbursement by BC Tel to RAC of RAC's costs of borrowing the funds advanced to BC Tel pursuant to the Agreement and does not bear any direct relationship to the amount of Outstanding Purchased Receivables or form part of the purchase price thereof.

59 Counsel for the Plaintiffs appears to take the position that, because RAC acquires Purchased Receivables with a face amount in excess of the total amount advanced by RAC to BC Tel, the Purchase Discount accordingly becomes a discount off the purchase price rather than a payment to compensate RAC for its costs of funds. I am unable to accept this submission. The amount of the Purchase Discount is clearly based upon the cost of funds to RAC and bears no relationship to the 5% spread (the "Reserve") between the face amount of the receivables purchased by RAC and the total advances made by RAC to BC Tel which is established to protect RAC against uncollectible receivables.

60 I, therefore, do not accept the submission of counsel for the Plaintiffs that the provisions of the Agreement result in a "sale in which the purchase price is unknown to the parties". A certainty of purchase price is a fundamental element of a sale transaction and in my view, the purchase price of the subject matter of the transaction between BC Tel and RAC on any given day can be determined and accordingly, the transaction does not fail to qualify as a sale by virtue of uncertainty of purchase price.

Identification of Assets

61 As a result of the inter-relationship among Outstanding Cash Payments, Purchase Discount and Reserve and the provisions of the Agreement relating to Cessation Requests and Eligible Receivables, it is acknowledged by both parties that a Particular Receivable may be a Purchased Receivable on day 1, not be a Purchased Receivable on day 2, and again be a Purchased Receivable on day 3 with the result that title to such receivable will move back and forth between BC Tel and RAC. The Plaintiffs submit that such provision is inconsistent with a true sale. They rely on certain authorities concerned with the characterization of a general assignment of book debts (a "GABD") as an absolute assignment or as a security agreement. In *Canada Trustco Mortgage Corp. v. Port O'Call Hotel Inc.* (1996), 27 B.L.R. (2d) 147 (S.C.C.) Cory, J. stated at p.167:

> I agree with the MNR that what the actual equity of the borrower in the book debts may be from time to time is irrelevant for the purpose of determining the legal effect of the equity of redemption. It would be absurd if a company were to fluctuate between having title and not having title to their book debts based on their ratio of debt to assets. Yet if a GABD is treated as an absolute assignment, this can be the only result, as the bank is limited to recovering the amount of the loan. Since the bank could not recover any book debts if the company had a surplus in their account, the book debts would belong to the company. When there was a deficit, some or all of the book debts would belong to the bank. Such a fluctuating state of affairs is inconsistent with the certainty required in commercial matters. I believe that the correct view is that a GABD represents a security interest with the legal title being with the lender and the equitable title remaining with the borrower. This is supported both by the jurisprudence and by the wording of the section.

62 In my view, the jurisprudence relating to the characterization of GABDs as security agreements is not determinative of the issue before this court with respect to the subject matter of the sale of receivables by BC Tel to RAC being ascertainable. In *Canada Trustco Mortgage Corp. v. Port O'Call Hotel Inc.* , *supra*, Cory, J. concluded that it would be inconsistent with the purpose and intention of a GABD to find that it was an absolute assignment or sale of the book debts to the lender and would be inconsistent with the purpose of the transaction and the intention of the parties. In that case, the court was not concerned with the ascertainment of receivables but with the nature of the assignment of ascertained or ascertainable

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

receivables in respect of which there was stated to be an "equity of redemption".

63 In the case at bar, clearly the intention of the parties as stated in the Agreement was to construct a sale transaction with title to the receivables passing to RAC, subject only to reconveyance in certain events contemplated by the Agreement. If one follows the procedure set out in the Agreement with respect to the General Trial Balance, on any particular day, it is possible to determine exactly which receivables constitute Purchased Receivables and accordingly, the subject matter of the sale of receivables by BC Tel to RAC is ascertainable on any given day. The fact that the Agreement contemplated that a particular receivable may, under certain circumstances, be reconveyed to BC Tel, does not, in my view, derogate from the fact that the original conveyance of the receivable to RAC was a true sale. Accordingly, in my view, the subject matter of the sale of receivables from BC Tel to RAC being ascertainable on any particular day satisfies the requirement that the subject matter of the sale must be ascertainable.

Collection of Receivables

64 The effect of Article 5 of the Agreement is that BC Tel carries out all servicing and collection of the Purchased Receivables as agent for RAC and receives no fee for performing such services. RAC may not replace BC Tel as its collection agent unless there has been a default under the Agreement. The Plaintiffs submit that these provisions are a further indication that the transaction is one of secured borrowing rather than sale. In the Schwarcz Article, *supra*, the author states at page 623:

> In practice, the seller often is appointed as the collection agent initially. This is not necessarily inconsistent with sale characterization if (1) the seller as collection agent, will be acting as an agent for the purchaser pursuant to established standards, much like any other agent, (2) the seller will receive a collection agent fee that represents an arm's length fee for these services, and (3) the purchaser has the right at any time to appoint itself or another person as collection agent in place of the seller.

65 I am not satisfied that the criteria set out by Mr. Schwarcz are determinative of the nature of the transaction between BC Tel and RAC. The Agreement clearly provides that BC Tel will service and collect the Purchased Receivables as agent for RAC and sets out standards of performance. With respect to the payment of a fee, it was the evidence of Mr. Dorwart, the former Assistant Treasurer of BC Tel, that BC Tel was prepared to provide these services without a fee in view of the fact that the fee would have, in any event, been reflected in the purchase price which BC Tel would receive for the Purchased Receivables.

66 It also seems to me that there is no logical reason why the fact that RAC cannot remove BC Tel as the collector of the Purchased Receivables so long as it is complying with the Agreement should be fatal to a determination that the transaction between BC Tel and RAC was a sale transaction. For practical purposes, it would seem to me to be both logical and efficient for BC Tel to continue to collect the Purchased Receivables and deal with the debtors.

67 Accordingly, in my view, the provisions of the Agreement relating to the collection of the Purchased Receivables by BC Tel on behalf of RAC are not inconsistent with a sale transaction.

Right of Redemption

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

The courts have determined that, where the vendor of an asset has a right of redemption or repurchase at its option, this will be a strong factor in favour of the characterization of a receivable transaction as a secured loan rather than a true sale transaction. An essential term of a secured loan transaction is the right of the borrower, upon repayment of the debt, to require the lender to reassign to it all of the lender's interests in the assets secured to pay the debt. In the case of a true sale, the vendor has no right to require title to the assets sold to be reassigned to it. In my view, this is the ultimate test to be applied to determine whether a particular transaction should be interpreted as a secured loan or as a true sale. The Plaintiffs submit that the Agreement grants to BC Tel the right to repurchase the Purchased Receivables from RAC in the event of a "Change in Circumstances" as defined in the Purchase Agreement and that the Agreement also provides that, after the Final Collection Date, RAC has the option of paying the Deferred Amount to BC Tel or transferring Purchased Receivables in that amount back to BC Tel. It was the evidence of witnesses for both parties that the usual practice was that on termination the Deferred Amount would normally be paid by the purchaser transferring Purchased Receivables back to the vendor. The Plaintiffs also submit that if the rights of the transferee of an asset can be extinguished upon repayment to the transferee of amounts advanced by it from a source other than the realization of the assets transferred, that is indicative of the transaction being a loan and not a sale of the subject assets and point out that all amounts paid by BC Tel to RAC during the term of the Agreement were paid out of general funds and not directly traceable to the proceeds of the collection of the Purchased Receivables by BC Tel which were not segregated from BC Tel's general funds.

68 Subsection 2.07(2) of the Purchase Agreement provides in effect that after termination of the Agreement and the payment to RAC of all amounts payable to it under the Purchase Agreement, RAC may, at its option, either pay the Deferred Amount to BC Tel in case or transfer to BC Tel Purchased Receivables in a total face amount equal to the Deferred Amount. I have difficulty interpreting this as a right of redemption in favour of BC Tel. Clearly, it is at the option of RAC as to whether it wishes to pay the Deferred Amount in cash and retain the excess Purchased Receivables or to transfer the excess Purchased Receivables back to BC Tel. The authorities cited by the Plaintiffs with respect to a right of redemption all appear to me to be situations where the assignor of the receivables was entitled at its election to redeem or repurchase the receivables upon payment of a specified amount to the assignee. In describing the fact situation in *Canada Trustco Mortgage Corp. v. Port O'Call Hotel Inc.*, *supra*, Cory, J. stated at page 156:

> Further, all the assignments limit liability to the extent of the outstanding indebtedness. Thus, if the loan secured by the GABD was repaid by the Bank or Treasury Branch would have no further interest in the assignment. The documents themselves refer to the assignment as being a continuing collateral security for the payment of the indebtedness. The clear intention of the parties is that the assignment is given as security for the payment of a debt and upon payment of the debt the GABD is to be of no force or effect. That is to say the lending institution could not, after payment of the debt, make use of the GABD to realise upon any of the book debts of the assignor. In my view since the assignment by its terms can be redeemed by payment of the debt it cannot or at least should not be construed as an absolute assignment.

69 That is not our case. Nowhere in the Agreement is BC Tel given any right at its option to repurchase or redeem the Purchased Receivables upon payment of a specified amount of RAC. The only instance in which BC Tel has the right to repurchase the Purchased Receivables is in the event of a "Change In Circumstances" as defined in section 7.06 of the Agreement. Section 7.06 provides that, in the event of any change in law which has the effect of increasing the cost to RAC of complying with its obligation to Purchased Receivables under the Agreement or reducing the rate of return to RAC in connection therewith, BC Tel will upon demand by RAC pay to RAC such increased costs or reduction in rate of return provided that if RAC makes such a demand upon BC Tel, BC Tel may, at its option, terminate the Purchase Agreement on written notice to RAC by repurchasing the Purchased Receivables for an amount equal to the Outstanding Cash Payments, the Purchase Discount and all other amounts payable to RAC pursuant to the Agreement. This again does not appear to me to be a right of redemption or repurchase granted to BC Tel and exercisable at its option. It only becomes operative in the event of a Change of Circumstances as defined and then only upon a demand being made by RAC to reimburse it for the effect upon it of such Change of Circumstances.

70 The Plaintiffs have also made reference to the Cessation Requests provided for in the Agreement which enable BC Tel

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

at any time to request that RAC cease purchasing receivables until such time as the amount of Purchased Receivables matches the Required Amount. Section 2.05 of the Agreement provides that BC Tel may deliver Cessation Requests from time to time in amounts in multiples of $1,000,000 up to a total aggregate amount of $75,000,000. Upon delivery of such a Cessation Request by BC Tel, RAC shall cease to purchase receivables until such time as the amount of the Outstanding Cash Payments has been reduced to the amount specified by BC Tel in the Cessation Request. It is clear from the wording of the Agreement that the exercise by BC Tel of its right to make Cessation Requests does not result in the redemption or repurchase by BC Tel of Purchased Receivables.

71 Even on the termination of the Agreement, BC Tel has no right to elect to repurchase Purchased Receivables in payment of the Deferred Amount. RAC may elect either to pay the Deferred Amount in cash or to retransfer Purchased Receivables to BC Tel. The evidence before this court was that on termination of the Purchase Agreement, RAC will continue to collect the Purchased Receivables and will pay BC Tel the Deferred Amount in cash.

72 Accordingly, I am unable to conclude that the Agreement grants to BC Tel any right of repurchase or redemption of accounts receivable at its option so as to lead to the conclusion that the securitization transaction is a secured loan transaction rather than a true sale.

73 I, therefore, conclude that none of the factors to be considered by the court in determining whether the securitization transaction in this instance was a true sale or a secured loan transaction negates the clear wording of the Agreement and the clear intention of the parties that the transaction be a true sale of receivables from BC Tel to RAC.

Oppression

74 The Plaintiffs in this action also seek relief pursuant to the oppression remedy provisions of section 241 of the *Canada Business Corporations Act*, R.S.C. (1985) c. C-44 (the "CBCA") and submit that the determination of the directors of BC Tel to effect a redemption of the Bonds through the proceeds of the securitization transaction with RAC unfairly disregarded the interests of the Plaintiffs as security holders of BC Tel. It is agreed that in order to find conduct which unfairly disregards the interest of security holders of a corporation, the Plaintiffs need not prove *male fides* on the part of the directors of the corporation and that the reasonable and legitimate expectations of security holders must be considered by the court in determining whether the oppression remedy is applicable. The concept of "reasonable and legitimate expectations" is defined by Kerans, J.A. in *Westfair Foods Ltd. v. Watt* (1991), 5 B.L.R. (2d) 160 (Alta. C.A.) at page 702 as follows:

> One deserving case is where the person to whom the profit will go has nourished that hope. The company and the shareholders entered voluntarily, not by duty or chance, into a relationship. Our guides are the rules in other contexts, such as contract law, equity and partnership law, where the courts have also considered just rules to govern voluntary relationships. In very general terms, one clear principle that emerges is that we regulate voluntary relationships by regard to the expectations raised in the mind of a party by the word or deed of the other, and which the first party ordinarily would realize it was encouraging by its words and deeds. This is what we call reasonable expectations, or expectations deserving of protection. Regard for them is a constant theme, albeit variously expressed, running through the cases on the section or its like elsewhere. I emphasize that all the words and deeds of the parties are relevant to an assessment of reasonable expectations, not necessarily only those consigned to paper, and not necessarily only those made when the relationship first arose.

75 In the case at bar, it is conceded that the prospect of a securitization transaction was not in the contemplation of BC Tel

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

or the Bondholders at the time that the Trust Deed was entered into or at the time that the Bonds were issued. The evidence before this court, and particularly that of Ms. Shaw of Sun Life, was that the Plaintiffs purchased the Bonds on reliance in part on the NFAC contained in the Trust Deed and with the understanding that the Bonds could not be redeemed, other than for sinking fund or improvement fund purposes, through the proceeds of borrowings by BC Tel at a lower interest rate. Ms. Shaw conceded, however, that the Bonds could be redeemed from the proceeds of a sale of assets and that was understood by Sun Life at the time that the Bonds were purchased. The evidence also establishes that, although the directors of BC Tel were aware at the time that the redemption of the Bonds was approved, that there would be an adverse reaction on the part of the Bondholders and that there was a risk of the redemption being challenged by legal action, they proceeded with the redemption based on legal, tax, and accounting advice that the transaction could be legitimately treated as a sale and that any legal challenge to the transaction would, in all probability, be unsuccessful. The directors also approved the redemption on the basis that there were substantial financial advantages to the company in the reduction of interest costs and capital tax and that it was clearly in the best interests of the company, and therefore of its shareholders, to enter into the securitization transaction and apply the proceeds to the redemption of the Bonds.

76 It appears to me that, in the context of the case at bar, the reasonable and legitimate expectations of the Plaintiffs when they purchased the Bonds have been frustrated not by the action of the directors in approving the securitization transaction and the redemption of the Bonds from the proceeds of such transaction but rather by the fact that securitization developed as a financing mechanism after the Bonds were purchased and the courts to date have not interpreted such transactions as being borrowing transactions and not true sales.

77 The decision of the directors of BC Tel to take advantage of the opportunity provided by securitization also raises the issue of the directors taking action which is in the best interests of the company, and therefore of the shareholders, but may be to the disadvantage of other security holders, in this case, the Bondholders. In this regard, I would adopt the statement of Weiler, J.A. in *Pente Investment Management Ltd. v. Schneider Corp.* (1998), 42 O.R. (3d) 177 (Ont. C.A.)at page 191 as follows:

> However, acting in the best interests of the company does not necessarily mean that the directors must act in the best interests of one of the groups protected under s.234. There may be a conflict between the interests of individual groups of shareholders and the best interests of the company. *Brant Investments v. Keep Rite* (1987), 60 O.R. (2nd) 737 ... affirmed (1991), 3 O.R. (3d) 289 at 301 ... Provided that the directors have acted honestly and reasonably, the court ought not to substitute its own business judgment for that of the Board of Directors. *Brant Investments, supra.* ...

78 I am, therefore, of the view, that the reasonable legitimate expectations of the bondholders were not frustrated by the entering into of the securitization transaction and the subsequent redemption of the bonds in that the Bondholders were aware that the Bonds could be redeemed by application of the proceeds of a sale of assets. I further find that the actions of the directors were in the best interests of the corporation and its shareholders and accordingly, although to the disadvantage of the Bondholders, do not constitute oppressive conduct giving rise to any remedy pursuant to the provisions of the CBCA.

Disposition

79 On the issues in this action I find as follows:

1. the redemption of the Bonds was not a refunding operation by BC Tel by the indirect application of borrowed funds,

2. the redemption of the Bonds was not a refunding operation by BC Tel by the direct application of borrowed funds in

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

that the securitization transaction was in law a true sale and not a secured borrowing,

3. the redemption of the Bonds by BC Tel did not affect the result that unfairly disregarded the interests of the Bondholders so as to give rise to an oppression remedy.

80 The action is dismissed. Counsel may make brief written submissions as to the costs of this action to me on or before February 28, 2003.

Action dismissed.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 3

2000 CarswellOnt 2824
Ontario Superior Court of Justice

Access Cash International Inc. v. Elliot Lake & North Shore Corp. for Business Development

2000 CarswellOnt 2824, [2000] O.J. No. 3012, 1 P.P.S.A.C. (3d) 209

Access Cash International, Inc., Applicant and Elliot Lake and North Shore Corporation for Business Development, Respondent

Molloy J.

Heard: August 27, 1999
Heard: September 23, 1999
Judgment: August 11, 2000
Docket: 99-CL-3404

Counsel: *Robyn M. Bell*, for Applicant.
Alex L. MacFarlane, for Respondent.

Subject: Corporate and Commercial; Insolvency

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Personal property security --- Scope of legislation — Consignments

Applicant owned, leased and sold automated teller machines — Bankrupt was exclusive Canadian distributor of applicant's ATMs — Respondent supplied credit facilities to bankrupt for which it took two general security agreements, two general assignments of book debts and chattel mortgage over bankrupt's assets — Applicant supplied 173 ATMs to bankrupt between September 1998 and February 1999 for which it had not been paid — Applicant and bankrupt signed Purchase Money Security Interest Agreement in January 1999 — PMSI registered under Personal Property Security Act on January 18, 1999 and served on respondent on January 21, 1999 — Bankrupt made assignment in bankruptcy in April 1999 — Applicant claimed to have ownership interest in ATMs because they were delivered to bankrupt on consignment — To escape priority provisions of PPSA applicant must have supplied ATMs on consignment and consignment must not have been designed to secure payment — Nothing in Placement Agreement between applicant and bankrupt was consistent with it being consignment agreement — One of principle features of consignment agreement is that merchant under no obligation to pay for goods until they are sold to third party — Bankrupt required to pay for any machine returned by retailer within 30 days — No stipulation in Placement Agreement that title to remain in applicant — No requirement that any proceeds received by bankrupt are held in trust for applicant — No right in applicant to demand return of good at will — No right of inspection — Applicant did not own most of ATMs and did not have any priority except through its registered PMSI — Distributorship agreement between applicant and bankrupt did provide that title to remain in applicant although many other indicia of consignment absent —

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Agreement expressly reserved title in goods to applicant until such time as they were removed from warehouse — Applicant had established ownership interest in ATMs stored in bankrupt's warehouse which never left warehouse for purpose of delivery to third party under sales, trial or placement programs — Applicant's interest in those ATMs not subject to PPSA — Personal Property Security Act, R.S.O. 1990, c. P.10.

Table of Authorities

Cases considered by *Molloy J.*:

Askin, Re (1960), 1 C.B.R. (N.S.) 153 (Ont. S.C.) — referred to

Farwest Systems Corp. (Receiver of) v. Omron Business Systems Inc. (1988), 69 C.B.R. (N.S.) 82 (B.C. S.C.) — considered

Glengarry A.E.T. Inc. (Trustee of) v. Manhattan Electric Cable Corp. (1986), 6 P.P.S.A.C. 112 (Ont. S.C.) — considered

H & I Carpet Corp., Re (1983), 49 C.B.R. (N.S.) 158 (Ont. S.C.) — referred to

Langley v. Kahnert (1905), 36 S.C.R. 397 (S.C.C.) — referred to

Now Generation Ltd., Re (1969), 13 C.B.R. (N.S.) 194 (Ont. S.C.) — referred to

Revere Electric Inc., Re (1993), 5 P.P.S.A.C. (2d) 39, 13 O.R. (3d) 637, 19 C.B.R. (3d) 29 (Ont. Bktcy.) — referred to

Richardson v. S.K. Dry Goods Co. (1931), 13 C.B.R. 38 (Ont. S.C.) — referred to

Rivabo Truck Bodies Ltd., Re (1975), 20 C.B.R. (N.S.) 252 (Ont. S.C.) — referred to

Seven Limers Coal & Fertilizer Co. v. Hewitt (1985), 52 O.R. (2d) 1, 10 O.A.C. 132, 5 P.P.S.A.C. 45, 56 C.B.R. (N.S.) 319 (Ont. C.A.) — applied

Stephanian's Persian Carpets Ltd., Re (1979), 1 P.P.S.A.C. 71, 31 C.B.R. (N.S.) 196 (Ont. S.C.) — considered

Stephanian's Persian Carpets Ltd., Re (1980), 1 P.P.S.A.C. 119, 34 C.B.R. (N.S.) 35 (Ont. Bktcy.) — considered

Toronto Dominion Bank v. Leigh Instruments Ltd. (Trustee of) (1998), 40 B.L.R. (2d) 1 (Ont. Gen. Div. [Commercial List]) — referred to

Toyerama Ltd., Re (1980), 1 P.P.S.A.C. 126, 34 C.B.R. (N.S.) 153 (Ont. Bktcy.) — considered

Vitrerie Claveau Glass Inc., Re (1962), 3 C.B.R. (N.S.) 150 (Que. S.C.) — referred to

Statutes considered:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Personal Property Security Act, R.S.O. 1980, c. 375
Generally — referred to

Personal Property Security Act, R.S.O. 1990, c. P.10
Generally — considered

s. 2(a) — considered

s. 2(a)(ii) — considered

s. 46(5) — considered

APPLICATION claiming ownership interest in personal property.

Molloy J.:

A. Background

1 The parties are the two principal secured creditors of Revenue Plus Limited ("Revenue Plus"), a bankrupt. The applicant claims that it has an ownership interest in certain automated cash teller machines previously in the possession of Revenue Plus and a prior security interest in respect of certain of the machines that is superior to that of the respondent.

2 The applicant ("Access Cash") is a Minnesota company that owns, leases and sells automated teller machines (ATMs). It is, apparently, the largest non-bank deployer of ATMs in the United States.

3 Revenue Plus was the exclusive Canadian distributor for Access Cash ATMs. It also dealt in ATMs from other suppliers. Prior to its bankruptcy, Revenue Plus was principally in the business of supplying ATMs to various merchants. Revenue Plus would also enter into servicing and processing contracts with those merchants pursuant to which it would service the ATMs as required and process the ATM transactions for a fee. In addition to its ATM business, Revenue Plus operated a "Call Centre" which managed calls in respect of transactions involving ATMs.

4 The respondent ("ELNOS") is a company incorporated for the purpose of promoting business development in a number of Northern Ontario communities. In 1997 and 1998, ELNOS supplied credit facilities to Revenue Plus, for which it took various forms of security (two general security agreements, two general assignments of book debts and accounts, and a chattel mortgage over Revenue Plus's assets). Notice of the ELNOS security interest was registered in November 1997 and September 1998.

5 Access Cash supplied 173 ATMs to Revenue Plus on a number of occasions between September 1998 and February 1999, for which it has not been paid. Initially, these machines were delivered on the basis of oral agreements between the parties. A draft agreement confirming the oral arrangements was prepared in October 1998 but the formal written agreements were not signed until January 11, 1999. On January 7, 1999, Access Cash and Revenue Plus signed a Purchase Money

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Security Interest Agreement. The PMSI was registered under the *Personal Property Security Act* ("PPSA") on January 18 and served on ELNOS on January 21, 1999. Eighteen ATMs were delivered to Revenue Plus after ELNOS had notice of Access Cash's PMSI.

6 It is conceded that Access Cash has a security interest in the ATMs delivered after ELNOS was given notice of the PMSI and that Access Cash's interest in that regard has priority to that of ELNOS.

7 Revenue Plus made a voluntary assignment into bankruptcy on April 6, 1999 and KPMG Inc. was appointed as trustee of its assets. The assets in the control of the trustee include ATMs supplied by Access Cash.

8 The dispute between Access Cash and ELNOS can be simply stated: Access Cash claims that it owns the ATMs because they were delivered to Revenue Plus on consignment; ELNOS disagrees.

B. The Applicable Law

The PPSA

9 The PPSA applies to "every transaction without regard to its form ...that in substance creates a security interest": s.2(a) of the PPSA. This is stipulated to include a "consignment that secures payment or performance of an obligation": s.2(a)(ii).

10 Access Cash maintains that it is the owner of the ATMs in question because it supplied them to Revenue Plus on consignment with title remaining in Access Cash. To escape the priority provisions of the PPSA, the ATMs must have been supplied on consignment *and* the consignment must not have been designed to secure payment. It is generally accepted that determining whether the PPSA applies involves a two-part test. First, is the arrangement between the parties truly a consignment as opposed to a sale? Second, if it is a consignment agreement, does it secure payment or performance of an obligation? *Stephanian's Persian Carpets Ltd., Re* (1980), 34 C.B.R. (N.S.) 35 (Ont. Bktcy.), at 37-38; *Revere Electric Inc., Re* (1993), 5 P.P.S.A.C. (2d) 39 (Ont. Bktcy.), at 45.

Onus of Proof

11 Both parties agree, and the case law establishes, that the onus of proving a transaction is a consignment rather than a sale is on the person alleging consignment, *i.e.* in this case, Access Cash. ELNOS asserts that the onus of proof remains on Access Cash for both parts of the test; Access Cash contends that the onus shifts to the respondent for the second branch of the test. In other words, Access Cash argues that if it discharges its primary onus by proving it provided the ATMs to Revenue Plus under a consignment agreement, the onus is then on ELNOS to prove the consignment agreement was a means of securing payment and therefore caught by the Act.

12 Access Cash relies upon the decision of Registrar Ferron in *Stephanian's Persian Carpets Ltd., Re* (1979), 31 C.B.R. (N.S.) 196 (Ont. S.C.), as affirmed on appeal by Saunders J. (1980), 34 C.B.R. (N.S.) 35 (Ont. Bktcy.). In *Stephanian's Persian Carpets Ltd.* the trustee in bankruptcy applied for a declaration that the claim advanced by the supplier

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Anglo-Oriental Rugs Ltd was subordinate to the interest of the trustee. The decision of Registrar Ferron is brief. He did not deal with whether the agreement pursuant to which the carpets were supplied was a true consignment agreement. (It would appear this was not seriously contested by the trustee.) His focus was entirely upon whether the intention of the parties to the contract was to create a security interest. He held that the "onus is on the trustee to show that the intention of the transaction between the bankrupt and the respondent was to create security". He then stated there was no evidence as to the intention of the parties and therefore dismissed the trustee's motion. It is clear that Registrar Ferron did place the onus on the trustee on this issue and that the question of onus, in the circumstances, determined the result. However, there is no discussion in the decision as to why the onus should be on the trustee and no reference to any authority in that regard. Registrar Ferron did not refer to there being two branches to the test and therefore cannot be taken to have addressed his mind to the issue of a shifting onus.

13 On appeal, Saunders J. reached the same result as did Registrar Ferron (*i.e.* that the goods were supplied pursuant to a consignment agreement not intended as security), but he arrived there by a very different route. Saunders J. set out the two-part test and dealt with both parts of the test in some detail. However, he made no reference to the reasons for decision of Registrar Ferron and did not mention the issue of onus of proof. It would appear from his reasons that the issue of onus did not play a pivotal role in his decision. In these circumstances, it is not clear that the Registrar's decision with respect to onus has been upheld by a higher court.

14 I was not referred to any authority clearly delineating a two-part test with a shifting onus; nor was I referred to any case (other than the decision of Registrar Ferron in *Stephanian's Persian Carpets Ltd.*) in which the onus of proving any aspect of a consignment agreement was placed on the party disputing the consignment. The decision of Registrar Ferron was a marked departure from the existing case law, in which the onus of proof in respect of consignment agreements had always been placed on the party asserting the consignment, often with the comment that it is a very heavy onus: *Askin, Re* (1960), 1 C.B.R. (N.S.) 153 (Ont. S.C.); *Vitrerie Claveau Glass Inc., Re* (1962), 3 C.B.R. (N.S.) 150 (Que. S.C.); *Now Generation Ltd., Re* (1969), 13 C.B.R. (N.S.) 194 (Ont. S.C.); *Rivabo Truck Bodies Ltd., Re* (1975), 20 C.B.R. (N.S.) 252 (Ont. S.C.) (Registrar Ferron); *Seven Limers Coal & Fertilizer Co. v. Hewitt* (1985), 52 O.R. (2d) 1 (Ont. C.A.).

15 In an article entitled "Consignment Sales and the Personal Property Security Act", published just two years after the *Stephanian's Persian Carpets Ltd.* decision at [1981-82] 6 Can. Bus. Law J. 40, Brian Colburn comments as follows on the onus issue (at pp.68-69):

> A significant practical point relating to the characterization issue has arisen recently. In discussing earlier the common law background on consignments, it was noted that the "positioning of the onus of proof became crucial". The Ontario Registrar in Bankruptcy in his decision in *Stephanian Persian Carpets Ltd., Re* determined that the onus is on the applicant trustee to show that the intention of the transaction ...was to create security. This, of course, is a change from the position consistently taken since *Askin, Re*. Because the characterization issue is essentially one of fact, or of mixed fact and law, the shifting of the burden to the party impeaching the transaction may prove to be one of the more significant elements in future contests.

16 In my opinion, the decision of the Court of Appeal in *Seven Limers Coal & Fertilizer Co. Inc. v. Hewitt* (1985), 52 O.R.(2d) 1 is determinative of this issue. This decision was five years after *Stephanian's Persian Carpets Ltd.* but does not refer to it. The issue before the Court was whether the plaintiff had supplied the goods in question to Hewitt "under consignment, not intended as security" such that it was not covered by the PPSA: see p. 4. The Court of Appeal was unequivocal in placing the burden of proof on the plaintiff. Although the Court did not break the test into two components (as was done in *Stephanian's Persian Carpets Ltd.*), and although the primary focus was on whether there was a consignment agreement at all, the Court did consider both aspects of the test and did not shift the burden of proof from the plaintiff supplier. Finlayson J.A., writing the unanimous decision, held at p.10:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> The onus is on the plaintiff in any proceedings to prove on a balance of probabilities what his claim is, but certainly in those unique situations in which there was *ex post facto* representation that the goods were delivered on an unusual basis having regard to the business of the debtor company, a strong evidentiary burden is imposed on the plaintiff to make his case on proper evidence. As I have indicated above, there was no proper evidence upon which the learned trial judge could have made the findings that this was a consignment, not intended as security, or a bailment. The plaintiff's case should have failed for want of proof.

17 Leaving the entire burden of proof on the party alleging the consignment is consistent with a broad body of case law as well as with plain common sense. Typically the party disputing the consignment is a trustee or another creditor, in either case a stranger to the disputed agreement. It would be extremely difficult for a stranger to an agreement to prove what its intent was. As was noted by Mr. Colburn in his article, these issues are largely fact-driven. The onus of proof cannot fairly be placed on a party with no knowledge of the facts. In my opinion, the decision of Registrar Ferron in *Stephanian's Persian Carpets Ltd.* is an anomaly and has been overruled by *Seven Limers Coal.* I find that the onus of proof in this case lies upon Access Cash throughout.

Characteristics of a Consignment Agreement

18 In *Stephanian's Persian Carpets Ltd.* , Saunders J. defined "consignment" as follows (at p. 37-38):

> In its simplest terms, a consignment is the sending of goods to another. An arrangement whereby an owner sends goods to another on the understanding that such other will sell the goods to a third party and remit the proceeds to the owner after deducting his compensation for effecting the sale is an example of a consignment agreement.

19 Brian Colburn, in his article, *supra*, provides the following definition (at p. 40):

> Consignments are transactions in which a consignor physically delivers goods to a consignee (who normally is a retailer of goods of that type) for sale or lease by the consignee on the basis of principal and agent. The consignee acts as the consignee's agent in selling or leasing the goods, and receives the proceeds of sale or lease in trust for the consignor. Title to the goods remains with the consignor. On resale by the consignee, title passes directly to the retail purchaser from the consignor through the agency of the consignee.

20 There is no particular magic in the words used by the parties in describing their agreement. The fact that the formal agreement between the parties is called a "consignment" agreement does not necessarily indicate it is in fact a consignment agreement. Conversely, the failure to use the word "consignment" is not necessarily fatal to the party claiming that the arrangement between the parties is in fact a consignment agreement. It is the substance of the agreement that counts, not the labels used by the parties. To determine the substance of the agreement, the court will look both to the terms of the contract itself and the conduct of the parties in relation to that contract: *Stephanian's Persian Carpets Ltd., Re, supra*, per Saunders J. at p. 41; *Farwest Systems Corp. (Receiver of) v. Omron Business Systems Inc.* (1988), 69 C.B.R. (N.S.) 82 (B.C. S.C.), at 86-87; *Askin, Re* (1960), 1 C.B.R. (N.S.) 153 (Ont. S.C.), at 156; *Rivabo Truck Bodies Ltd., Re* (1975), 20 C.B.R. (N.S.) 252 (Ont. S.C.) (Reg.) at 254-255. Typically, this principle has been applied to look past the words used by the parties to suggest consignment and to determine whether in actual operation the arrangement between the parties was a true consignment as opposed to a sale dressed up to look like a consignment. However, there have also been cases where the formal contract between the parties was consistent with a sale agreement but the actual conduct of the parties demonstrated that the formal agreement had been abandoned and goods were actually delivered on consignment: see *Farwest Systems Corp., supra*; *Glengarry A.E.T. Inc. (Trustee of) v. Manhattan Electric Cable Corp.* (1986), 6 P.P.S.A.C. 112 (Ont. S.C.).

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

21 In deciding whether an arrangement between parties is a consignment, the court will consider the presence or absence of certain *indicia* found to be characteristic of a consignment. In the list that follows, "supplier" refers to the consignor or vendor (depending on whether the arrangement is a consignment or sale) and "merchant" refers to the consignee or purchaser. The following are *indicia* of consignment:

- The merchant is the agent of the supplier.
- Title in the goods remains in the supplier.
- Title passes directly from the supplier to the ultimate retail purchaser and does not pass through the merchant.
- The merchant has no obligation to pay for the goods until they are sold to a third party.
- The supplier has the right to demand the return of the goods at any time.
- The merchant has the right to return unsold goods to the supplier.
- The merchant is required to segregate the supplier's goods from his own.
- The merchant is required to maintain separate books and records in respect of the supplier's goods.
- The merchant is required to hold sale proceeds in trust for the supplier;
- The supplier has the right to stipulate a fixed price or a price floor for the goods.
- The merchant has the right to inspect the goods and the premises in which they are stored.
- The goods are shown as an asset in the books and records of the supplier and are not shown as an asset in the books and records of the merchant.
- The shipping documents refer to the goods as consigned.
- The supplier maintains insurance on the goods after they are delivered to the merchant.
- It is apparent from the merchant's dealings with others that the goods belong to the supplier rather than the merchant.

(See *Glengarry A.E.T. Inc. (Trustee of) v. Manhattan Electric Cable Corp., supra*, at 117-119; *Stephanian's Persian Carpets Ltd., Re, supra*, at 39-40; *Langley v. Kahnert* (1905), 36 S.C.R. 397 (S.C.C.), at 401-402; *H & I Carpet Corp., Re* (1983), 49 C.B.R. (N.S.) 158 (Ont. S.C.), at 159-160; *Toyerama Ltd., Re* (1980), 34 C.B.R. (N.S.) 153 (Ont. Bktcy.); *Vitrerie Claveau Glass Inc., Re*; *Migneault & Fils Cie. v. Archambault, supra*, at 151; *Rivabo Truck Bodies Ltd., Re, supra*, at 255-256; *Richardson v. S.K. Dry Goods Co.* (1931), 13 C.B.R. 38 (Ont. S.C.), at 39; *Farwest Systems Corp. (Receiver of) v. Omron Business Systems Inc., supra*, at 85; *Seven Limers Coal & Fertilizer Co. Inc. v. Hewitt, supra*, at 9; B. Colburn, "Consignment Sales and the Personal Property Security Act", *supra*, at 60-61.)

22 It is not necessary for all of the *indicia* of consignment to be present in order for an agreement to constitute a true consignment agreement. However, the more *indicia* present, the more likely the agreement will be found to be a consignment. Some of the *indicia* are more important than others. The three most important criteria are: the existence of an agency relationship; the right of the merchant to return the goods; and, the stipulation that no payment is due to the supplier until the goods have been sold to a third party: B. Colburn, "Consignment Sales and the Personal Property Security Act" at p.61 and 66-67; *Rivabo Truck Bodies Ltd., Re, supra*, at 255; *Stephanian's Persian Carpets Ltd., Re*, at 41. That said, there

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

are certainly cases in which consignment has been established in the absence of one of these three key factors: *e.g. Toyerama, Re, supra*, (agreement specifically denied agency and contained no express right to return the goods); *Stephanian's Persian Carpets Ltd., Re* (no express right to return the goods, although the court found such a right was inferred).

Whether the Consignment Secures Payment

23 It is clear from the PPSA that not all consignment agreements will be subject to its provisions, only those which secure payment or performance of an obligation. Again, it is the substance of the transaction that counts, not its form. In *Stephanian's Persian Carpets Ltd.* both the supplier and the trustee described the arrangement between the supplier and the merchant as being designed to provide "security". The supplier was a wholesaler of very expensive Oriental rugs. The merchant retailer was financially unable to maintain an inventory of such items without some form of financing. Therefore, the supplier and the merchant entered into an agreement which provided, among other things, that the supplier would provide inventory to the merchant for display to prospective customers, title would remain in the supplier, and the merchant would only become liable for payment to the supplier in respect of any individual carpet upon that carpet being sold to a customer. Saunders J. noted that this arrangement was mutually advantageous to the supplier and the merchant. The supplier was able to expose its goods for sale and the merchant's financial risk was minimized and its cash flow problem solved. Most importantly, Saunders J. held, notwithstanding that the arrangement relieved financial pressures for the merchant and protected the supplier from claims by the merchant's creditors, this was not a security interest as contemplated by the PPSA. The reason is a simple matter of logic. The merchant was only liable for payment once a rug had been sold to a customer. That being the case, in respect of unsold rugs still on the premises of the merchant, there was no money owing and hence nothing to secure. For rugs that had left the premises with customers, payment was owing, but there was no longer any security in place. The supplier would not be any further ahead by repossessing the rugs on the premises as they belonged to the supplier in any event and no payment had been made for them.

24 A similar result was reached in *Toyerama, Re*. The supplier, Regal Toys, had a large quantity of Laffy Cathy dolls and Willie Walker dogs which were surplus stock and which it wanted to offload in the upcoming Christmas season. The retail merchant, Toyerama, was a seasonal business with cash flow problems. It was not prepared to pay for the toys as it was uncertain they could be sold at the retail level. The goods were delivered to Toyerama's warehouse pursuant to an agreement that Toyerama would only become liable for payment for toys which it sold to third parties or delivered to its own retail outlets. Once toys left Toyerama's warehouse, payment obligations were triggered. However, there was no obligation to pay for unsold goods remaining in the warehouse. Saunders J. held that in light of that payment obligation, toys shipped from the warehouse to a Toyerama retail outlet had in effect been sold to Toyerama. However, toys remaining in the warehouse that had neither been sold to third parties nor delivered to retail outlets were found to be held on consignment. Further, Saunders J. held, "There was no security interest created by the consignment in the toys that never left the warehouse and their availability for removal did not provide security for the payment for the toys that had been sold or delivered to retail outlets."

25 The fact that a financing statement is filed under the PPSA does not create a presumption that the legislation applies to the transaction: PPSA s. 46 (5). Likewise, the fact that the agreement refers to its being a security document is not determinative. In *Glengarry A.E.T. Inc (Trustee of) v. Manhattan Electric Cable Corp., supra*, the agreement between the supplier and the merchant specifically provided that it was deemed to be a security agreement. The supplier filed two financing statements under the PPSA but they had technical irregularities. The agreement otherwise had many of the *indicia* of a consignment agreement. Rosenberg J. held that the agreement created a consignment and that it was not intended to create a security interest in respect of unsold goods. He held at p.117:

> In the cases of *Stephanian's Persian Carpets Ltd., Re* ... and *Toyerama, Re* ...[cites omitted] Saunders J. found that since no moneys were owing until a sale was made the goods which belonged to the vendor could not be security for unpaid moneys. In my view, the same considerations apply here. The goods themselves could not be security for any moneys owing. And accordingly, so far as the goods themselves are concerned there was no requirement to register under the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

PPSA and Manhattan was entitled to repossess.

C. Factual Context: The Arrangement Between Access Cash and Revenue Plus

26 The evidence before me on this application is in the form of affidavits and cross-examination transcripts. The evidence on behalf of Access Cash comes from Mr. Jon Thomas, its vice-president and the person who dealt directly with John Lennie, the president of Revenue Cash regarding the agreement between the two companies. There was no evidence before me from Mr. Lennie. Therefore, Mr. Thomas's evidence as to the negotiations and discussions underlying the agreement is essentially uncontested. The respondent filed an affidavit of Mr. John Stenger of ELNOS and Mr. Alan Shiner, the receiver for Revenue Cash. While I was initially concerned that conflicting evidence might make it inappropriate to decide this matter in the absence of *viva voce* evidence, a closer analysis now satisfies me that any conflicts in the evidence are more in the nature of inferences to be drawn from the documents and conduct of the parties rather than disputed facts. There are no credibility issues to be resolved.

27 After meetings and discussions that began in the spring of 1998, an understanding was reached that Revenue Cash would become the exclusive distributor of Access Cash ATMs in Canada. Access Cash would supply ATMs to Revenue Cash for three uses:

(i) for sale by Revenue Cash to third parties ("the sales program");

(ii) for placement at a retail location for a monthly fee ("the placement program");

(iii) for placement with a retail location on a trial basis with a view to an ultimate sale ("the trial program").

28 In addition to installing ATMs, Revenue Plus entered into processing and servicing contracts with its customers in all three of its programs. Some of those services were sub-contracted to Access Cash Canada Co. (a company related to the applicant).

29 Mr. Thomas testified that the initial oral arrangement between the parties was that ATMs for the sales program would be sold to Revenue Plus on credit terms, which was the usual practice of Access Cash. However, from the outset, Access Cash had stipulated that ATMs for the placement program and trial program would be supplied on a consignment basis. Title would remain with Access Cash during the placement period. Access Cash would receive 60% of the net transaction revenue for each transaction associated with the placement program and the trial program (instead of the usual 5% it would receive under the sales program). In addition, Revenue Plus would pay Access Cash a monthly fee. The monthly fee and higher share of revenue were meant to compensate Access Cash for its continued ownership interest and its costs of financing the ATMs. Mr. Thomas's evidence on this is not contradicted. However, none of this was confirmed in writing at the time. On September 1, 1998, (prior to the shipment of any ATMs) Mr. Thomas forwarded to Mr. Lennie a draft Distributor Marketing Agreement. This document is clearly a sales agreement, makes no reference to consignment, and contains none of the *indicia* of consignment.

30 On September 24, 1998, Access Cash supplied the first shipment of 37 ATMs to Revenue Plus. This was a clear sale on credit terms with partial payment due in 30 days and the balance in 60 days. Access Cash has never been paid for these 37 ATMs.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

31 In mid October, Revenue Plus was pressing for delivery of more ATMs to be used in its placement program. Mr. Thomas testified that at about this time he considered that Access Cash might be better off with a consignment arrangement for all ATMs shipped to Revenue Plus, *i.e.* for the sales program as well as the placement and trial programs. He said that Mr. Lennie agreed to this and that his (Mr. Thomas's) belief was that there was an oral agreement by mid to late October that all ATMs would be delivered on consignment, with title remaining with Access Cash until sale to a third party. Mr. Thomas made revisions to paragraph 15 of the Distributor Marketing Agreement to reflect this change in the contractual terms between the parties and sent it to Mr. Lennie on November 3, 1998. The agreement was eventually signed in this form on January 11, 1999 (with minor changes of no consequence). Mr. Thomas's evidence is that the terms of the oral agreement under which the parties operated from mid October until January 11, 1999 were the same as the terms of the written contract signed on that date. There is no evidence to contradict that.

32 The terms of the Distributor Marketing Agreement relied upon by Access Cash as evidencing a consignment arrangement between the parties are as follows:

15. LEASE AGREEMENT, STORAGE AND RELEASE, AND SECURITY AGREEMENT

(a) <u>[Revenue Plus] shall, at [Access Cash's] request, maintain designated warehouse space and lease the same to [Access Cash] without a charge for rent, for the purpose of storing on [Access Cash's] behalf Products for future sales to [Revenue Plus]. Such Products, until released, delivered and paid for by [Revenue Plus] as hereinafter provided, are [Access Cash's], and title and ownership is acknowledged by [Revenue Plus] to be in [Access Cash], and not in [Revenue Plus] or anyone else. Any Product delivered and placed in [Revenue Plus's] warehouse shall be received in trust by [Revenue Plus], and returned on demand to [Access Cash]</u>. [Revenue Plus] agrees that, at the request of [Access Cash], it will sign any documents or instruments, whether for public filing or otherwise to acknowledge to [Access Cash] and the world and/or give notice thereof, that [Access Cash] owns the Products.

(b) <u>[Revenue Plus] may purchase the Products held in its warehouse from [Access Cash] by giving [Access Cash] a written order no less than 48 hours</u> by facsimile or otherwise. Such order shall state the number of ATM(s) it desires to purchase at the prices published by [Access Cash] and attached as an Exhibit to this Agreement. The credit terms shall be as agreed upon by the parties. <u>Once [Access Cash] accepts [Revenue Plus's] written order and responds in writing by facsimile, then [Revenue Plus] may remove the ATM(s) designated by [Access Cash] from the warehouse</u>.

(c) <u>[Access Cash] may sell Products to [Revenue Plus] and retain a purchase money security interest in the Products</u>. In such event, [Revenue Plus] agrees that, at the request of [Access Cash], it will sign any documents or instruments, whether for public filing or otherwise to acknowledge to [Access Cash] and the world and/or to give notice thereof, that [Access Cash] has retained a purchase money security interest in the Products. [Revenue Plus] will sign a Security Agreement on terms that are mutually agreeable to the parties. (Emphasis added)

33 The other provisions of the Distribution Agreement (which was a pro forma agreement prepared as a sales contract) were unchanged. Those provisions obviously contemplate a sale from Access Cash to Revenue Plus. In addition, ELNOS relies on paragraph 9 and 22(b) of the Distribution Agreement which clearly negate any agency relationship between the parties. Paragraph 9 provides, in part, that Revenue Plus "buys the Product on its own account ...and resells products in its own name and for its own account at its sole risk and expense, but under the trademarks, logos and other indicia assigned by [Access Cash]". Paragraph 22(b) states:

Should any legislation, including any decree or regulation, be enacted in a jurisdiction within the APR, the effect of which is to convert [Revenue Plus's] status to one of an exclusive agency or distributorship, then, as regards such jurisdiction, this Agreement will be deemed to have terminated with the mutual consent of both parties on the business day immediately preceding the effective date of such legislation.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

34 The Distributor Agreement does not actually require that Revenue Plus segregate the consigned goods from other inventory in its warehouse unless requested to do so by Access Cash. However, according to Mr. Thomas, such a request was made and he understood that the Access Cash ATMs were kept in a separate fenced area after November 1998. In practice, however, the Access Cash ATMs were stored in a specific area of the warehouse, but were intermingled with other goods.

35 On the same day as the Distributor Marketing Agreement was executed, the parties signed a separate agreement ("the Placement Agreement") to govern the placement and trial programs of Revenue Plus. The recitals to that agreement refer to Revenue Plus as a "reseller" of ATMs under a Distributor Marketing Agreement with Access Cash. The Placement Agreement does *not* mention "consignment" and does *not* provide that title to the goods is to remain in Access Cash. The recitals provide that the purpose of the Placement Agreement is for Access Cash to provide financial assistance to Revenue Plus for its placement and trial programs under the terms set out therein. Those terms include the following:

• Access Cash agreed "to sell to [Revenue Plus] ATMs at the... Canadian Wholesale Price".

• Access Cash would "finance such ATMs at the monthly rate of .02274% times the Canadian Wholesale Price" for the term of a trial program, not to exceed 6 months.

• At the end of such trial period, one of three things would happen: (1) Revenue Plus could sell the ATM to the trial program customer at the designated retail price and upon such sale immediately pay Access Cash its Canadian Wholesale Price; or (2) the customer could retain the ATM under the placement program and Revenue Plus would continue to make the monthly financing payment to Access Cash referred to above; or (3) if the customer did not purchase the ATM or continue under the placement program, Revenue Plus would pay Access Cash its Canadian Wholesale Price within 30 days.

• During the trial program, in addition to the monthly financing fee, Access Cash would receive 60% of the net transaction revenues.

• During the placement program, in addition to the monthly financing fee, Access Cash would receive 50% of the net transaction revenues.

36 Access Cash made further shipments of ATMs to Revenue Plus in October, November and December, 1998, all of which are alleged to be under the terms embodied in the agreements signed in January 1999.

37 Paragraph 15(c) of the Distributor Agreement contemplated the possibility of Access Cash selling machines to Revenue Plus and retaining a purchase money security interest, in which event an agreement to that effect was to be signed by the parties and appropriate notices filed. A Purchase Money Security Agreement was signed on January 7, 1999 and notices filed as referred to above. Subsequent to the filing of the PMSI, an additional 23 ATMs were delivered to Revenue Plus.

38 Revenue Cash paid GST, PST and Import Tax on all ATMs shipped by Access Cash, without distinction based on the program for which the ATMs in question were to be used or whether they were shipped before or after the-amendment to the Distributor Marketing Agreement in October.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

39 With the exception of the first 37 ATMs shipped to Revenue Plus as a sale on credit, all ATMs supplied by Access Cash to Revenue Plus were recorded on Access Cash's internal financial records as continuing to be assets of Access Cash. Access Cash also carried insurance coverage for the ATMs shipped to Revenue Plus.

40 Under the sales program, Access Cash recommended a retail price for sales to third parties. The agreements between the parties did not require Revenue Plus to sell the machines at or above the price suggested by Access Cash, but the prices actually charged by Revenue Plus were at or above that price.

D. Analysis

1. The Original 37 ATMs

41 It is clear on the evidence that the first 37 ATMs-were sold to Revenue Plus on credit terms. There was no PMSI registered in respect of those machines and there is nothing about the arrangement to support any inference that they were supplied on consignment.

2. ATMs Supplied After January 7, 1999

42 The ATMs supplied after January 7, 1999 are protected by the PMSI registered by Access Plus. Therefore, Access Plus has priority over ELNOS in respect of those machines, a conclusion which was not disputed by ELNOS at the hearing before me.

3. Other ATMs (Supplied from October to December 1998)

43 There was a change in the arrangements between the parties in October 1998. The agreements signed in January 1999 reflect any changes made to the agreement between the parties and govern the relationship between them from about the end of October 1998. As is often the case, the arrangements between Access Cash and Revenue Plus contain some of the *indicia* of a consignment agreement and some features inconsistent with consignment.

Language Used

44 Neither of the written agreements use the word "consignment" to describe the arrangement between the parties. Both agreements refer to "sales" to Revenue Plus. To a certain extent, the references in the October revised draft of the Distributor Agreement to the arrangement being a sale can be explained by the fact that it was a *pro forma* agreement used by Access Cash for standard sales agreements. Although Access Cash amended paragraph 15 of the agreement to reflect the change in its arrangements with Revenue Plus in October 1998, it failed to make corresponding amendments in the rest of the agreement. However, considerable time elapsed between October when the draft amendment was first prepared and January 1999 when it was finally signed. In that context, the absence of language indicative of consignment is more significant.

Agency

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

45 The Distribution Agreement explicitly negates an agency relationship between the parties. While not explicit, the only reasonable inference from the Placement Agreement is that it does not create an agency. Thus, for all three programs, Revenue Plus was not the agent of Access Cash. This is a factor inconsistent with consignment, although not fatally so: *Toyerama Ltd., supra.*

Title to the Goods

46 It is an essential feature of a consignment agreement that title remain in the supplier. The Distributing Agreement provides that the ATMs sent to Revenue Plus are to be stored in the designated area of the Revenue Plus warehouse pending "future sale to Revenue Plus". Title is specified to remain in Access Cash until an ATM is "released, delivered or paid for" by Revenue Plus. The Distributing Agreement further provides that Revenue Plus may give 48 hours notice to Access Cash that it wishes to purchase one of the ATMs, and that if accepted by Access Cash Revenue Plus could then remove the ATM from its warehouse. Title to ATMs sold by Revenue Plus to third parties passes from Revenue Plus to the third party, and not from Access Cash.

47 The Placement Agreement does not stipulate that title is to remain in Access Cash. On the contrary, the Placement Agreement contemplates a sale to Revenue Plus. Further, the Placement Agreement refers to the Distributor Agreement and describes Revenue Plus as a "reseller" under that agreement, which confirms that before Revenue Plus sold goods to a third party, it first purchased them from Access Cash.

48 The only situation in which the agreements between the parties clearly reserves title to Access Cash is when the ATMs are in the Revenue Plus warehouse prior to being placed with or sold to a retailer.

Timing of Merchant's Obligation to Pay for the Goods

49 The mere delivery of ATMs to Revenue Plus and placement in its warehouse did not trigger any obligation by Revenue Plus to pay anything to Access Cash. However, any circumstance in which Revenue Plus could remove inventory from the warehouse gave rise to a payment requirement. For ATMs used in the sales program, there was first a sale to Revenue Plus and Revenue Plus was then obliged to pay the wholesale price to Access Cash, regardless of its selling price to its own customer. For ATMs used in the trial program and placement program, the full price of the machine was not immediately due. However, while the ATM was under the trial program or long term placement program, Revenue Plus was required to make monthly payments to Access Cash as a financing fee and was also required to pay to Access Cash a far higher share of the transaction revenues than would otherwise be the case. Further, upon termination of a trial period without a sale or long term placement to its customer, Revenue Plus was required to pay the wholesale price to Access Cash within 30 days.

Sale Proceeds to be Held in Trust

50 There is nothing in any of the agreements requiring Revenue Plus to hold any proceeds from its sale or lease of the ATMs in trust for Access Cash. The only reference in the agreements to any trust obligations is in paragraph 15(a) of the Distributor Agreement which provides that ATMs delivered and placed in [Revenue Plus's] warehouse shall be received in trust by [Revenue Plus]. This is consistent with the fact that payments received by Revenue Plus from third parties were received in its own right as title always passed through Revenue Plus and never directly from Access Cash. This is not

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

consistent with consignment.

The Distributing Right of Supplier to Demand Return of the Goods

51 Agreement provided that the ATMs in the Revenue Plus warehouse were held in trust for Access Cash and that Access Cash could demand their return at any time. This is a factor consistent with consignment. There was no such express right in the Placement Agreement, nor can one be inferred as such would be inconsistent with the rights to possession of the third party retailers contemplated in the agreement.

Right of Merchant to Return the Goods at Will

52 Neither of the agreements provides any right to Revenue Plus to return the goods if it wished. Mr. Thomas's evidence was that this was simply not anticipated but that Access Cash would have been willing to accept the return of any unsold ATMs. Such an intention is consistent with the terms of the Distribution Agreement in respect of machines that never left the warehouse. Since Revenue Plus had no obligation to pay for those machines, it is a logical inference that they could be returned.

53 However, a right in Revenue Plus to return ATMs in the trial and placement program is inconsistent with the Placement Agreement. If a customer under the trial program elected not to buy the ATM, and if a long term placement agreement for that customer was not agreed to by Access Cash, then Revenue Plus was required under the agreement to pay the wholesale price of the ATM to Access Cash within 30 days.

Stipulated Sales Price

54 Access Plus did not have right in the agreement to stipulate a sales price or a price below which an ATM could not be sold. This factor does not support consignment. Although Access Plus recommended a retail price, this is an equally common practice for distributors in sales agreements and in any event was not binding on Revenue Plus.

Insurance

55 Access Cash continued to carry insurance for the ATMs delivered to Revenue Plus. However, it did not carry insurance for the full value of the ATMs delivered. Mr. Thomas explained that the full value was not insured because Access Cash believed there would be some turnover of the ATMs provided and because Access Cash did some self-insuring. There would be no reason for Access Cash to insure any goods shipped to Revenue Plus if it did not have an ownership interest in them. This is a factor supportive of Access Cash's understanding that the goods were shipped on consignment. On the other hand, Revenue Plus also carried insurance on the ATMs until it sold them to a third party, a factor inconsistent with consignment. Thus, the insurance treatment of the ATMs is conflicting and may reflect that there was no meeting of the minds on the issue of ownership.

Books and Records of the Parties

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

56 Access Cash carried the ATMs as an asset on its books, a factor consistent with consignment. Revenue Plus carried the ATMs as an asset on its books, a factor inconsistent with consignment. Again, this may reflect a lack of clear understanding between the parties on the ownership issue.

57 There was no requirement that Revenue Plus keep separate books and records in respect of goods it held on consignment and it did not do so. Further, the records of Access Cash do not clearly show the status of the various ATMs shipped to Revenue Plus after they left the warehouse. Access Cash could not determine from its own records which ATMs were delivered in respect of the sales program and which were destined for the trial or placement program.

58 The shipping records do not reflect a consignment arrangement.

Right of Supplier to Inspect Goods and Premises

59 Access Cash had an ongoing cooperative relationship with Revenue Plus and its representatives were frequently at Revenue Plus' premises. However, this was entirely at the discretion of Revenue Plus as there was nothing in either the Distributor Agreement or the Placement Agreement providing a right of inspection to Access Cash. Access Cash had no right under the agreements to enter and inspect ATMs on the premises of third party retailers who had possession of ATMs under the trial or placement programs. The agreements did not grant any right to Access Cash to inspect the books and records of Revenue Plus in respect of its ATMs.

Other Factors

60 I have also considered the manner in which Revenue Plus dealt with the goods. The Receiver's evidence was that numerous customers who had obtained ATMs from Revenue Plus were unaware of any ownership interest of Access Cash and understood that the ATM was owned by Revenue Plus. On the other hand, Mr. Thomas reports evidence from other customers who apparently understood that Access Cash was the owner of the machines. There was no firsthand evidence from any customers. I do not find this to be a useful factor one way or the other. Likewise, the use of StellarCom or Access Cash brands on the machines is not conclusive one way or the other given the distributorship arrangement between them and the ongoing involvement of both companies in servicing and processing.

E. Conclusions

ATMs in the Trial Program and Placement Program

61 The ATMs used by Revenue Plus in its trial program and its placement program were the property of Revenue Plus, not Access Cash. The only evidence supporting Access Cash's contention that these machines were held on consignment and remained the property of Access Cash is the evidence of Mr. Thomas as to his understanding and subjective intent. However, Mr. Thomas also testified that the terms under which Access Cash provided ATMs for the trial and placement programs were embodies in the written Placement Agreement. That agreement was not an Access Cash standard form agreement. It was drafted by Access Cash specifically for its arrangements with Revenue Plus, was presented to Revenue Plus on November 3, 1998 in draft form and ultimately signed by the parties on January 11, 1999.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

62 There is nothing in the Placement Agreement consistent with it being a consignment agreement. One of the principle features of a consignment agreement is that the merchant is under no obligation to pay for the goods until they are sold to a third party. However, under the Placement Agreement, Revenue Plus is required to pay for any machine returned by a retailer within 30 days. The Placement Agreement expressly contemplates a sale to Revenue Plus which is to be financed by Access Cash as long as the ATMs remain in the trial program or are transferred into a long term placement on terms accepted by Access Cash. There is no stipulation that title is to remain in Access Cash, no requirement that any proceeds received by Revenue Plus are to be held in trust for Access Cash, no right in Access Cash to demand the return of goods at will, and no right of inspection. The failure of the Placement Agreement to provide that title remained in Access Cash is particularly telling in light of the inclusion of such a term in the amendment to paragraph 15 of the Distributor Agreement, which was drafted at the same time and by the same party.

63 In short, there is nothing to support a finding of consignment. Mr. Thomas may have had that understanding as to the nature of the agreement, but he was mistaken. Where the agreement between the parties has been committed to writing, the subjective intent or understanding of one party is not admissible to vary the contract's clear terms: *Toronto Dominion Bank v. Leigh Instruments Ltd. (Trustee of)* (1998), 40 B.L.R. (2d) 1 (Ont. Gen. Div. [Commercial List]). This is not a situation, such as in *Farwest Systems Corp. (Receiver of) v. Omron Business Systems Inc.*, *supra*, where it is clear from the actions of the parties that they had decided to abandon their formal written agreement and conduct business on a wholly different basis. Nor is this a case where the court should look beyond the clear words of the written agreement and determine the true nature of the agreement based on the conduct of the parties. There is nothing about the conduct of the parties that is inconsistent with the written Placement Agreement. Further, this situation is distinguishable from cases in which courts have scrutinized the conduct of parties to determine if the description of their relationship in the formal contract as being one of consignment is in fact a sham to benefit the supplier. Here the agreement itself is inconsistent with consignment and it is the supplier who attempts to claim otherwise.

64 As was noted by the Court of Appeal in *Seven Limers Coal & Fertilizer Co. Inc. v. Hewitt*, *supra*, at p. 10, where the supplier makes an *ex post facto* representation that goods were delivered on an unusual basis having regard to the business of the parties, "a strong evidentiary burden is placed on the [supplier] to make his case on proper evidence". That evidentiary burden is not met in this case. Accordingly, I find that the ATMs covered by the Placement Agreement were not on consignment and were the property of Revenue Plus. With the exception of such machines covered by the PMSI, Access Cash has no claim to the machines or their proceeds superior to that of ELNOS.

65 In the alternative, if I have erred in respect of my finding that the ATMs subject to the Placement Agreement were not on consignment, there is nevertheless no priority claim by Access Cash because the agreement falls within the PPSA as being a consignment that "secures payment or the performance of an obligation". Saunders J. found that the consignment agreement in *Stephanian's Persian Carpets Ltd., Re*, *supra*, was not intended as security because no payment was due in respect of the goods until they had been sold to a third party. He noted, at p. 42, that his interpretation of the words "intended as security" in the relevant provision of the PPSA was a narrow one and that as a result "there may rarely be consignment agreements to which the PPSA will apply". He suggested a situation where the consignee enters into lease option arrangements with his customer remitting rental payments to the consignor as an example of a consignment agreement falling within the PPSA. That is not precisely the situation here, but it is similar. The point established in *Stephanian's Persian Carpets Ltd.* is that an Agreement in this case, secure payment if there is no payment due. Under the Placement Agreement in this case, however, two types of payment were due to Access Cash: a monthly financing fee and a percentage of the transaction revenues generated by the ATMs. Therefore, if the Placement Agreement is in the nature of a consignment, then it is one that secures payment and is therefore subject to the requirements of the PPSA. As a result, Access Cash does not have any priority except through its registered PMSI.

ATMs in the Sales Program

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

66 Unlike the Placement Agreement, the Distributor Agreement does provide that title is to remain in Access Cash. This is one indication that the ATMs may have been placed with Revenue Plus on consignment. There are, however, some features of the agreement that are not fully consistent with a consignment. Although Access Cash carried the ATMs as an asset on its records and insured them, so also did Revenue Plus. There is a stipulation that ATMs delivered to the Revenue Plus warehouse are "received in trust" for Access Cash, but there is no stipulation that proceeds of any sale effected by Revenue Plus are to be held in trust for Access Cash. The obligation to pay for the goods does not arise upon their delivery to Revenue Plus, but neither does it arise only upon a sale to a third party. Rather, the agreement contemplates that Revenue Plus will be the purchaser of the goods. The agreement provides that the ATMs are to be held in the designated area of the warehouse on behalf of Access Cash for the purpose of storage pending "future sale to [Revenue Plus]". Title is stipulated to be in Access Cash "until released, delivered or paid for by [Revenue Plus]". Paragraph 15(b) of the agreement contemplates that ATMs could only be released from the warehouse upon Revenue Plus submitting a purchase order that is accepted by Access plus. To the knowledge of Access Cash, when the ultimate retail customer financed the purchase of an ATM through Alliance, title passed through Revenue Plus. This is, therefore, not a classic consignment agreement in which title passes directly from the supplier to the ultimate retail purchaser without passing through the merchant, such as is described by the Supreme Court of Canada in *Langley v. Kahnert, supra*. Further, many of the traditional *indicia* of consignment are missing altogether. For example, there is no relationship of agency, no right of inspection, no requirement to maintain separate books and records for the goods held on consignment, and no stipulation as to a fixed or minimum retail selling price.

67 The agreement is clear, however, in its reservation of title in the goods to Access Cash until such time as they are removed from the warehouse. The goods are required to be stored in a designated area which is deemed to be leased to Access Cash and until the goods leave that space no payment obligations arise. Clearly, a future sale to Revenue Plus is contemplated, but equally clearly that sale is not deemed to arise upon delivery of the goods into the custody of Revenue Plus.

68 The arrangement between the parties in this case has many of the features of the agreement at issue in *Toyerama, Re, supra*, in which Saunders J. observed (at page 157) that "the characterization of the agreement as one of consignment or sale is not clear-cut". In *Toyerama, Re* payment obligations were triggered when the toys left the warehouse, whether for sale to a third party or delivery to one of Toyerama's own retail outlets. Saunders J. held that toys delivered from the warehouse to a Toyerama retail outlet were sold to Toyerama and therefore no longer consignment goods. However, he also found that the determining factor in characterizing the agreement was the payment obligation and that since Toyerama had no obligation to pay for goods stored in its warehouse, those goods were held on consignment. In coming to that conclusion, Saunders J. noted (at page 157) that "a consignment contract has been described as one of bailment". Likewise, in the case before me, Access Cash was stipulated to retain title to the ATMs in Revenue Plus's warehouse and as long as the ATMs remained in the warehouse, there was no obligation on the part of Revenue Plus to pay for them. In my opinion, this constituted a consignment or bailment of those goods and they had not been purchased by Revenue Plus.

69 Applying the principles set out in *Stephanian's Persian Carpets Ltd., Re, supra*, and *Toyerama, Re, supra*, the consignment (or bailment) created under the Distributor Agreement cannot fall within the provisions of the PPSA. Since no payment was required in respect of those goods, there was no payment obligation to secure.

70 Accordingly, Access Plus has established an ownership interest in the ATMs stored in the Revenue Plus warehouse and which never left the warehouse for the purpose of delivery to a third party under the sales, trial or placement programs and its interest is not subject to the PPSA.

Form of Order

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

71 Access Cash shall be entitled to a declaration in respect of its prior secured interest arising from its PMSI as well as a declaration of its ownership interest in the ATMs stored at the Revenue Plus warehouse as referred to in paragraph 70. Given the determinations I have made and the fact that some of the ATMs may have been removed from the warehouse other than as directly contemplated under the agreement, I will not rule at this time on the right of Access Cash to trace its interest to the proceeds of any sale. If there are outstanding issues to be addressed in this regard, or if counsel are unable to agree on the appropriate form of this order, I can be spoken to.

Other Issues

72 I have not dealt with the marshalling issue in respect of the call centre operation as this was not fully argued before me and will require updated information. To the extent that this issue still needs to be resolved, a further motion or application should be brought. It does not need to be returnable before me.

73 Success on the application before me has been divided. My inclination is to make no order as to costs. However, if counsel do not agree with that disposition, an appointment should be made through my secretary to arrange an appearance to address the issue.

Order accordingly.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 4

2008 BCCA 327
British Columbia Court of Appeal

Cliffs Over Maple Bay Investments Ltd. v. Fisgard Capital Corp.

2008 CarswellBC 1758, 2008 BCCA 327, [2008] 10 W.W.R. 575, [2008] B.C.W.L.D. 6017, [2008] B.C.W.L.D. 6018, [2008] B.C.J. No. 1587, 168 A.C.W.S. (3d) 785, 258 B.C.A.C. 187, 296 D.L.R. (4th) 577, 434 W.A.C. 187, 46 C.B.R. (5th) 7, 83 B.C.L.R. (4th) 214

Cliffs Over Maple Bay Investments Ltd. (Respondent / Petitioner / Respondent) and Fisgard Capital Corp. and Liberty Holdings Excel Corp. (Appellants / Respondents / Applicants)

Frankel, Tysoe, D. Smith JJ.A.

Heard: August 12, 2008
Judgment: August 15, 2008
Docket: Vancouver CA036261

Counsel: G.J. Tucker, A. Frydenlund for Appellants
H.M.B. Ferris, P.J. Roberts for Respondent
M. Sennott for Century Services Inc.
M.B. Paine for Monitor, Bowra Group

Subject: Insolvency; Corporate and Commercial

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy and insolvency — Proposal — Companies' Creditors Arrangement Act — Arrangements — Effect of arrangement — Stay of proceedings

Applicant creditors held mortgages registered against debtor company's property development — Debtor commenced proceeding under Companies' Creditors Arrangement Act ("CCAA") — Stay order was granted pursuant to s. 11 of CCAA — Debtor applied for extension of stay and authorization for debtor-in-possession financing — Creditors applied to have initial stay set aside and sought appointment of interim receiver — Chambers judge granted debtor's application and dismissed creditors' application — Creditors appealed — Appeal allowed — Ability of court to grant or continue stay under s. 11 of CCAA is not free standing remedy that court may grant whenever insolvent company wishes to undertake restructuring — Section 11 is ancillary to fundamental purpose of CCAA, which is to facilitate compromises and arrangements between companies and their creditors — Stay of proceedings freezing rights of creditors should only be granted in furtherance of CCAA's fundamental purpose — It was not suggested that debtor intended to propose arrangement or compromise to its creditors before embarking on its restructuring plan — In absence of such intention, it was inappropriate for stay to have been granted or extended under s. 11 — Chambers judge failed to take this important

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

factor into account.

Bankruptcy and insolvency --- Proposal — Companies' Creditors Arrangement Act — Miscellaneous issues

Applicant creditors held mortgages registered against debtor company's property development — Debtor commenced proceeding under Companies' Creditors Arrangement Act ("CCAA") — Stay order was granted pursuant to s. 11 of CCAA — Debtor applied for extension of stay and authorization for debtor-in-possession financing — Creditors applied to have initial stay set aside and sought appointment of interim receiver — Chambers judge granted debtor's application and dismissed creditors' application — Creditors appealed — Appeal allowed — Ability of court to grant or continue stay under s. 11 is not free standing remedy that court may grant whenever insolvent company wishes to undertake "restructuring" — Section 11 is ancillary to fundamental purpose of CCAA, which is to facilitate compromises and arrangements between companies and their creditors — It was not suggested that debtor intended to propose arrangement or compromise to its creditors before embarking on its restructuring plan — In absence of such intention, it was inappropriate for stay to have been granted or extended under s. 11 — If stay under CCAA should not be extended because debtor is not proposing arrangement or compromise with creditors, it followed that DIP financing should not have been authorized to permit debtor to pursue restructuring plan that did not involve arrangement or compromise with its creditors.

Table of Authorities

Cases considered by *Tysoe J.A.*:

Anvil Range Mining Corp., Re (2001), 2001 CarswellOnt 1325, 25 C.B.R. (4th) 1 (Ont. S.C.J. [Commercial List]) — referred to

Anvil Range Mining Corp., Re (2002), 2002 CarswellOnt 2254, 34 C.B.R. (4th) 157 (Ont. C.A.) — referred to

Charles Osenton & Co. v. Johnston (1941), [1942] A.C. 130, [1941] 2 All E.R. 245, 110 L.J.K.B. 420, 57 T.L.R. 515 (U.K. H.L.) — considered

Fairview Industries Ltd., Re (1991), 1991 CarswellNS 35, 11 C.B.R. (3d) 43, (sub nom. *Fairview Industries Ltd., Re (No. 2))* 109 N.S.R. (2d) 12, (sub nom. *Fairview Industries Ltd., Re (No. 2))* 297 A.P.R. 12 (N.S. T.D.) — referred to

Friends of the Oldman River Society v. Canada (Minister of Transport) (1992), [1992] 2 W.W.R. 193, [1992] 1 S.C.R. 3, 3 Admin. L.R. (2d) 1, 7 C.E.L.R. (N.S.) 1, 84 Alta. L.R. (2d) 129, 88 D.L.R. (4th) 1, 132 N.R. 321, 48 F.T.R. 160, 1992 CarswellNat 649, 1992 CarswellNat 1313 (S.C.C.) — considered

Hongkong Bank of Canada v. Chef Ready Foods Ltd. (1990), 51 B.C.L.R. (2d) 84, 1990 CarswellBC 394, 4 C.B.R. (3d) 311, (sub nom. *Chef Ready Foods Ltd. v. Hongkong Bank of Canada)* [1991] 2 W.W.R. 136 (B.C. C.A.) — followed

Lehndorff General Partner Ltd., Re (1993), 17 C.B.R. (3d) 24, 9 B.L.R. (2d) 275, 1993 CarswellOnt 183 (Ont. Gen. Div. [Commercial List]) — referred to

New Skeena Forest Products Inc., Re (2005), 7 M.P.L.R. (4th) 153, [2005] 8 W.W.R. 224, (sub nom. *New Skeena Forest Products Inc. v. Kitwanga Lumber Co.)* 210 B.C.A.C. 247, (sub nom. *New Skeena Forest Products Inc. v. Kitwanga Lumber Co.)* 348 W.A.C. 247, 2005 BCCA 192, 2005 CarswellBC 705, 9 C.B.R. (5th) 278, 39 B.C.L.R.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(4th) 338 (B.C. C.A.) — considered

Reference re Companies' Creditors Arrangement Act (Canada) (1934), [1934] 4 D.L.R. 75, 1934 CarswellNat 1, 16 C.B.R. 1, [1934] S.C.R. 659 (S.C.C.) — followed

Reza v. Canada (1994), 1994 CarswellOnt 1158, 1994 CarswellOnt 675, 24 Imm. L.R. (2d) 117, 21 C.R.R. (2d) 236, 116 D.L.R. (4th) 61, (sub nom. *Reza v. Canada (Minister of Employment & Immigration))* 72 O.A.C. 348, 22 Admin. L.R. (2d) 79, [1994] 2 S.C.R. 394, (sub nom. *Reza v. Canada (Minister of Employment & Immigration))* 167 N.R. 282, 18 O.R. (3d) 640 (note) (S.C.C.) — considered

Skeena Cellulose Inc., Re (2001), 29 C.B.R. (4th) 157, 2001 BCSC 1423, 2001 CarswellBC 2226 (B.C. S.C.) — considered

United Used Auto & Truck Parts Ltd., Re (2000), 2000 BCCA 146, 135 B.C.A.C. 96, 221 W.A.C. 96, 2000 CarswellBC 414, 73 B.C.L.R. (3d) 236, 16 C.B.R. (4th) 141, [2000] 5 W.W.R. 178 (B.C. C.A.) — considered

Ursel Investments Ltd., Re (1990), 2 C.B.R. (3d) 260, 1990 CarswellSask 34 (Sask. Q.B.) — considered

Ursel Investments Ltd., Re (1992), (sub nom. *Deloitte & Touche Inc. v. Ursel Investments Ltd. (Receiver of))* [1992] 3 W.W.R. 106, (sub nom. *Deloitte & Touche Inc. v. Ursel Investments Ltd. (Receiver of))* 89 D.L.R. (4th) 246, 10 C.B.R. (3d) 61, (sub nom. *Deloitte & Touche Inc. v. Ursel Investments Ltd. (Receiver of))* 97 Sask. R. 170, (sub nom. *Deloitte & Touche Inc. v. Ursel Investments Ltd. (Receiver of))* 12 W.A.C. 170, 1992 CarswellSask 19 (Sask. C.A.) — referred to

Statutes considered:

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3
s. 47(1) — referred to

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

s. 2 "debtor company" — referred to

s. 3(1) — referred to

s. 4 — considered

s. 5 — considered

s. 6 — considered

s. 11 — considered

s. 11(3) — referred to

s. 11(6) — considered

s. 11.7 [en. 1997, c. 12, s. 124] — referred to

APPEAL by creditors from order of chambers judge granting debtor's application to extend stay of proceedings and to

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

authorize debtor-in-possession financing.

Tysoe J.A. **(orally):**

1 The appellants appeal from the order dated June 27, 2008, by which the chambers judge extended the stay of proceedings that was initially granted on May 26, 2008, until October 20, 2008, and authorized financing in the amount of $2,350,000.

2 The proceeding was commenced by The Cliffs Over Maple Bay Investments Ltd. (the "Debtor Company") under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, (the "*CCAA*") after the appellants appointed a receiver on May 23, 2008. As is often the case for initial applications under the *CCAA*, no notice was given to the appellants or any other of the Debtor Company's creditors of the application giving rise to the May 26 stay order. In accordance with section 11(3) of the *CCAA*, the stay contained in the order was expressed to expire on June 25.

3 The Debtor Company then made application for further relief at the hearing commonly called the comeback hearing. The Debtor Company requested an extension of the stay until October 20, 2008, and authorization for financing in the amount of $2,350,000. This financing, which, following upon American terminology, is commonly referred to as "debtor-in-possession" or "DIP" financing, was to be secured by a charge having priority over the security held by the appellants and all other secured and unsecured creditors. The appellants made a concurrent application requesting that the May 26 order be set aside and that an interim receiver be appointed pursuant to s. 47(1) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3. The chambers judge granted the Debtor Company's application and dismissed the appellants' application.

Background

4 The business of the Debtor Company is the development of a 300 acre site near Duncan, British Columbia, consisting of single family lots and multi-residential units, a hotel and apartments and a golf course. The business plan was to build the golf course and to construct servicing for subdivided lots, which were to be sold to purchasers.

5 The development of the non-golf course lands was to be carried out in five phases. Phase I consists of 70 single family lots and 60 multi-residential units. Its construction is 95% complete and 54 of the 70 single family lots have been sold and conveyed to the purchasers, with the sale proceeds being applied towards the Debtor Company's mortgage financing.

6 Phase II consists of 76 single family lots and is 50% complete. Phase III consists of 69 single family lots, 112 multi-residential lots and 225 hotel units, and it is 5% complete. Phases IV and V consist of 131 single family lots and 60 multi-residential units, and each is 1% complete.

7 The golf course, which is the focal point of the development, is approximately 60 to 70% complete. A restrictive covenant in favour of the District of North Cowichan stipulates that the golf course must be at least 80% complete before more than 200 lots can be sold.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

8 There are four mortgages registered against the development. The first two mortgages are not significant — the first mortgage secures an amount of $900,000 that is also secured by a cash collateral deposit, and the second mortgage secured a loan from Liberty Mortgage Services Ltd. that has not yet been discharged because there is a dispute between the Debtor Company and Liberty Mortgage Services Ltd. as to whether $85,000 of interest is still owing.

9 The third mortgage is held by the appellants. It is in the principal sum of $19,500,000 and has an interest rate of 19.75% per annum. It matured on March 1, 2008, and its balance is approximately $21,160,000 as of June 15, 2008. The fourth mortgage is held by the appellant, Liberty Holdings Excell Corp., and The Canada Trust Company. It is in the principal sum of $7,650,000 and has an interest rate of 28% per annum. It matured on January 1, 2008, and its balance is approximately $8,800,000 as of June 15, 2008.

10 In addition to the indebtedness secured by the mortgages, the Debtor Company has liabilities in the following approximate amounts:

$4,460,000	— trade creditors
1,700,000	— equipment leases
1,135,000	— loans from related parties
45,000	— unpaid source deductions
$7,340,000	

11 The Debtor Company was having some difficulties with respect to the development prior to March 2008 as a result of delays and substantial budget overruns. Ongoing construction on the development was limited. The main two mortgages had matured or were about to mature, and the Debtor was unsuccessful in its efforts to obtain refinancing. However, matters came to a head in March 2008 when the Debtor Company learned that its anticipated water source for the irrigation of the golf course was problematic.

12 It had been contemplated that the Debtor Company would obtain water for the golf course's irrigation from a joint utilities board consisting of representatives of the City of Duncan, the District of North Cowichan and the Cowichan First Nation. The joint utilities board had jurisdiction over reclaimed water from sewage lagoons located on the lands of the Cowichan First Nation. The joint utilities board was apparently prepared to provide water from the sewage lagoons for the irrigation of the golf course but it was unable to enter into an agreement with the Debtor Company because three members of the Cowichan First Nation had rights of possession over part of the sewage lagoons and were being advised by their consultant that they should not agree to an extension of the lease of the lagoons.

13 The Debtor Company advised the mortgage lenders of the water problem, and the lenders reacted by serving the Debtor Company with notices of intention to enforce their security in April 2008. On May 23, 2008, the mortgage lenders appointed a receiver, which precipitated the commencement of the *CCAA* proceeding by the Debtor Company. On May 26, 2008, the chambers judge granted the Debtor Company's *ex parte* application under the *CCAA* and directed the holding of the comeback hearing after notice had been given to the Debtor Company's creditors. The Debtor Company applied for authorization of the DIP financing at the comeback hearing.

14 When the chambers judge granted the *ex parte* application on May 26, 2008, he appointed The Bowra Group Inc. as monitor pursuant to s. 11.7 of the *CCAA* (the "Monitor"). The first report of the Monitor dated June 16, 2008, was before the chambers judge at the comeback hearing. Based on two previous appraisals and discussions with the realtor having the listing

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

for the development, the Monitor estimated the value of the development under the following three scenarios:

(a) liquidation value with no source of water for irrigation — $10 million;

(b) liquidation value with a source of water for irrigation — $28 million;

(c) going concern value with completion of the development — $50 million.

The Monitor also reported that the realtor believes that if the development were to be completed, there would be sufficient sale proceeds to satisfy all obligations of the Debtor Company. The appellants took issue with the going concern valuation and submitted that the development should be re-appraised by an appraiser they consider to be trustworthy.

15 In its report, the Monitor also recommended that the court authorize the DIP financing to enable it to pursue a water source for the irrigation of the golf course. The Monitor stated that it believes that the existing management of the Debtor Company will be unable to execute the restructuring in the absence of assistance and direction. The Monitor requested that it be given additional powers so that it could pursue the water source and to receive any offers for the purchase of all or part of the development, with the view that once a water source is secured, it would make further recommendations to the court with respect to the completion of the development. The application of the Debtor Company at the comeback hearing included a request for the expansion of the Monitor's powers.

Decision of the Chambers Judge

16 The appellants argued before the chambers judge, as they did on this appeal, that this matter should not be under the *CCAA* because the business of the Debtor Company is a single real estate development and the business was essentially dormant as at the date of the application. The chambers judge considered s. 11(6) of the *CCAA*, which reads as follows:

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.

The chambers judge concluded that the preconditions contained in s. 11(6) had been met. He did not state why he considered a stay order to be appropriate in the circumstances, although his reasons reflect that he understood the nature and state of the Debtor Company's business.

17 The chambers judge considered various authorities in relation to the application for the DIP financing. After considering the benefits and prejudice of the DIP financing, the chambers judge concluded that it was appropriate to authorize it.

18 Finally, the chambers judge granted the expanded powers to the Monitor. This aspect of the order was not directly challenged on appeal, but it may be affected by the outcome on the first ground of appeal.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Appraisal Evidence

19 The affidavit of the principal of the Debtor Company filed at the time of the commencement of the *CCAA* proceeding exhibited the first 11 pages of two appraisals of portions of the development. As a result of the dispute between the parties over the value of the development, the Debtor Company applied for leave to file a supplemental appeal book containing complete copies of the appraisals. We tentatively received the supplemental appeal book subject to a subsequent ruling on the leave application.

20 In view of my conclusion on this appeal, the value of the development is not relevant. I would decline to grant the requested leave.

Standard of Review

21 Both aspects of the order challenged on appeal were discretionary in nature. The standard of review in respect of discretionary orders has been expressed in various ways. In *Reza v. Canada*, [1994] 2 S.C.R. 394, 116 D.L.R. (4th) 61 (S.C.C.), the standard of review was expressed in terms of whether the judge at first instance "has given sufficient weight to all relevant circumstances" (¶ 20).

22 In *Friends of the Oldman River Society v. Canada (Minister of Transport)*, [1992] 1 S.C.R. 3 at 76-7, 88 D.L.R. (4th) 1 (S.C.C.), the Court quoted the following statement in *Charles Osenton & Co. v. Johnston*, [1942] A.C. 130 (U.K. H.L.) at 138 with approval:

> The law as to the reversal by a court of appeal of an order made by the judge below in the exercise of his discretion is well-established, and any difficulty that arises is due only to the application of well-settled principles in an individual case. The appellate tribunal is not at liberty merely to substitute its own exercise of discretion for the discretion already exercised by the judge. In other words, appellate authorities ought not to reverse the order merely because they would themselves have exercised the original discretion, had it attached to them, in a different way. But if the appellate tribunal reaches the clear conclusion that there has been a wrongful exercise of discretion in that no weight, or no sufficient weight, has been given to relevant considerations such as those urged before us by the appellant, then the reversal of the order on appeal may be justified.

This passage was also referred to by this Court in a case involving the *CCAA*, *New Skeena Forest Products Inc., Re*, 2005 BCCA 192 (B.C. C.A.) at ¶ 20. Newbury J.A. also made reference in that paragraph to the principle that appellate courts should accord a high degree of deference to decisions made by chambers judges in *CCAA* matters and will not exercise their own discretion in place of that already exercised by the chambers judge. She also stated at ¶ 26 that appellate courts should not interfere with an exercise of discretion where "the question is one of the weight or degree of importance to be given to particular factors, rather than a failure to consider such factors or the correctness, in the legal sense, of the conclusion."

23 In my opinion, the comments of Newbury J.A. in *New Skeena* were directed at ongoing *CCAA* matters and do not necessarily apply to the granting and continuation of a stay of proceedings at the hearing of the initial *ex parte* application or the comeback hearing. However, in view of my conclusion on this appeal, I need not decide whether a different standard of review applies in respect of threshold decisions to grant or continue stays of proceedings in the early stages of *CCAA*

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

proceedings.

Analysis

24 On this appeal, the appellants challenge the decision of the chambers judge to continue the stay of proceedings until October 20, 2008, on the same basis as they opposed the application before the chambers judge. They say that the *CCAA* should not apply to companies whose sole business is a single land development or to companies whose business is essentially dormant. However, the real question is not whether the *CCAA* applies to the Debtor Company because it falls within the definition of "debtor company" in s. 2 of the *CCAA* and it satisfies the criterion contained in s. 3(1) of the *CCAA* of having liabilities in excess of $5 million. The *CCAA* clearly applies to the Debtor Company, and it is entitled to propose an arrangement or compromise to its creditors pursuant to the *CCAA*. The real question is whether a stay of proceedings should have been granted under s. 11 of the *CCAA* for the benefit of the Debtor Company.

25 I agree with the submission on behalf of the Debtor Company that the nature and state of its business are simply factors to be taken into account when considering under s. 11(6) whether it is appropriate to grant or continue a stay. If the more deferential standard of review is applicable to the granting and continuation of the stay of proceedings at the initial and comeback hearings, there would be insufficient basis to interfere with the decision of the chambers judge because he did give weight to these factors. However, there is another, more fundamental, factor that was not considered by the chambers judge.

26 In my opinion, the ability of the court to grant or continue a stay under s. 11 is not a free standing remedy that the court may grant whenever an insolvent company wishes to undertake a "restructuring", a term with a broad meaning including such things as refinancings, capital injections and asset sales and other downsizing. Rather, s. 11 is ancillary to the fundamental purpose of the *CCAA*, and a stay of proceedings freezing the rights of creditors should only be granted in furtherance of the *CCAA*'s fundamental purpose.

27 The fundamental purpose of the *CCAA* is expressed in the long title of the statute:

> An Act to facilitate compromises and arrangements between companies and their creditors.

28 This fundamental purpose was articulated in, among others, two decisions quoted with approval by this Court in *United Used Auto & Truck Parts Ltd., Re*, 2000 BCCA 146, 16 C.B.R. (4th) 141 (B.C. C.A.). The first is *Reference re Companies' Creditors Arrangement Act (Canada)*, [1934] S.C.R. 659, 16 C.B.R. 1 at 2, [1934] 4 D.L.R. 75 (S.C.C.), where the following was stated:

> . . . the aim of the Act is to deal with the existing condition of insolvency in itself to enable arrangements to be made in view of the insolvent condition of the company under judicial authority which, otherwise, might not be valid prior to the initiation of proceedings in bankruptcy. *Ex facie* it would appear that such a scheme in principle does not radically depart from the normal character of bankruptcy legislation."
>
> The legislation is intended to have wide scope and allow a judge to make orders which will effectively maintain the status quo for a period while the insolvent company attempts to gain the approval of its creditors for a proposed arrangement which will enable the company to remain in operation for what is, hopefully, the future benefit of both the company and its creditors.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

29 The second decision is *Hongkong Bank of Canada v. Chef Ready Foods Ltd.* (1990), 4 C.B.R. (3d) 311 (B.C. C.A.) at 315-16, where Gibbs J.A. said the following:

> The purpose of the *C.C.A.A.* is to facilitate the making of a compromise or arrangement between an insolvent debtor company and its creditors to the end that the company is able to continue in business. It is available to any company incorporated in Canada with assets or business activities in Canada that is not a bank, a railway company, a telegraph company, an insurance company, a trust company, or a loan company. When a company has recourse to the *C.C.A.A.*, the Court is called upon to play a kind of supervisory role to preserve the status quo and to move the process along to the point where a compromise or arrangement is approved or it is evident that the attempt is doomed to failure. Obviously time is critical. Equally obviously, if the attempt at compromise or arrangement is to have any prospect of success, there must be a means of holding the creditors at bay, hence the powers vested in the Court under s. 11.

30 Sections 4 and 5 of the *CCAA* provide that the court may order meetings of creditors if a debtor company proposes a compromise or an arrangement between it and its unsecured or secured creditors or any class of them. Section 6 authorizes the court to sanction a compromise or arrangement if a majority in number representing two-thirds in value of each class of creditor has voted in favour of it, in which case the compromise or arrangement is binding on all of the creditors.

31 The filing of a draft plan of arrangement or compromise is not a prerequisite to the granting of a stay under s. 11: see *Fairview Industries Ltd., Re* (1991), 109 N.S.R. (2d) 12, 11 C.B.R. (3d) 43 (N.S. T.D.). In my view, however, a stay should not be granted or continued if the debtor company does not intend to propose a compromise or arrangement to its creditors. If it is not clear at the hearing of the initial application whether the debtor company is intending to propose a true arrangement or compromise, a stay might be granted on an interim basis, and the intention of the debtor company can be scrutinized at the comeback hearing. The case of *Ursel Investments Ltd., Re* (1990), 2 C.B.R. (3d) 260 (Sask. Q.B.), rev'd on a different point (1991), 89 D.L.R. (4th) 246 (Sask. C.A.) is an example of where the court refused to direct a vote on a reorganization plan under the *CCAA* because it did not involve an element of mutual accommodation or concession between the insolvent company and its creditors.

32 Counsel for the Debtor Company has cited two decisions containing comments approving the use of the *CCAA* to effect a sale, winding up or liquidation of a company such that its business would not be ongoing following an arrangement with its creditors: namely, *Lehndorff General Partner Ltd., Re* (1993), 17 C.B.R. (3d) 24 (Ont. Gen. Div. [Commercial List]) at ¶ 7 and *Anvil Range Mining Corp., Re* (2001), 25 C.B.R. (4th) 1 (Ont. S.C.J. [Commercial List]) at ¶ 11), aff'd (2002), 34 C.B.R. (4th) 157 (Ont. C.A.) at ¶ 32. I agree with these comments if it is intended that the sale, winding up or liquidation is part of the arrangement approved by the creditors and sanctioned by the court. I need not decide the point on this appeal, but I query whether the court should grant a stay under the *CCAA* to permit a sale, winding up or liquidation without requiring the matter to be voted upon by the creditors if the plan of arrangement intended to be made by the debtor company will simply propose that the net proceeds from the sale, winding up or liquidation be distributed to its creditors.

33 Counsel for the Debtor Company also relies upon the decision in *Skeena Cellulose Inc., Re* (2001), 29 C.B.R. (4th) 157 (B.C. S.C.), where a creditor unsuccessfully opposed an extension of the stay of proceedings on the basis that the restructuring plan was wholly dependent upon the debtor company finding a purchaser of its assets. I note that the debtor company in that case was planning to make an arrangement with its creditors. I again query, without deciding, whether the court should continue the stay to allow the debtor company to attempt to fulfil a critical prerequisite to its plan of arrangement without requiring a vote by the creditors. I appreciate that it is frequently necessary for insolvent companies to satisfy certain prerequisites before negotiating a plan of arrangement with its creditors, but some prerequisites may be so fundamental that they should properly be regarded as an element of the debtor company's overall plan of arrangement.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

34 In the present case, the Debtor Company described its proposed restructuring plan in the following paragraphs of the petition commencing the *CCAA* proceeding:

> 47 The Petitioner intends to proceed with a three-part strategic restructuring plan consisting of:
>
> (a) securing sufficient funds to complete Phase 2 and 3;
>
> (b) securing access to water for the irrigation system of the golf course; and
>
> (c) finishing the construction of the golf course.
>
> 48 Upon completion of the matters described in the preceding paragraph, the Petitioner believes that proceeds generated from the sale of the remaining units in Phases 1-3, will be sufficient to fund the balance of the costs that will be incurred in completing the remaining portions of the Development.

35 It was not suggested in the petition, nor in the Monitor's report before the chambers judge at the comeback hearing, that the Debtor Company intended to propose an arrangement or compromise to its creditors before embarking on its restructuring plan. In my opinion, in the absence of such an intention, it was not appropriate for a stay to have been granted or extended under s. 11 of the *CCAA*. The chambers judge failed to take this important factor into account, and it is open for this Court to interfere with his exercise of discretion. To be fair to the chambers judge, I would point out that this factor was not drawn to his attention by counsel, and it was raised for the first time at the hearing of the appeal.

36 Although the *CCAA* can apply to companies whose sole business is a single land development as long as the requirements set out in the *CCAA* are met, it may be that, in view of the nature of its business and financing arrangements, such companies would have difficulty proposing an arrangement or compromise that was more advantageous than the remedies available to its creditors. The priorities of the security against the land development are often straightforward, and there may be little incentive for the creditors having senior priority to agree to an arrangement or compromise that involves money being paid to more junior creditors before the senior creditors are paid in full. If the developer is insolvent and not able to complete the development without further funding, the secured creditors may feel that they will be in a better position by exercising their remedies rather than by letting the developer remain in control of the failed development while attempting to rescue it by means of obtaining refinancing, capital injection by a new partner or DIP financing.

37 The failure of the chambers judge to consider the fundamental purpose of the *CCAA* and his error in extending the stay also infects his exercise of discretion in authorizing the DIP financing. If a stay under the *CCAA* should not be extended because the debtor company is not proposing an arrangement or compromise with its creditors, it follows that DIP financing should not be authorized to permit the debtor company to pursue a restructuring plan that does not involve an arrangement or compromise with its creditors. It also follows that expanded powers should not have been given to the Monitor.

38 I wish to add that it was open, and continues to be open, to the Debtor Company to propose to its creditors an arrangement or compromise along the lines of the restructuring plan described in paragraph 47 of the petition, although it may be a challenge to make such a plan attractive to its creditors. The creditors could then vote on such an arrangement or compromise which would involve, on their part, the concession that their rights would remain frozen while the Debtor Company carried out its restructuring. What the Debtor Company was endeavouring to accomplish in this case was to freeze the rights of all of its creditors while it undertook its restructuring plan without giving the creditors an opportunity to vote on the plan. The *CCAA* was not intended, in my view, to accommodate a non-consensual stay of creditors' rights while a debtor company attempts to carry out a restructuring plan that does not involve an arrangement or compromise upon which the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

creditors may vote.

Other Matters

39 In addition to the appellants and the Debtor Company, two persons appeared at the hearing of the appeal without having obtained intervenor status. The first was the Monitor, which also filed a factum. Other than clarifying certain facts, the factum was limited to the issue of preserving the charge against the assets of the Debtor Company as security for the Monitor's fees and disbursements in the event that the appeal was allowed on the appellants' first ground. In my opinion, the Monitor should have obtained intervenor status if it wished to make submissions on appeal, but the issue became academic when counsel for the appellants advised that his clients did not object to the Monitor retaining the priority charge for its fees and disbursements up to the day on which the decision on appeal is pronounced.

40 The second additional person appearing at the hearing of the appeal was Century Services Inc., which is the lender arranged by the Debtor Company to provide the DIP financing authorized by the chambers judge. Century Services Inc. wished to make submissions with respect to the priority charge for its financing, the first tranche of which was apparently advanced last week. After counsel for the appellants advised us that there were evidentiary matters subsequent to the decision of the chambers judge bearing on this issue, we declined to hear submissions on behalf of Century Services Inc. We did not have affidavits dealing with this matter, and the Supreme Court is better suited to deal with issues that may turn on the evidence.

Disposition

41 I would allow the appeal and set aside the order dated June 27, 2008. I would declare that the powers and duties of the Monitor contained in the orders dated May 26, 2008, and June 27, 2008, continued until today's date and that the Administration Charge created by the May 26 order shall continue in effect until all of the Monitor's fees and disbursements, including the fees and disbursements of its counsel, have been paid. I would remit to the Supreme Court any issues relating to the DIP financing that has been advanced.

***Frankel J.A.*:**

42 I agree.

***D. Smith J.A.*:**

43 I agree.

***Frankel J.A.*:**

44 The respondent's application to file a supplemental appeal book is dismissed. The appeal is allowed in the terms stated by Mr. Justice Tysoe.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Appeal allowed.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 5

2014 ONSC 2781
Ontario Superior Court of Justice [Commercial List]

Romspen Investment Corp. v. 6711162 Canada Inc.

2014 CarswellOnt 5836, 2014 ONSC 2781

Romspen Investment Corporation, Applicant and 6711162 Canada Inc., 1794247 Ontario Inc., 1387267 Ontario Inc., 1564168 Ontario Inc., 2033387 Ontario Inc., Hugel Lofts Ltd., Altaf Soorty and Zoran Cocov, Respondents

In the Matter of the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as Amended

In the Matter of 6711162 Canada Inc., and Those Other Companies Listed in Schedule "A" Hereto

D.M. Brown J.

Heard: May 2, 2014
Judgment: May 5, 2014
Docket: CV-14-10470-00CL, CV-14-10529-00CL

Counsel: S. Jackson, for Romspen Investment Corporation
D. Magisano, S. Puddister, for Respondents / CCAA Applicants, 6711162 Canada Inc., 1794247 Ontario Inc., 1387267 Ontario Inc., 1564168 Ontario Inc., 2033387 Ontario Inc., Hugel Lofts Ltd. and Casino R.V. Resorts Inc.
A. Bouchelev, for Altaf Soorty and Zoran Cocov
E. Tingley, for Pezzack Financial Services Inc.

Subject: Civil Practice and Procedure; Contracts; Corporate and Commercial; Estates and Trusts; Insolvency

Headnote

Bankruptcy and insolvency

Civil practice and procedure

Construction law

Debtors and creditors

***D.M. Brown J.*:**

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

I. Competing applications for the appointment of a receiver and the making of an initial order under the Companies' Creditors Arrangement Act

1 Romspen Investment Corporation ("Romspen") lent money to 6711162 Canada Inc. ("671") and certain related companies. That loan has matured and has not been repaid. Romspen applies for the appointment of a receiver under section 243(1) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, together with the appointment of a construction lien trustee pursuant to section 68 of the *Construction Lien Act*, R.S.O. 1990, c. C.30.

2 6711162 Canada Inc. and certain related companies opposed the appointment of a receiver and, instead, they have applied for an initial order under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36. Romspen opposed the making of a *CCAA* initial order.

3 The key business issue at stake in these competing applications is who gets to control the development and/or realization of a partially-completed residential condominium project in Midland, Ontario — a court-appointed receiver or the current owners and management of one of the CCAA Applicants, Hugel Lofts Limited?

4 For the reasons set out below, I grant the application for the appointment of a receiver and construction lien trustee, and I dismiss the application for an initial order under the *CCAA*.

II. Evidence about the debt and secured assets

5 Romspen is a commercial mortgage lender. The respondents, Altaf Soorty and Zoran Cocov, are the principals of a group of property holding and development companies which own parcels of land in Midland, Cambridge and Ramara, Ontario and to which Romspen lent money.

A. The Loan and the demands

6 By Commitment Letter dated July 18, 2011, Romspen agreed to provide 671162 Canada Inc. ("671") and 1794247 Ontario Inc. ("179") with a $16 million loan facility for a two year term expiring August 1, 2013. The Commitment Letter stated:

> The Loan shall be funded by way of advances, the amount(s) and timing of such advances(s) to be in the absolute discretion of Lender.

7 The funds were to be used "for general corporate purposes...to retire existing mortgage indebtedness [on two properties]...to pay fees and transaction costs, to set up an interest reserve, and up to $10,000,000 for the acquisition of additional real property, to be secured by mortgage(s) and other security satisfactory to Lender in its sole discretion."

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

8 The Loan was secured by first mortgages on three properties in Ramara, as well as by a second mortgage on a fourth. Three of the properties were owned by 671 and 179; the fourth was owned by Soorty and Cocov. The Commitment Letter stated that the Borrower had represented that the cumulative value of the four properties was $28.1 million. The Loan was also secured by general security agreements.

9 A year later, on June 12, 2012, the parties amended the Commitment Letter in several respects (the "First Supplement"). First, another company controlled by Soorty and Cocov, Casino R.V. Resorts Inc., was added as a "Borrower". Second, an additional advance of $470,000 was made, secured by two other properties. The parties agreed that this advance was transitional in nature and ultimately was taken out by replacement financing.

10 However, the principals of the CCAA Applicants made some very serious allegations about the validity of the First Supplement. Soorty, in his April 17, 2014 affidavit, deposed:

> I did not sign the said document and verily believe that it is a forgery. Unlike all other documents signed between Romspen Investment Corporation and myself, the pages of the First Supplement are not initialed and the signatures not witnessed, even though space for witnessess' signatures is provided.

Soorty so deposed evidently to support his contention that he had never agreed to make Casino R.V. a "Borrower" under the Loan, which on its face was one of the effects of the First Supplement. In his April 17 affidavit Cocov also alleged that his signature on the First Supplement was a forgery.

11 Romspen adduced evidence which showed that slightly over 15 other documents were signed as part of the additional $470,000 loan put in place by the First Supplement. Soorty signed many of those on behalf of Casino R.V. One of the documents was an opinion by corporate counsel for Casino R.V. dated June 14, 2012 which stated that the "Loan and Security Documents have been duly and validly executed and delivered by the Company and create valid and legally binding obligations of the Company enforceable against the Company in accordance with the term thereof".

12 After Romspen filed that evidence Soorty swore a further affidavit (April 23) in which he backpedalled from his forgery allegation, now contending that:

> I have no recollection of ever signing [the First Supplement]. If I ever did sign it, it was without understanding and appreciation of the nature and legal consequences of the document that was put in front of me.

Then, in his affidavit in support of the *CCAA* application, Soorty deposed that "even a cursory review of the First Amendment shows that it was put together in a rather hap-hazard fashion". Finally, in his second affidavit in support of the *CCAA* application, Soorty simply stated that the First Supplement "was placed in front of me with little time to obtain meaningful legal advice".

13 Yet, as will be discussed in detail shortly, on June 7, 2013, one year after the First Supplement, both Soorty and Cocov signed a forbearance letter with Romspen, including Soorty signing the letter on behalf of Casino R.V. Resorts Inc. Why, one might ask, if the First Supplement which added Casino R.V. as a Borrower was a "forgery" or was based on a lack of "understanding and appreciation", would Soorty proceed to sign, one year later, the forbearance letter on behalf of Casino? In my view the answer is clear — there is absolutely no basis to support the allegations of Soorty and Cocov that the First

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Supplement was a forgery or that they did not understand it. Their allegations of forgery can only be described as falsehoods, and such falsehoods severely undermine the credibility of the *CCAA* application given that Soorty and Cocov are the principals of the CCAA Applicants.

14 To continue with the technical narrative, a further amendment was made to the Commitment Letter on August 15, 2012 (the "Second Supplement"). Four entities were added as "Borrowers": Hugel Lofts Limited, 20333387 Ontario Inc., 1564168 Ontario Inc., and 1387267 Ontario Inc. The use of the loaned funds provision was amended so that the next advances under the Loan could be used by the Borrowers to refinance a condominium project in Midland and "to provide funds to assist in completion of construction on [the Midland Condo Project] on a cost to complete basis in accordance with a project budget to be approved by Lender (including contingency allowance satisfactory to Lender)(approximately $7,000,000) and to pay further fee and transaction costs."

15 Also, the Second Supplement increased the security provided by the Borrowers to include three Midland properties, including the lands upon which the Midland Condo Project was being built, as well as three properties in Cambridge. Romspen took first and second mortgages on the Midland lands, a first mortgage on one Cambridge property, and second mortgages on two other Cambridge properties which were behind mortgages held by Pezzack Financial Services Inc.

16 The mortgage security taken by Romspen contained a standard provision enabling it to appoint a receiver upon an event of default, and the chargor also agreed to consent to a court order appointing a receiver.

17 The Second Supplement also amended the Commitment Letter by adding, as a schedule, Romspen's Standard Construction Conditions. Section 4 of those Conditions stated:

> **4. Cost to Complete**
>
> The Lender shall not be required to make any advance unless prior to making such advance, the Lender is satisfied that the unadvanced portion of the Loan will be sufficient to pay the cost to complete the Project. Where insufficient unadvanced funds remain, the Borrower shall be required to pay such additional funds to the Lender so as to make the unadvanced portion of the Loan equal to the cost to complete.

18 According to Wesley Roitman, a Managing General Partner of Romspen, in the months following the execution of the Second Supplement Romspen became concerned that the costs to complete the Midland Condo Project would exceed the budgeted $7 million and that a funding gap of about $3.1 million would arise. On June 7, 2013, the parties entered into a forbearance agreement. After reciting the language of the Commitment Letter's Section 4 "Cost to Complete", the forbearance letter went on to state:

> At this time, the amount required to be invested by you to comply with Section 4 above, is $3,180,994.00. You have advised that you have been and are currently unable to fund this amount. *Your failure to fund this amount constitutes an act of default under the loan and the security granted in connection therewith.*
>
> (emphasis added)

19 Notwithstanding putting the Borrowers on notice that they had committed an act of default, in the forbearance letter

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Romspen stated that it agreed to forbear from exercising its available rights and remedies with respect to the act of default and would make the current advance requested by the Borrowers under the Loan "to fund continuing construction with respect to the condominium development at 151 Marina Park Avenue, Midland, Ontario".

20 The Borrowers did not invest the $3,180,994.00 stipulated in the forbearance agreement. The record showed that at most they invested a further $270,000 on June 20, 2013 and paid a supplier's $89,383 invoice on June 14, 2013.

21 Rompsen stopped making any further advances under the Loan in October, 2013.

22 In December, 2013, suppliers to the Midland Condo Project registered liens totaling about $2.248 million.

23 On January 3, 2014, Romspen sent to all of the Borrowers, except Casino, a demand letter and *BIA* s. 244(1) Notice of Intention to Enforce Security. The demand stated that as of January 3, 2014, the sum of $11.996 million was owed under the Loan. Payment was demanded by January 17, 2014. None was made.

24 On March 28, 2014, Romspen sent to Casino R.V. Resorts a demand letter and *BIA* s. 244(1) Notice of Intention to Enforce Security which stated that as of March 28, 2014 the amount due under the Loan was $12.284 million.

25 On March 4, 2014 Romspen commenced its application to appoint a receiver, subsequently amending its notice of application on April 3. A schedule for the hearing of Romspen's receivership application was set by the Court on April 11, 2014.

26 Then, on April 28, 2014, 671, 179, 1387267 Ontario Inc., 1564168 Ontario Inc., 2033387 Ontario Inc. and Hugel Lofts Ltd. (the "CCAA Applicants"), issued their notice of application seeking an initial order under the *CCAA*.

B. The businesses of the CCAA Applicants

27 Five of the CCAA Applicants own vacant land: 671 and 179 own the properties in Ramara, and 138, 156 and 203 own the Cambridge properties. At the present point of time, those CCAA Applicants operate simply as land holding companies; they have no employees.

28 The other CCAA Applicant, Hugel Lofts, owns the land on which the Midland Condo Project is located, together with two undeveloped parcels of land in Midland.

C. The Midland Condo Project and other Midland properties

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

29 The Midland Condo Project involves a partially constructed 4-storey residential building with 53 units. Construction is either about 50% or two-thirds completed, depending on which evidence one consults. The project has had a difficult development history, with Hugel Lofts acquiring the already-started project in power of sale proceedings in June, 2012 for $4 million, with a mortgage back for $3.1 million.

30 Between December 11 and December 20, 2013, trades registered six construction liens against the Midland Condo Project, with certificates of action registered this past January and February. In early April Hugel Lofts filed notices of intent to defend those lien actions. Construction has ceased on the Project.

31 There was a dispute in the evidence about the fair market value of the three properties in Midland. The CCAA Applicants pointed to an October 3, 2013 "short narrative appraisal" prepared by Real Estate Appraisers and Consulting Limited which appraised the properties at $18 million (the "RE Appraisal"). That appraisal consisted of an "as is" appraisal of the one parcel on which the Midland Condo Project is located (151 Marina Park Ave.), which the appraiser arrived at by deducting the costs to complete from an appraised "as if complete" sellout value for the 53 condo units. The RE Appraisal also contained "as if" appraisals of the other two Midland parcels assuming "all approvals for the proposed development are in place and the subdivisions registered" (Vindon and Victoria Streets).

32 The RE Appraisal recounted the following history of the Midland Condo Project as obtained from the current property owner — i.e. Hugel Lofts:

> Based on the information available, the structure was erected a few years ago by the previous owner. Due to finance and other difficulties, the construction work was (sic) for several years. This property in conjunction with the remaining undeveloped lands was sold under power of sale in 2012. Our client (the new owner) reported that the construction work was resumed in summer 2013.
>
> . . .
>
> The building as of the date of appraisal is described as about 50% completed.
>
> It is also reported that all units were completely presold by the previous owner for about $275 per sq ft. These sales were however void after liquidation of the previous owner.
>
> Per our client, that marketing of the new project will be launched in Spring 2014 and the new price range will be between $300 and $325 per sq ft. *Our client reported that many of the previous buyers show strong interest of coming back.*
>
> (emphasis added)

Photographs of the Midland Condo Project taken by the appraiser in October, 2013 showed significant completion of the exterior work on the building, but the need for extensive interior work.

33 The RE Appraisal used a "cost to complete" for the Midland Condo Project of $6.591 million based upon a payment schedule dated September 15, 2013 provided by the general contractor, Sierra Construction. Sierra's schedule recorded a total value for its construction contract of $7.452 million, with the value of work done to that date of $1.145 million.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

34 Hugel Lofts proposes to build on the two undeveloped parcels (Vindon and Victoria Streets) 68 condo apartment units, 39 senior apartment units, 66 bungalows, 62 townhouse units and 80,000 sq. ft. of commercial space. The RE Appraisal assigned an "as is" value to 151 Marina Park of $10.6 million, and a "hypothetical" "as if" value of $7.4 million to the other two parcels.

35 Romspen's internal valuations placed the worth of the Midland properties at far less than $18 million.

D. The Ramara properties

36 The CCAA Applicants contended that the four Ramara Properties — 5781 Rama Road, 5819 Rama Road, 4243 Hopkins Bay Road and 4285 Hopkins Bay Road — were worth about $27 million on a built-out basis. An August 11, 2010 narrative appraisal of the vacant, unserviced development land prepared by Schaufler Realty Advisors for 671 provided a "hypothetical value of the subject site as fully serviced sites approved for the contemplated commercial and residential development" as of October 6, 2012 of $27.1 million.

37 The Schaufler Appraisal noted that the four properties had been acquired for $4.4 million.

38 A November 21, 2013 "draft" appraisal prepared by Schaufler also used a $27.1 million hypothetical value.

39 Romspen's internal valuations placed the "as is" worth of the Ramara properties at far, far less than $27.1 million.

E. The Cambridge Properties

40 138, 156 and 203 own six parcels of vacant land in Cambridge, some of which are "brown-field" lands which will require remediation for environmental reasons. Romspen holds first mortgages over the Cambridge properties owned by 138, and second mortgages over those owned by 156 and 203, with Pezzack Financial Services and TD Canada Trust holding $300,000 in first mortgages on those properties.

III. Evidence about the owners' approach should the Court grant a CCAA initial order

41 Soorty deposed that the CCAA Applicants intend to complete the Midland Condo Project without any further financial support from Romspen and he believed that the proceeds from condo units sales would be "sufficient to repay Romspen, resolve any lien claims and make a proposal to creditors using the remaining properties as the basis for that proposal":

> The Applicants simply want to complete the Condo Project with funds that will likely be supplied by Zoran and I (from our own resources) and repay Romspen the funds they did advance once the Condo Project is complete.

Soorty deposed elsewhere:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> ... I believe that Zoran and I should have the opportunity to restructure the Applicants' affairs, repay Romspen on its loan, pay remaining creditors and keep control of our real estate development projects. As shown above, there is more than enough value in the Applicants' assets to repay Romspen in full.

A. Proposed sources of funds

A.1 Principals of CCAA Applicants mortgage other assets under their control

Harbour Mortgage

42 As to the sources of those funds, Soorty deposed that a related company, 1026517 Ontario Limited, owned lands in Mississauga which secured a collateral mortgage in favour of Harbour Mortgage Corp. in the amount of $8 million. He deposed that Harbour Mortgage had "agreed to increase the loan amount to $11,250,000, thereby providing 1026517 Ontario Limited with an additional $3,250,000. I intend to use these funds to finish the construction at the Midland Property".

43 The April 2, 2014 term sheet signed by Harbour Mortgage had not been signed and accepted by Soorty on behalf of 1026517 Ontario. The "loan amount" of $11.25 million was "not to exceed 65% of the appraised value and/or value as determined by the Lender" of the Mississauga properties. No evidence of their value was placed in evidence. The term sheet offered a loan with a 12-month term, and described the "use of funds" as follows:

> The proceeds of the Loan shall be used to refinance existing debt and to repatriate Borrower equity for planned future development.

The term sheet made no reference to a permitted use of funds for the Midland Condo Project.

National Bank

44 Cocov deposed that he was the President of Harmony Homes Oshawa Ltd., a recently completed townhome condominium project in Oshawa, and that the National Bank had agreed to provide Harmony Homes with a mortgage for $4.8 million: "I intend to use these funds to complete construction at 151 Marina Park Avenue, Midland, Ontario."

45 Cocov attached to his affidavit an April 11, 2014 "Discussion Paper" from National Bank which stated: "This Discussion Paper is an outline of proposed terms for purpose of considering your application only and is not: (i) a commitment letter; nor (ii) an agreement to provide financing". The Discussion Paper only referenced the Oshawa property, and it described the "purpose of proposed loan" as "refinancing", with the "type of facility" as "first rank conventional mortgage financing". The Discussion Paper made no reference to the Midland Condo Project, and I infer from its terms that the bank simply envisaged that its loan would replace the existing financing for the Oshawa property.

46 Harmony Home signed the Discussion Paper on April 17, 2014. This motion was heard on May 2. No detailed evidence was provided concerning what discussions, if any, had ensued between Harmony Home and National Bank between April 17 and May 2.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

47 The Projected Statement of Cash Flows for the period May 2 through to June 6, 2014 filed by the CCAA Applicants did not make any reference to cash receipts from financings from either Harbour Mortgage or National Bank.

A.2 Proposed DIP Financing

48 Soorty deposed that the CCAA Applicants would require $250,000 to complete four model suites, together with $50,000 in soft costs to begin pre-sales. Soorty and Cocov would finance those costs using their personal funds to make available up to $300,000 in "drip" financing, provided their financing was given a DIP Priority Charge.

49 The filed CCAA Cash Flow statement contemplated using $150,000 of the DIP financing during the initial 30-day period.

A.3 HST Refund

50 Soorty deposed that in early April, 2014, Cocov had contacted the CRA which had advised that it had approved an HST refund to Hugel Lofts of about $254,000. The filed CCAA Cash Flow statement contemplated receipt of the HST Tax refund during the week of May 23, 2014. The CCAA Applicants did not adduce any written communications from CRA which confirmed the entitlement to the HST Refund or the expected date of refund issuance.

B. Costs to complete the Midland Condo Project

51 As to the costs to complete the Midland Condo Project, Soorty initially deposed that the Project's general contractor, Sierra Construction (Woodstock) Limited:

> [I]s prepared to complete the Condo Project for $5.5 million plus H.S.T. (the "Project Completion Costs"). In fact, they have guaranteed to complete the Condo Project for no more than then Project Completion Costs.

The April 23, 2014 Sierra Construction letter which Soorty filed in support of that evidence did not support Soorty's assertion. Sierra Construction did write that "the all in number to complete should be $5,500,000.00 (HST is not included)". However, it continued:

> Sierra, the project trades and their respective suppliers have suffer and continue to suffer damages as a result of non-funding. Collectively and in the interest of the Lien holders, we request the project/developer not be placed in receivership and the courts allow the project to be completed. Our summary would indicate the costs spent to date and the costs to complete weighted against the projected revenues, support the request for the project to continue to completion. We look forward in assisting you in completing this project.

Sierra's letter contained no "guarantee" that it would complete construction for $5.5 million.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

52 In a subsequent affidavit Soorty attached a further, April 28, 2014 letter from Sierra which stated, in part:

> The outstanding Construction Liens cumulative balance is $1,378,605.02 per our understanding you intend to vacate the liens. Some contractor Liens are in dispute, the true Lien value is $957,949.00. The remaining cost to complete the construction portion of the project plus consulting fees, Tarion Warranty inspections, Models suite upgrades, the all in number to complete should be $5,500,000.00 (HST is not included). Based on earlier submission/correspondence Sierra is prepared to enter into a fix price contract for the remainder of the project work.
>
> Collectively and in the interest of the Lien holders, we request the project/developer not be placed in receivership and the courts allow the project to be completed. We look forward in assisting you in completing this project.

53 The CCAA Applicants did not file a detailed statement from Sierra which identified the work needed to complete the Midland Condo Project, similar to the one attached as Appendix "E" to the October, 2013 RE Appraisers report, nor did they file any explanation about why Sierra, which in that October, 2013 statement valued the work remaining to be done at $6.3 million, would be prepared to commit to complete the work for the significantly lesser amount of $5.5 million.

54 Also, Sierra's April 28 letter suggested that it would not be prepared to resume work unless its lien was vacated. The CCAA Applicants did not address where the funds would come from to either pay off or bond off Sierra's lien, let alone those of other lien claimants, apart from their evidence about dealings with Harbour Mortgage and National Bank.

55 Romspen filed its own internal calculations which placed all of the costs to complete — both "hard" and "soft" — several million dollars higher than the $5.5 million referred to by Sierra.

C. Summary

56 In sum, the evidence filed by the CCAA Applicants disclosed that, if granted CCAA protection, they would look to the future sale of the units from the Midland Condo Project to "repay the Romspen Indebtedness in full and provide funds for resolving lien claims". The evidence of projected unit sales revenue of $17.579 million filed by the CCAA Applicants consisted of a short email (which contained no date) from Mr. Jonathan Weizel, who described himself as a sales representative at Royal LePage Terrequity Realty in Thornhill. Soorty deposed that Weizel had been responsible for selling out the Midland Condo Project before the previous owners were placed into a receivership.

57 Soorty also deposed that the CCAA Applicants proposed "...leaving the balance of the Applicants' assets as a basis for a proposal to the Applicants' remaining creditors". In terms of the amounts due to those "remaining creditors", Crowe Soberman Inc., in its April 30, 2014 Pre-Filing Report in its capacity as the proposed Monitor, estimated the amounts owed by Hugel Lofts at $15.98 million, consisting of $12 million due to Romspen, $958,000 due to lien claimants, and $3 million due to unsecured creditors, including related parties. Soorty deposed:

> The most significant unsecured creditors are Zoran and I with respect to shareholder loans we have made to facilitate completion of the Condo Project.

58 Soorty, in his *CCAA* affidavit, deposed that save for Hugel Lofts, the other CCAA Applicants have "nominal financial

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

obligations", and Crowe Soberman made no mention of any other liabilities concerning the CCAA Applicants, from which I infer that such liabilities are limited to the amounts contained in the charges registered against the Ramara and Cambridge properties owned by the CCAA Applicants.

IV. Analysis

A. A summary of the applicable legal principles

59 Romspen seeks the appointment of SF Partners Inc. as receiver and construction lien trustee over the respondents under *BIA* s. 243(1), section 101 of the *Courts of Justice Act* and section 68 of the *Construction Lien Act*. In *Bank of Nova Scotia v. Freure Village on Clair Creek*, the court reviewed the factors to be taken into account in considering a request to appoint a receiver:

> The Court has the power to appoint a receiver or receiver and manager where it is "just or convenient" to do so: the *Courts of Justice Act*, R.S.O. 1990, c. 43, s. 101. In deciding whether or not to do so, it must have regard to all of the circumstances but in particular the nature of the property and the rights and interests of all parties in relation thereto. The fact that the moving party has a right under its security to appoint a receiver is an important factor to be considered but so, in such circumstances, is the question of whether or not an appointment by the Court is necessary to enable the receiver-manager to carry out its work and duties more efficiently...It is not essential that the moving party, a secured creditor, establish that it will suffer irreparable harm if a receiver-manager is not appointed....
>
> While I accept the general notion that the appointment of a receiver is an extraordinary remedy, it seems to me that where the security instrument permits the appointment of a private receiver - and even contemplates, as this one does, the secured creditor seeking a court appointed receiver - and where the circumstances of default justify the appointment of a private receiver, the "extraordinary" nature of the remedy sought is less essential to the inquiry. Rather, the "just or convenient" question becomes one of the Court determining, in the exercise of its discretion, whether it is more in the interests of all concerned to have the receiver appointed by the Court or not. This, of course, involves an examination of all the circumstances which I have outlined earlier in this endorsement, including the potential costs, the relationship between the debtor and the creditors, the likelihood of maximizing the return on and preserving the subject property and the best way of facilitating the work and duties of the receiver-manager.[1]

60 The CCAA Applicants seek the making of an initial order under *CCAA* s. 11.02. In broad terms, the purpose of the *CCAA* is to permit a debtor to continue to carry on business and, where possible, avoid the social and economic costs of liquidating its assets. As pointed out by the Supreme Court of Canada in *Century Services Inc. v. Canada (Attorney General)*:

> 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.[2]

61 Both an order appointing a receiver and an initial order under the *CCAA* are highly discretionary in nature, requiring a court to consider and balance the competing interests of the various economic stakeholders. As a result, the specific factors taken into account by a court are very circumstance-oriented. In the case of land development companies, some courts have identified several of the factors which might influence a decision about whether to grant an initial order under the *CCAA*. For example, in *Cliffs over Maple Bay Investments Ltd. v. Fisgard Captial Corp.*, the British Columbia Court of Appeal stated:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Although the *CCAA* can apply to companies whose sole business is a single land development as long as the requirements set out in the *CCAA* are met, it may be that, in view of the nature of its business and financing arrangements, such companies would have difficulty proposing an arrangement or compromise that was more advantageous than the remedies available to its creditors. The priorities of the security against the land development are often straightforward, and there may be little incentive for the creditors having senior priority to agree to an arrangement or compromise that involves money being paid to more junior creditors before the senior creditors are paid in full. If the developer is insolvent and not able to complete the development without further funding, the secured creditors may feel that they will be in a better position by exercising their remedies rather than by letting the developer remain in control of the failed development while attempting to rescue it by means of obtaining refinancing, capital injection by a new partner or DIP financing.[3]

62 More recently, C. Campbell J., in *Re Dondeb Inc.*, after quoting the above passage from *Cliffs over Maple Bay*, stated:

Similarly, in *Octagon Properties Group Ltd.*, [2009] A.J. No. 936, 2009 CarswellAlta 1325 (Q.B.), paragraph 17, Kent, J. made the following comments:

> This is not a case where it is appropriate to grant relief under the CCAA. First, I accept the position of the majority of first mortgagees who say that it is highly unlikely that any compromise or arrangement proposed by Octagon would be acceptable to them. That position makes sense given the fact that if they are permitted to proceed with foreclosure procedures and taking into account the current estimates of value, for most mortgagees on most of their properties they will emerge reasonably unscathed. There is no incentive for them to agree to a compromise. On the other hand if I granted CCAA relief, it would be these same mortgagees who would be paying the cost to permit Octagon to buy some time. Second, there is no other reason for CCAA relief such as the existence of a large number of employees or significant unsecured debt in relation to the secured debt. I balance those reasons against the fact that even if the first mortgagees commence or continue in their foreclosure proceedings that process is also supervised by the court and to the extent that Octagon has reasonable arguments to obtain relief under the foreclosure process, it will likely obtain that relief.

A similar result occurred in *Shire International Real Estate Investments Ltd.*, [2010] A.J. No. 143, 2010 CarswellAlta 234, even after an initial order had been granted.

In *Edgeworth*, dealing with the specifics of that case I noted:

> Were it not for the numerous individual investors (UDIs, MICs) and others who claim to have any interest in various of the lands as opposed to being general creditors of the Edgeworth companies, I doubt I could have been persuaded to grant the Initial CCAA Order.

. . .

[In the present case] the request for an Initial Order under the *CCAA* was dismissed for the simple reason that I was not satisfied that a successful plan could be developed that would receive approval in any meaningful fashion from the creditors. To a large extent, Mr. Dandy is the author of his own misfortune not just for the liquidity crisis in the first place but also for a failure to engage with creditors as a whole at an early date.

In his last affidavit filed Mr. Dandy explained why certain properties were transferred into individual corporations to allow additional financing that would permit the new creditors access to those properties in the event of default. To a certain extent this was perceived by creditors as "robbing Peter to pay Paul" and led to the distrust and lack of confidence the vast majority of creditors exhibit. Had there been full and timely communication both the creditors and the court may have concluded that a *CCAA* plan could be developed.

. . .

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Following further submissions on behalf of the debtor I advised the parties that in my view the conditions necessary for approval of an Initial *CCAA* Order were not met but that a comprehensive Receivership Order should achieve an orderly liquidation of most of the properties and protect the revenue from the operating properties with the hope of potential of some recovery of the debtor's equity.[4]

B. Applying the legal principles to the evidence

63 The evidence adduced by Romspen established the indebtedness of the Borrowers under the Loan, the maturing of the Loan facility in September, 2013, the demands for payment, the failure of the Borrowers to repay the amount demanded and the validity of the security held by Romspen on the Ramara, Midland and Cambridge properties. The Borrowers did not dispute the amount owed, and the security documents contained a clear contractual right of Romspen to appoint a receiver upon an act of default and required the Borrowers, in such circumstances, to consent to an order appointing a receiver. An active development was underway on only one of the properties securing the Loan — the Midland Condo Project — the other lands being vacant and undeveloped. The other creditors who hold security against the Cambridge lands did not oppose the appointment of a receiver. Pezzack Financial simply submitted that in the event a receiver were appointed, the receiver should not enjoy priority over Pezzack Financial for its fees and expenses on those properties where Pezzack Financial held the first mortgages. The lien claimants against the Midland Condo Project did not appear on the return of the application, although served with the court materials. Sierra Construction provided the Borrowers with a letter of support, but did not formally appear in the proceeding.

64 In the usual course of affairs those circumstances would point towards the appropriateness of granting the requested order appointing a receiver, as well as a construction lien trustee. However, the Borrowers opposed the making of such an order on two main grounds. First, they argued that by its conduct Rompsen had caused the Borrowers to default under the Loan and Romspen should not be allowed to take advantage of such conduct. Second, they contended that the plan advanced by the CCAA Applicants offered a fairer way to balance the competing economic interests at play and any consideration of the appointment of a receiver should be deferred until the CCAA Applicants had been afforded an opportunity to complete the Midland Condo Project. Let me deal with each argument in turn.

65 First, Soorty, in his affidavit in support of the CCAA application, and the CCAA Applicants in their written submissions to the Court, contended that their default on the Loan was caused by Romspen's wrongful failure to advance the full amount of the Loan as it was contractually required to do, leading to the trades to lien the Midland Condo Project. The CCAA Applicants argued that a lender was not entitled to take advantage of, or seek relief in respect of, a default which its own wrongful conduct had created.

66 While the authorities certainly contemplate that a court may refuse to appoint a receiver where the lender's conduct has placed the debtor in default of its borrowing obligations,[5] that is not this case. When the Loan facility was amended to permit the use of funds for the continued construction of the Midland Condo Project, the Second Supplement, by incorporating Section 4 of Romspen's Standard Construction Conditions, made quite express the circumstances under which Rompsen was required to advance further funds for that project:

> The Lender shall not be required to make any advance unless prior to making such advance, the Lender is satisfied that the unadvanced portion of the Loan will be sufficient to pay the cost to complete the Project. Where insufficient unadvanced funds remain, the Borrower shall be required to pay such additional funds to the Lender so as to make the unadvanced portion of the Loan equal to the cost to complete.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

67 The June, 2013 Forbearance Letter contained an acknowledgement by the Borrowers of their failure to have advanced their own funds towards the Midland Condo Project:

> At this time, the amount required to be invested by you to comply with Section 4 above, is $3,180,994.00. You have advised that you have been and are currently unable to fund this amount. *Your failure to fund this amount constitutes an act of default under the loan and the security granted in connection therewith.*

68 In sum, the evidence established that it was the failure of the Borrowers to abide by the terms of the Commitment Letter, as amended by the Second Supplement and the Forbearance Letter, which led to them to commit acts of default.

69 The CCAA Applicants also strongly intimated in their evidence that throughout the earlier part of this year Romspen had misled them into thinking that the difficulties with the Loan could be worked out. In support of that submission they pointed to language in an April 4, 2014 email from Roitman to them which talked about the completion of the Midland Condo Project as "clearly...the best outcome for all of us". That was not an accurate characterization of the email by the CCAA Applicants, as can be seen when one reads the email in full:

> Al, these emails are not really very useful. As we have discussed at length, Romspen's lawyers need to push our case forward as forcefully as they can. This does not prevent us from changing course later on. When you and Zoran have your affairs arranged to the point where you can move the project forward again, we will be glad to discuss terms for reinstating the loan and completing the project. Clearly this would be the best outcome for all of us, *but we have waited about one year already for you guys to work things out between each other and to find the funding to cover the cost, and we just can't wait forever.*
>
> (emphasis added)

70 The last phrase in Roitman's email most likely suggests the real reason for the default of the CCAA Applicants under the Loan — internal disagreements between Soorty and Cocov about how much each of them should contribute to the continued construction of the Midland Condo Project. The June 7, 2013 forbearance agreement signed by both hinted at this problem, with its reference to Soorty and Cocov having advised "that you have been and are currently unable to fund this amount" (i.e. $3.18 million). Soorty expressly referred to the internal problems in paragraph 55 of his *CCAA* initial affidavit when he deposed: "As a sign of our good faith, I was prepared to put $2 million towards the Condo Project immediately, however, Zoran required additional time to finalize similar financing".

71 Turning to the second argument advanced by the Borrowers/CCAA Applicants, does their proposed approach to complete the construction of the Midland Condo Project offer a better, more practical alternative to Romspen's proposed appointment of a receiver?

72 At a high level, a certain unfairness characterizes the plan of the CCAA Applicants. Under their plan, they would see the development of the Midland Condo Project to its end and use the unit sales proceeds to pay off Romspen in full and, evidently, to pay most of the amounts sought by the lien claimants. They would then develop out the other secured properties to propose a plan to the other unsecured creditors, but according to Soorty most of the unsecured debt consists of shareholders loans from Cocov and himself. Reduced to its essence, the plan seems to be no more than asking the court to impose on Romspen an extension of the term of the Loan beyond its 2-year term and to allow management to continue operating as they have in the past. In other words, the CCAA Applicants do not propose the compromise of debt or the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

liquidation of part of their businesses — they want to carry on just as they have in the past.

73 I accept the evidence of Romspen about the unfairness of such an approach. Romspen stated that it had "absolutely no confidence" in the ability of Soorty and Cocov to manage the affairs of the CCAA Applicants during any stay period, pointing to them letting the first general contractor on the Midland Condo Project, Dineen, place liens on it, and allowing subsequent contractors to do so as well. Roitman also deposed about Soorty and Cocov:

> They have evidently been unable to manage their mutual partnership relationship. Moreover, notwithstanding their purported ability according to the Soorty affidavit to refinance their obligations to Romspen with other assets they control, they have had over 12 months to make those arrangements and have failed to do so. Had they done so, Romspen would have extended the facility.
>
> There is no plan acceptable to Romspen short of immediate payment in full. The plan proposed by the Debtors, apart from the priming of Rompsen's security and the multi-layered professional expenses associated with a CCAA, in circumstances where there is no operating business, amounts to little more than what Messrs. Soorty and Cocov have been unable to do over the past 12 months.

74 Two other questions arise as part of this higher level analysis. First, the RE Appraisal recited that management had told the appraiser that "all units were completely presold by the previous owner" and "many of the previous buyers show strong interest in coming back". If that in fact was the case, why have Soorty and Cocov been unable to attract replacement financing for the Midland Condo Project? Second, the CCAA Applicants emphasized the significant equity available in the other Midland properties, as well as the Ramara and Cambridge properties, arguing that Romspen should hang in for the duration of the Midland Condo Project because it was fully secured. Perhaps the more appropriate question to pose is why the CCAA Applicants are not prepared to realize on some of the equity in those other properties to pay out Romspen now, given that the Loan matured well over half a year ago? The answer appears to be that they want the *CCAA* initial order to secure for them a compelled extension of the term of the Romspen Loan at minimal cost. I do not regard that as a proper use of the *CCAA* process in the circumstances.

75 Other questions arise when one turns to the specifics of the general plan proposed by the CCAA Applicants. It is apparent that the proposed DIP financing would be wholly inadequate to complete the construction of the Midland Condo Project. Where will the other funds come from? The suggestion by the CCAA Applicants that National Bank and Harbour Mortgage may serve as sources for such financing simply is not borne out by the specifics contained in the respective Discussion Paper and Term Sheet. Put another way, I see no credible evidence before the Court to suggest that that the CCAA Applicants are anywhere close to finding sources to fund the costs to complete the construction of the Midland Condo Project, let alone to resolve the existing lien claims which one would expect would be one of the necessary first steps to get this project back up and running.

76 Further, the 30-day Cash Flow statement filed in support of the short-term plan to build model suites rested heavily on the receipt of the HST Refund, yet the CCAA Applicants placed no evidence before the Court from CRA which would indicate that such a refund would be received within the next 30 days.

77 Finally, I would have very strong reservations about leaving the court-supervised completion of the Midland Condo Project in the hands of Soorty and Cocov, even with a Monitor present. As I mentioned earlier, their allegations that their signatures had been forged on the First Supplement were without foundation and most seriously undermined their credibility. Also, Soorty exaggerated his evidence on other important issues, such as the actual purposes of the funds being sought from

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

National Bank and Harbour Mortgage, as well as his initial characterization of Sierra Construction having offered a "guaranteed" cost to complete.

78 For these reasons, I dismiss the application by the CCAA Applicants for an initial order under the *CCAA*, and I grant the application of Romspen for the appointment of SF Partners Inc. as receiver and construction lien trustee.

C. The scope of the appointment

79 Romspen holds security, by way of mortgages and general security agreements, over the companies which own the Ramara Properties — 6711162 Canada Inc. and 1794247 Ontario Inc. — the companies which own the Cambridge Properties — 1387267 Ontario Inc., 1564168 Ontario Inc. and 2033387 Ontario Inc. — and the company which owns the Midland Properties - Hugel Lofts Ltd. A receiver is appointed over those companies and those properties.

80 One of the Ramara Properties — 4271-4275 Hopkins Bay Road, Rama — is owned by Altaf Soorty and Zoran Cocov. At the hearing I had questioned Romspen's counsel about why his client was seeking the appointment of a receiver over Soorty and Cocov. He responded by pointing to GSAs given by both individuals to Romspen. After further discussion counsel advised that he had received instructions to withdraw the request for a receiver over Soorty and Cocov. I had not been able to read most of the application records prior to the hearing. I now see that Romspen obtained a charge from Soorty and Cocov over the Hopkins Bay Road properties owned by them. My queries about the need to appoint a receiver over the individual respondents were not focused on that property, but on whatever other assets the two individuals possessed. Consequently, I consider it most appropriate to appoint a receiver over the property owned by Soorty and Cocov at 4271-4275 Hopkins Bay Road, Rama.

81 Much ink was spilt by both sides over the appointment of a receiver over Casino R.V. Resorts Inc. That issue can be dealt with quickly. Romspen loaned money to Casino and received a package of security in return, part of which included the addition of Casino as a "Borrower" under the Commitment Letter pursuant to the First Supplement. All parties agreed that that loan was repaid in full. On July 16, 2012, Romspen wrote that upon receipt of the amount to pay out the loan to Casino, it would provide its signed authorization to register its assignment of its *PPSA* registrations in respect of the loan, as well as a release of its interest. The loan was repaid, but apparently Romspen did not provide those documents. It contended it was never asked to do so.

82 Be that as it may, while I am prepared to grant Romspen's request to add Casino R.V. Resorts Inc. as a party to the receivership application, I am not prepared to appoint a receiver over Casino or any properties it previously provided as security. The appointment of a receiver is an equitable remedy. Casino repaid the loan and Romspen agreed to release its interest. Under those circumstances, it is neither fair nor reasonable for Romspen to seek the appointment of a receiver over Casino.

83 Counsel for Romspen circulated a draft appointment order at the hearing. On behalf of Pezzack Financial Services Inc., Mr. Tingley submitted that the receiver's charge should not enjoy priority over his client's first mortgages on Cambridge Properties because the receivership really concerned a dispute involving the Midland Condo Project. That was a reasonable request in the circumstances, and I order that in respect of the Cambridge Properties the charge granted to the receiver shall stand subordinate to any first charges registered against those properties by any person other than Romspen.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

84 A sealing order shall issue in respect of the Confidential Exhibits to the Affidavit of Wesley Roitman in order to preserve the integrity of any sales and marketing process undertaken by the Receiver. Counsel can submit a revised draft appointment order to my attention through the Commercial List Office for issuance.

V. Costs

85 I would encourage the parties to try to settle the costs of these applications. If they cannot, Rompsen may serve and file with my office written cost submissions, together with a Bill of Costs, by May 16, 2014. Any party against whom costs are sought may serve and file with my office responding written cost submissions by May 29, 2014. The costs submissions shall not exceed three pages in length, excluding the Bill of Costs.

86 Any responding cost submissions should include a Bill of Costs setting out the costs which that party would have claimed on a full, substantial, and partial indemnity basis. If a party opposing a cost request fails to file its own Bill of Costs, I shall take that failure into account as one factor when considering the objections made by the party to the costs sought by any other party. As Winkler J., as he then was, observed in *Risorto v. State Farm Mutual Automobile Insurance Co.*, an attack on the quantum of costs where the court did not have before it the bill of costs of the unsuccessful party "is no more than an attack in the air".[6]

Footnotes

1 (1996), 40 C.B.R. (3d) 274 (Ont. Gen. Div.), paras. 10 and 12.

2 [2010] 3 S.C.R. 379, para. 14.

3 2008 BCCA 327, para. 36.

4 2012 ONSC 6087, paras. 19-21, 25, 26 and 31.

5 *Royal Bank of Canada v. Chongsim Investments Ltd.* (1997), 456 C.B.R. (3d) 267 (Ont. Gen. Div.)

6 (2003), 64 O.R. (3d) 135 (S.C.J.), para. 10, quoted with approval by the Divisional Court in *United States of America v. Yemec*, [2007] O.J. No. 2066 (Div. Ct.), para. 54.

End of Document Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 6

2012 ONSC 6087
Ontario Superior Court of Justice [Commercial List]

Dondeb Inc., Re

2012 CarswellOnt 15528, 2012 ONSC 6087, 223 A.C.W.S. (3d) 772, 97 C.B.R. (5th) 264

In the Mater of the Companies Creditors Arrangement Act, R.S.C. 1985, c. C-36, as Amended

In the Matter of a Proposed Plan of Compromise or Arrangement with Respect to Dondeb Inc. and the Additional Applicants Listed on Schedule "A" Hereto (collectively, the "Applicants"), Applicants

C. Campbell J.

Heard: October 11, 15, 17, 18 2012
Judgment: November 22, 2012
Docket: CV-12-00009865-00CL

Counsel: David P. Preger, Lisa S. Corne, Michael Weinczok for Applicants
Jeffrey J. Simpson, A. Ronson for Pace Savings & Credit Union Limited
Gary Sugar for David Sugar, et al
D.R. Rothwell for RMG Mortgage/MCAP Financial Corporation
Harry Fogul for Regional Financial
Robin Dodokin for Empire Life Insurance Co.
Beverly Jusko, M.R. Kestenberg for TD Bank Canada Trust
Roger Jaipargas for Faithlife Financial
R.B. Bissell for Vector Financial Services Limited
Jeffrey Larry for First Source Mortgage Corporation
Douglas Langley for Virgin Venture Capital Corporation
David Mende for Addenda Capital Inc.
J. Dietrich, W. Rabinovitch for A. Farber & Partners Inc.
M. Church for SEIU (Union)

Subject: Insolvency; Property

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy and insolvency — Companies' Creditors Arrangement Act — Initial application — Dismissal of application

Debtors were group of companies which owned and managed properties — Debtors brought application for initial order

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

under Companies' Creditors Arrangement Act — Application dismissed — Unlikely that plan could be developed that sufficient number of creditors would agree to — Application was opposed by approximately 75 per cent of creditors, who had concerns about principal of group of companies' plan to transfer certain properties to secure additional funding, and did not wish debtor-in-possession financing to occur — Principal had not engaged with creditors from early date and was to some extent author of own misfortune — Goal of protection under Act was liquidation, which could be achieved by appointing receiver.

Table of Authorities

Cases considered by *C. Campbell J.*:

Azure Dynamics Corp., Re (2012), 91 C.B.R. (5th) 310, 2012 CarswellBC 1545, 2012 BCSC 781 (B.C. S.C. [In Chambers]) — referred to

Cliffs Over Maple Bay Investments Ltd. v. Fisgard Capital Corp. (2008), 2008 BCCA 327, 2008 CarswellBC 1758, 83 B.C.L.R. (4th) 214, 296 D.L.R. (4th) 577, 434 W.A.C. 187, 258 B.C.A.C. 187, 46 C.B.R. (5th) 7, [2008] 10 W.W.R. 575 (B.C. C.A.) — considered

First Leaside Wealth Management Inc., Re (2012), 2012 CarswellOnt 2559, 2012 ONSC 1299 (Ont. S.C.J. [Commercial List]) — referred to

Lehndorff General Partner Ltd., Re (1993), 17 C.B.R. (3d) 24, 9 B.L.R. (2d) 275, 1993 CarswellOnt 183 (Ont. Gen. Div. [Commercial List]) — referred to

Nortel Networks Corp., Re (2009), 2009 CarswellOnt 4467, 55 C.B.R. (5th) 229 (Ont. S.C.J. [Commercial List]) — referred to

Octagon Properties Group Ltd., Re (2009), 58 C.B.R. (5th) 276, 2009 CarswellAlta 1325, 2009 ABQB 500, 486 A.R. 296 (Alta. Q.B.) — considered

Shire International Real Estate Investments Ltd., Re (2010), 64 C.B.R. (5th) 92, 2010 CarswellAlta 234, 2010 ABQB 84 (Alta. Q.B.) — considered

Ted Leroy Trucking Ltd., Re (2010), (sub nom. *Century Services Inc. v. Canada (A.G.))* [2010] 3 S.C.R. 379, [2010] G.S.T.C. 186, 12 B.C.L.R. (5th) 1, (sub nom. *Century Services Inc. v. A.G. of Canada)* 2011 G.T.C. 2006 (Eng.), (sub nom. *Century Services Inc. v. A.G. of Canada)* 2011 D.T.C. 5006 (Eng.), (sub nom. *Leroy (Ted) Trucking Ltd., Re)* 503 W.A.C. 1, (sub nom. *Leroy (Ted) Trucking Ltd., Re)* 296 B.C.A.C. 1, 2010 SCC 60, 2010 CarswellBC 3419, 2010 CarswellBC 3420, 409 N.R. 201, (sub nom. *Ted LeRoy Trucking Ltd., Re)* 326 D.L.R. (4th) 577, 72 C.B.R. (5th) 170, [2011] 2 W.W.R. 383 (S.C.C.) — considered

Timminco Ltd., Re (2012), 2012 ONSC 506, 95 C.C.P.B. 48, 2012 CarswellOnt 1263, 85 C.B.R. (5th) 169 (Ont. S.C.J. [Commercial List]) — referred to

Timminco Ltd., Re (2012), 2012 CarswellOnt 9633, 2012 ONCA 552 (Ont. C.A.) — referred to

Statutes considered:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

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

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — referred to

s. 11.02 [en. 2005, c. 47, s. 128] — referred to

APPLICATION by debtors for protection under *Companies Creditors Arrangement Act.*

***C. Campbell J.*:**

1 The applicants seeking an Initial Order under the *Companies Creditors Arrangement Act* are a group of companies owned and controlled by or through the main holding company Dondeb Inc. The proposed relief would include a stay of proceedings in respect of the various companies which own and or operate businesses and real property in Ontario.

2 The application is vigorously opposed by numerous secured creditors which have mortgage or other security on property beneficially owned by one or more of the companies in the Dondeb "group".

3 The applicants seek the protection of the *CCAA* to enable an orderly liquidation of the assets and property of the various companies to enable what is asserted to be the remaining equity after sale and expenses to accrue to the benefit of the Dondeb Group.

4 It is urged that the flexible mechanism of the *CCAA* is appropriate as there are common expenses across some of the companies', common security across others and that any order in liquidation would prevent the incurrence of added cost should individual properties and companies placed in liquidation with the loss of remaining equity.

5 The applications propose a Debtor in Possession (DIP) financing and administrative charge to secure the fees of professionals and expenses associated with *CCAA* administration. The application is opposed by approximately 75% in value of the secured creditors.

6 The basis of the opposition can be summarized as follows:

i) That in many instances the properties over which security is held is sufficiently discrete with specific remedies including sale being more appropriate than the "enterprise" approach posed by the applicants.

ii) That the proposed DIP/financial and administration changes are an unwarranted burden to the equity of specific properties are evidence of the inappropriate application of the *CCAA*.

iii) That in the circumstances individual receivership orders for many of the properties is a more appropriate

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

remedy where the creditors and not the debtor would have control of the process.

iv) That the creditors have lost confidence in the Dondeb family owners of the Dondeb group for a variety of reasons including for breach of promise and representation.

v) That it is now evident that the applicants will be unable to propose a realistic plan that is capable of being accepted by creditors given a difference in position with respect to value of various properties.

7 Those who support the applicants in the main wish to see those businesses that are operating on some of the properties such as in one instance, a school, and others like retirement homes continue in a way that may not be possible in a bankruptcy.

8 During the course of the submissions on the first return date an alternative was proposed by a number of secured creditors, namely a joint or consolidated receivership of the various entities to maximizing creditor control of the process and ensure that costs of administration be allocated to each individual property and company.

9 The application was adjourned to be returnable October 15, 2012 to allow both the applicants and the opposing creditors to consider their positions hopefully achieve some compromise. In the meantime 4 notices of intention under the BIA were stayed.

10 The return of the application on October 15, 2012 did produce some modification of position on both sides but not sufficient to permit a *CCAA* order to be agreed to.

11 The applicants revised the proposed form of Initial Order to allow for segregation of accounts on the individual properties an entitlement.

12 The rationale of the applicants for the original Initial Order sought was that if liquidated or otherwise operated in an orderly way by the debtor and a "super" monitor, greater value could be achieved than the secured debt owing in respect to at least a number of the properties which could be available (a) to other creditors in respect of which guarantees or multiple property security could enhance recovery and or (b) the equity holders.

13 The second major reason advanced by a significant number of creditors appearing through counsel was that they no longer had any confidence in Mr. Dandy, the principal of Dondeb Inc. Significant examples of alleged misleading supported the positions taken.

14 I accept the general propositions of law advanced on behalf of the applicants that pursuant to s.11.02 of the *CCAA* the court has wide discretion "on any terms it may impose" to make an Initial Order provided the stay does not exceed 30 days [see *Nortel Networks Corp., Re* [2009 CarswellOnt 4467 (Ont. S.C.J. [Commercial List])], 2009, CanLII 39492 at para 35 and *Lehndorff General Partner Ltd., Re* (1993), 17 C.B.R. (3d) 24 (Ont. Gen. Div. [Commercial List]) CF 33.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

15 The more recent decision of the Supreme Court of Canada in *Ted Leroy Trucking Ltd., Re*, 2010 SCC 60 (S.C.C.) at para 15 confirms the breadth and flexibility of the CCAA to not only preserve and allow for restructuring of the business as a going concern but also to permit a sale process or orderly liquidation to achieve maximum value and achieve the highest price for the benefit of all stakeholders. See also *Timminco Ltd., Re*, 2012 ONSC 506 (Ont. S.C.J. [Commercial List]) at para 49-50 (leave to appeal denied 2012 ONCA 552 (Ont. C.A.)).

16 I also accept the general proposition that given the flexibility inherent in the *CCAA* process and the discretion available that that an Initial Order may be made in the situation of "enterprise" insolvency where as a result of a liquidation crisis not all of the individual entities comprising the "enterprise" may be themselves insolvent but a number are and to propose of the restructuring is to restore financial health or maximize benefit to all stakeholders by permitting further financing. Such process can include liquidation. See *First Leaside Wealth Management Inc., Re*, 2012 ONSC 1299 (Ont. S.C.J. [Commercial List]) and also *Edgeworth Properties Inc. (Re)* CV-11-9409-CL [Commercial List].

17 I also accept that while each situation must be looked at on its individual facts the court should not easily conclude that a plan is likely to fail. See *Azure Dynamics Corp., Re*, 2012 BCSC 781 (B.C. S.C. [In Chambers]) at paras 7-10.

18 In *Cliffs Over Maple Bay Investments Ltd. v. Fisgard Capital Corp.*, 2008 CarswellBC 1758 (B.C. C.A.), the British Columbia Court of Appeal overturned the decision of the chambers' judge extending a stay of proceedings and authorizing DIP financing under the *CCAA* in the case of a debtor company in the business of land development because:

> Although the *CCAA* can apply to companies whose sole business is a single land development as long as the requirements set out in the *CCAA* are met, it may be that, in view of the nature of its business and financing arrangements, such companies would have difficulty proposing an arrangement or compromise that was more advantageous than the remedies available to its creditors. The priorities of the security against the land development are often straightforward, and there may be little incentive for the creditors having senior priority to agree to an arrangement or compromise that involves money being paid to more junior creditors before the senior creditors are paid in full. If the developer is insolvent and not able to complete the development without further funding, the secured creditors may feel that they will be in a better position by exerting their remedies rather than by letting the developer remain in control of the failed development while attempting to rescue it by means of obtaining refinancing, capital injection by a new partner or DIP financing.

19 Similarly, in *Octagon Properties Group Ltd., Re*, 2009 CarswellAlta 1325 (Alta. Q.B.) paragraph 17, Kent, J. made the following comments:

> This is not a case where it is appropriate to grant relief under the CCAA. First, I accept the position of the majority of first mortgagees who say that it is highly unlikely that any compromise or arrangement proposed by Octagon would be acceptable to them. That position makes sense given the fact that if they are permitted to proceed with foreclosure procedures and taking into account the current estimates of value, for most mortgagees on most of their properties they will emerge reasonably unscathed. There is no incentive for them to agree to a compromise. On the other hand if I granted CCAA relief, it would be these same mortgagees who would be paying the cost to permit Octagon to buy some time. Second, there is no other reason for CCAA relief such as the existence of a large number of employees or significant unsecured debt in relation to the secured debt. I balance those reasons against the fact that even if the first mortgagees commence or continue in their foreclosure proceedings that process is also supervised by the court and to the extent that Octagon has reasonable arguments to obtain relief under the foreclosure process, it will likely obtain that relief.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

20 A similar result occurred in *Shire International Real Estate Investments Ltd., Re*, 2010 CarswellAlta 234 (Alta. Q.B.) even after an initial order had been granted.

21 In Edgeworth, dealing with the specifics of that case I noted:

> Were it not for the numerous individual investors (UDIs, MICs) and others who claim to have any interest in various of the lands as opposed to being general creditors of the Edgeworth companies, I doubt I could have been persuaded to grant the Initial CCAA Order.

22 At the conclusion of oral submissions which followed on a hearing of the application which commenced on Friday October 11, 2012 continued on October 15 with additional written material and concluded on Wednesday October 17, 2012 again with additional written material and oral submissions the following conclusions were reached.

(i) The application for an Initial Order under the CCAA based on the material filed be dismissed.

(ii) The issue of costs incurred by the proposed Monitor Farber and of counsel to the debtor be reserved for further consideration (if not resolved) basis on material to be provided to counsel for the creditors and their submissions.

(iii) The request for a more limited *CCAA* Initial Order which like the Original Application is opposed by a significant body of creditors is also rejected.

(iv) A Global Receivership Order which is supported by most of the creditors appearing to oppose the application and which has the support of Farber which will become Receiver of those companies and properties covered by the application will issue in a format to be approved by counsel and the court.

23 For ease of administration the Global Receivership Order will issue in Court File No. CV-12-9794-CL and make reference to the various companies and properties to be covered by the Order.

24 In order to further facilitate administration the following proceedings, each being Notices of Intention to make a proposal

Dondeb Inc.	31-1664344
Ace Sel/Storage & Business Centre	31-1664774
1711060 Ontario Ltd.	31-1664775
2338067 Ontario Ltd.	31-1664772
King City Holdings Ltd.	31-1671612
1182689 Ontario Inc.	31-1671611
2198392 Ontario Inc.	31-1673260

hereby stayed and suspended pending further order of the court.

25 The request for an Initial Order under the *CCAA* was dismissed for the simple reason that I was not satisfied that a successful plan could be developed that would receive approval in any meaningful fashion from the creditors. To a large

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

extent, Mr. Dandy is the author of his own misfortune not just for the liquidity crisis in the first place but also for a failure to engage with creditors as a whole at an early date.

26 In his last affidavit filed Mr. Dandy explained why certain properties were transferred into individual corporations to allow additional financing that would permit the new creditors access to those properties in the event of default. To a certain extent this was perceived by creditors as "robbing Peter to pay Paul" and led to the distrust and lack of confidence the vast majority of creditors exhibit. Had there been full and timely communication both the creditors and the court may have concluded that a *CCAA* plan could be developed.

27 Under the proposed Initial Order the fees of the proposed monitor and of counsel to the debtor were an issue as well as leaving the debtor in possession with the cost that would entail.

28 Counsel for each of the various creditors represented urged that their client's individual property should not be burdened with administrative expenses and professional fees not associated with that property.

29 Counsel for the debtor advised that to the extent possible his client and the monitor would keep individual accounts. This proposal did not appease the opposing creditors who did agree that their clients could accept what was described as a "global" receiver and that the Farber firm would be acceptable as long as the receiver's charge was allocated on an individual property basis. In other words, the opposing creditors are prepared to accept the work of the professionals of the receiver but not fund the debtor or its counsel.

30 The issue of the fees of Farber incurred todate in respect of preparation of the *CCAA* application was agreed between the opposing creditors, Farber and its counsel and are not an issue. Counsel for the debtor requested that the court consider a request for fees and costs on the part of the debtor. In order to give an opportunity for the parties to consider the details of such request and possible resolution the issue was deferred to a later date.

31 Following further submissions on behalf of the debtor I advised the parties that in my view the conditions necessary for approval of an Initial *CCAA* Order were not met but that a comprehensive Receivership Order should achieve an orderly liquidation of most of the properties and protect the revenue from the operating properties with the hope of potential of some recovery of the debtor's equity.

32 Counsel are to be commended for the effort and success in reaching agreement on the form of order acceptable to the court.

33 The *CCAA* is a flexible instrument, which with judicial discretion, is capable of permitting restructuring, including in appropriate situations, liquidation.

34 In my view the use of the *CCAA* for the purpose of liquidation must be used with caution when liquidation is the end goal, particularly when there are alternatives such as an overall less costly receivership that can accomplish the same overall

WestlawNext® CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

goal.

Schedule "A"

1. Dondeb Inc.

2. Ace Self Storage and Business Centre Inc.

3. 1182689 Ontario Inc.

4. King City Holdings Inc.

5. 1267818 Ontario Ltd.

6. 1281515 Ontario Inc.

7. 1711060 Ontario Ltd.

8. 2009031 Ontario Inc.

9. 2198392 Ontario Ltd.

10. 2338067 Ontario Inc.

11. Briarbrook Apartments Inc.

12. Guelph Financial Corporation

Application dismissed.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 7

2012 ONSC 4693
Ontario Superior Court of Justice [Commercial List]

Romspen Investment Corp. v. Edgeworth Properties

2012 CarswellOnt 10902, 2012 ONSC 4693, 222 A.C.W.S. (3d) 854

Romspen Investment Corporation, Applicant and Edgeworth Properties - Derrick View Estates Inc., 1253122 Alberta Ltd., Edgeworth Properties - Heartland Ridge Inc., Edgeworth Properties - Southpoint Landing Inc., Edgeworth Place at Spruce Ridge Drive Inc., Edgeworth Properties — Creekside Estates Inc., Edgeworth Place at Heartland Inc., Edgeworth Properties — Wolf Creek Estates Inc., Edgeworth Estates at Manning Drive Phase I Inc., Edgeworth Properties — Ellerslie Ridge Inc., 1519560 Alberta Ltd., Derrick View Estates Phase II Inc., 1330433 Alberta Ltd., Respondents

C. Campbell J.

Heard: July 31 - August 3, 2012
Judgment: August 15, 2012
Docket: CV-11-9452 CL

Counsel: David P. Preger, Lisa S. Corne, for Plaintiff, Romspen Investment Corporation
R. Shayne Kukulowicz, Kate Stigler, for Defendants, Edgeworth Properties Inc. et al.
Katherine McEachern, for Monitor
Craig A. Mills, Terrence Warner, Lesley Akst, for Receiver
Ken Lenz, for Edgeworth Mortgage Investment Corporation, Edgeworth Mortgage Investment II Corporation, Biggs Avenue Mortgage Investment Corporation and the preferred shareholders of same
John Salmas, for Canada Mortgage and Housing Corporation

Subject: Property; Corporate and Commercial; Insolvency; Securities

Headnote

Real property --- Mortgages — Priorities — Between types of creditors — Registered and unregistered or equitable mortgagee

Table of Authorities

Cases considered by *C. Campbell J.*:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Dominion Stores Ltd. v. United Trust Co. (1976), 1 R.P.R. 1, 11 N.R. 97, [1977] 2 S.C.R. 915, 71 D.L.R. (3d) 72, 1976 CarswellOnt 383, 1976 CarswellOnt 404 (S.C.C.) — considered

Holt Renfrew & Co. v. Henry Singer Ltd. (1982), 1982 CarswellAlta 92, 20 Alta. L.R. (2d) 97, 135 D.L.R. (3d) 391, 37 A.R. 90, [1982] 4 W.W.R. 481 (Alta. C.A.) — considered

RJC New Brunswick Inc. v. 1301725 Alberta Ltd. (2012), 2012 CarswellAlta 547, 2012 ABQB 213 (Alta. Master) — considered

Statutes considered:

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

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — referred to

Land Titles Act, R.S.A. 2000, c. L-4
Generally — referred to

s. 161(a) — considered

s. 203 — considered

APPLICATION by mortgagee for declaration of priority and for orders that receiver distribute proceeds of sale to it and permitting it to proceed with judicial sale or foreclosure.

***C. Campbell J.*:**

1 Romspen Investment Corporation ("Romspen") claims as the first secured mortgage creditor of the Respondents and seeks on this motion a declaration of the validity of its security over the real property and related personal property of the Respondents and an order as against Edgeworth (in CCAA) and other claimant creditors for the listing and sale of various remaining receivership properties.

2 The relief sought is opposed on behalf of the many holders of undivided interest investors (the "UDI Investors") and various lot purchasers (the "Lot Purchasers") in many of the properties over which Romspen claims for security. The UDI Investors also oppose the distribution proposed by the Receiver to Romspen of funds from the sale of properties previously authorized by orders of this Court.

3 As the UDI Investors and the Lot Purchasers were not represented by counsel at this time, the Court requested the Receiver of Edgeworth to undertake an investigation of the claims of the UDI Investors and Lot Purchasers and obtain a report from Alberta counsel to the Receiver with respect to the priority claim of Romspen.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

4 The Romspen relief is also opposed on behalf of mortgage corporation investors (MIC) in respect of receivership properties over which they claim priority of security interest.

5 The Court having heard the Romspen position delayed rendering a decision to enable representatives on behalf of UDIs and Lot Purchasers to make further submissions. Written submissions were received from Mr. Clinton Thierman who also made oral submissions as did Mr. Wei Cheng Tan and Mr. Edwin Neo. Mr. Murray Wotherspoon made oral comments.

6 Having heard submissions on behalf of all parties and for the reasons below, I am satisfied that Romspen is entitled to the relief sought and the Order with the amendments agreed on by counsel discussed in the telephone conference call of August 3 should issue.

7 Romspen seeks an order:

a) declaring that it holds valid, enforceable, first, and in certain cases second, ranking security against the real properties and related personal property owned by the Edgeworth Respondents, subject only to certain charges created by the Receivership Order, the *Bankruptcy and Insolvency Act*, and liens for unpaid municipal realty taxes collectively;

b) directing MNP Ltd. in its capacity as Court-appointed receiver to distribute to Romspen from the net sale proceeds realized from the Properties sold by the Receiver, all amounts required to repay the indebtedness of the Respondents to Romspen; and

c) permitting Romspen to proceed with judicial sale/foreclosure proceedings in Alberta in respect of the remaining Receivership Properties (other than the property owned by Edgeworth Place at Spruce Ridge Drive Inc.).

8 Romspen advanced funds to the Respondents pursuant to a Commitment Letter dated September 27, 2010, as amended by Supplement No. 1 dated October 7, 2010. Of the funds advanced by Romspen, $9.7 million was used by the Respondents to refinance and replace preexisting mortgages registered against Spruce Ridge, $1.34 million was used to refinance and replace a pre-existing mortgage on a property known as Half Moon Lake and $5.5 million was used to purchase the Blackfalds property.

9 Romspen's advances to the Respondents are secured by a mortgage and supplemental mortgage registered against title to all of the Properties, and a security interest in all of the Respondents' personal property.

10 In addition, Romspen acquired an assignment of certain loans and security held by Liberty Mortgage Services Ltd., Sterling Bridge Mortgage Corp. and Hurlburt Farms Ltd., each of which rank in priority to Romspen's blanket mortgage.

11 Based on the material before the court, I accept the analysis by Romspen that all of the existing interests and encumbrances registered against the Receivership Properties and in particular as set out in the table in the material where the interests of Rompsen, the MIC investors, the UDI investors and the Lot Purchasers rank in terms of priority i set out.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

12 There are seven properties in which postponements were given by Edgeworth Mortgage Investment Corporation to Romspen's $23.5 million blanket mortgage. In respect of each of those seven Properties, Romspen's $23.5 million blanket mortgage is either in first or second position (behind one of the assigned mortgages noted above). In respect of three of the seven properties, the first-ranking mortgage which has now been assigned to Romspen was registered before the MIC mortgage was registered. Therefore, Romspen as assignee of the first ranking mortgages, ranks in priority to the MICs with respect to those three properties regardless of whether the postponements granted by the MICs are valid. Moreover, there are four Properties which are subject to a mortgage held by Edgeworth Mortgage Investment II Corporation or Biggs Avenue Corporation. However, in each case where there is a mortgage held by Edgeworth Mortgage Investment II Corporation, or Biggs Avenue Corporation, Romspen's $23.5 million blanket mortgage was registered before Edgeworth Mortgage Investment II Corporation's charge, and before Biggs Avenue Corporation's charge.

13 In response to the Edgeworth Group's application for relief pursuant to the *CCAA*, Romspen sought leave to commence foreclosure proceedings in respect of the Properties. In light of objections raised by the Respondents and certain other stakeholders, and a proposal for a compromise which would avoid seeing Romspen ensnared in a costly, full-blown *CCAA* proceeding, Romspen sought the appointment of the Receiver, as an alternative to foreclosure, provided that it was on terms which treated all mortgagees equally.

14 Although all mortgagees were initially treated equally under the Appointment Order, that changed with the Order dated December 12, 2011 lifting the stay of proceedings to permit Firm Capital Mortgage Funds Inc. to proceed with judicial sale/foreclosure proceedings to be supervised by this Court.

15 When Romspen proffered the receivership option, the Edgeworth group and its chief restructuring officer were optimistic that they would be in a position to seek approval of a sale of the Properties within 60 to 90 days which would generate sufficient proceeds to repay the third party mortgagees, including Romspen, in full. Unfortunately, that has not happened.

16 Romspen now wishes to realize upon the Judicial Sale Properties, without the associated costs of the Receiver. The expenses associated with the within the receivership are significant. For example, where a Receiver's sale of a property has been approved by the Court in Ontario, an associated recognition motion in Alberta has been necessary. The costs associated with the receivership could may well represent the difference between a partial recovery for MIC and UDI investors and lot purchasers (or some of them) and a shortfall for Romspen. In the circumstances, I conclude, there is no benefit to be gained by incurring further professional costs associated with the receivership which will only reduce potential recoveries for all of the stakeholders, including the MICs, UDIs and lot purchasers.

17 The position of the UDI investors is well set out in the written submissions by Mr. Thierman which in essence comes down to a statement of the UDI contractual position against Edgeworth which is urged was one of trust given the promise of registration of their interest which is urged should be binding on the Romspen given imputed or actual knowledge of the UDI interests.

18 Mr. Thierman in an impassioned written submission urges rejection of the Romspen position in summary as follows:

a) that UDI investors are innocent victims of the breaches of trust and contract by Edgeworth and its officers;

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

b) since the UDI investors were entitled to property by their investment, Edgeworth could not issue the postponements to Romspen as it did not have the legal capacity to do so.

c) Romspen must have known that Edgeworth did not have the power to grant a mortgage in favour of Romspen and should not be entitled to priority.

19 Alberta Counsel to the Receiver provided 2 opinions. The first dated July 20, 2012 and the second dated July 27, 2012 to address additional queries from various stakeholders.

20 In the opinion of Alberta Counsel to the Receiver, based on the clear wording of s. 203 of the Land Titles Act Alberta which is amply supported by case law, absent fraud considerations, a mortgagee even with actual knowledge of a prior unregistered interest will acquire title without any impact of the unregistered interest.

21 Section 203 of the *Act* provides as follows:

203(1) In this section,

(a) "interest" includes any estate or interest in land;

(b) "owner" means

(i) the owner of an interest in whose name a certificate of title has been granted,

(ii) the owner of any other registered interest in whose name the interest is registered, or

(iii) the caveator or transferee of a caveat in whose name the caveat is registered.

(2) A person contracting or dealing with or taking or proposing to take a transfer, mortgage, encumbrance, lease or other interest from an owner is not, except in the case of fraud by that person,

(a) bound or concerned, for the purpose of obtaining priority over a trust or other interest that is not registered by instrument or caveat, to inquire into or ascertain the circumstances in or the consideration for which the owner or any previous owner of the interest acquired the interest or to see to the application of the purchase money or any part of the money, or

(b) affected by any notice, direct, implied or constructive, of any trust or other interest in the land that is not registered by instrument or caveat, any rule of law or equity to the contrary notwithstanding.

(3) The knowledge of the person that any trust or interest that is not registered by instrument or caveat is in existence shall not of itself be imputed as fraud.

(4) This section is deemed to have been in force since the commencement of *The Land Titles Act*, SA 1906 c24, in place of section 135 of that Act and similar sections in successor Acts.

22 The Receiver's Alberta Counsel, Mr. Warner, adds the following:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> The question is whether there is present an additional element of dishonesty that the cases refer to such that the mortgage of Romspen should be subordinated to the UDI and Lot Purchaser interests. Simply having knowledge of the terms and conditions of the UDI and Lot Purchase agreements, and knowledge that taking the mortgage would defeat those interests, does not, by itself elevate the transaction to the level of fraud. Edgeworth *may* have acted in breach of the UDI and Lot Purchaser agreements, but we are not prepared to assume that Edgeworth fraudulently and do not do so in the context of this supplemental opinion; that is simply not for us to determine. However, even if Edgeworth did act fraudulently based upon its agreements with the UDI and Lot Purchaser holders, which we are not either suggesting or assuming, that would not lead to the conclusion that Romspen either acted fraudulently, or that its mortgage should be tainted by that alleged fraud. Absent evidence of collusion with intent to defeat the interests of the UDI and Lot Purchaser interests, we stand by our opinion that Romspen has priority.

23 Section 203 of the *Act* represents an unequivocal abrogation of the doctrine of actual notice in Alberta such that, absent fraud, an unregistered interest cannot under any circumstances trump a registered interest. This absolute rule, codified in section 203 of the *Act*, was recognized by the Supreme Court of Canada in *Dominion Stores Ltd. v. United Trust Co.*, 1976 CarswellOnt 383 (S.C.C.), in paragraph 75, where Spence J., on behalf of the majority, remarked as follows:

> ***There is no doubt that when such a term appears*** in the governing ***statute, the result is that unregistered encumbrances fail in any way to affect the title of the purchaser for value.***
>
> [emphasis added]

24 Further, in *Holt Renfrew & Co. v. Henry Singer Ltd.*, 1982 CarswellAlta 92 (Alta. C.A.), the Alberta Court of Appeal noted that the *Act* expressly provides that "knowledge of the existence of an unregistered interest shall not of itself be imputed as fraud". The Court in *Holt Renfrew & Co. v. Henry Singer Ltd.* explained that there must be some additional element or dishonesty of some sort on the part of a mortgagee, in addition to knowledge of an unregistered interest, in order to defeat or subordinate a registered charge. Knowledge that a proposed charge or transfer will defeat an unregistered interest is not sufficient to subordinate a registered transfer or mortgage.

25 In *RIC New Brunswick Inc. v. 1301725 Alberta Ltd.*, 2012 ABQB 213 (Alta. Master), the court followed the interpretation of section 203 of the *Act* set out in *Holt Renfrew*, and upheld a mortgage over lands notwithstanding the mortgagee's knowledge of an unregistered agreement by the mortgagor to convey a portion of the lands to a third party after that portion of the lands had been subdivided. Although the mortgagee had knowledge of that agreement, there was no instrument registered on title to protect the third party at the time the mortgage was granted and the funds were advanced. The mortgagee was not a party to the agreement between the mortgagor and the third party, had not been party to any misrepresentations or discussions with the third party, or agreed to discharge its mortgage over the portion of the lands to be conveyed after subdivision. Accordingly, as there was no evidence of any bad faith or any element of *mala fides* or dishonesty on the part of the mortgagee, it was entitled to rely upon the certainty of title and the protection afforded to mortgagees by the *Act*.

26 The assertion on behalf of the UDI investors is that Edgeworth breached a contractual or trust relationship and that Romspen should not be able to take advantage of that failure even though Romspen advanced some $15 million by way of its mortgage and other first mortgages on some properties it assumed.

27 There is no evidence before the court to suggest that Romspen itself committed a fraud and in the absence of that finding, Romspen is entitled to have its priority confirmed. I accept the opinion of Alberta counsel for the Receiver that there

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

are no facts before the court that would support an argument for Equitable Subordination of the Romspen debt even assuming the concept were to apply.

28 A further submission was made on the behalf of UDI investors by Mr. Wei Cheng Tan to the effect that Romspen should be required to first be repaid from properties that are not subject to UDI interests. A mortgage creditor such as Romspen is entitled to recover against any property over which it has priority of security.

29 There is no basis in Alberta land law to limit the Romspen recovery in the way the UDI investors propose.

The MICs

30 The MIC Investors Committee opposes the declaration of validity of the postponements granted to Romspen by the corporations referred to as MICs.

31 It is the position of the MICs that these corporations raised some $57 million from investors on the basis that those investors would receive first or second priority security on specific properties covered by the mortgages granted in favour of the MICs.

32 The issue on this motion is whether the postponements granted by one of the MICs, [EMIC. 1] to Romspen are valid and enforceable

33 The position put forward by Mr. Lenz on behalf of the MICs is that Romspen is not entitled to rely on the postponements granted by the MICs since the MICs were not parties to either of the commitment letters or either of the mortgages relied on by Romspen.

34 Basically put, it is asserted that the MICs were not parties to the main agreement and there is no evidence of any consideration flowing from the MICs to Romspen since the MICs were not owned by Edgeworth.

35 The MICs position is that there may be a lack of corporate seals in respect of some of the postponements is also relied on as is the assertion of independent shareholders in the MIC's from those of Edgeworth.

36 The response of Romspen to the position of the MIC's is twofold. The first being that the MIC in question had at least one common corporate officer with Edgeworth and their officer signed postponements on behalf of the MIC.

37 The second response of Romspen is reliance on section 161 (a) of the *Alberta Land Titles Act* which reads as follows:

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

"161 An instrument or caveat executed by a corporation notwithstanding anything to the contrary in the Act, statute, constating documents, charter or memorandum and articles of association incorporating the corporation, is for the purposes of this Act deemed to be sufficiently executed if the instrument or caveat is

(a) ***sealed with the corporate seal of the corporation and countersigned by at least one officer or director of the corporation***, ..."

[emphasis added]

38 On the material before the court I am prepared to conclude that the postponements granted by the MICs in favor of Romspen were executed by an authorized officer and there is no evidence to suggest that the were not sealed with the appropriate corporate seals.

Conclusion

39 For the foregoing reasons I conclude that Romspen be entitled to the declaratory relief requested and to the distribution of funds in the hands of the Receiver as set out in the motion record. The form of draft order that was settled on the teleconference call on August 3, 2012 will issue in the form signed.

40 There will be an opportunity for the UDI investors and others to claim against future sums if any that may be recovered once Romspen has been repaid its debt.

Application granted.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 8

2011 ONSC 4223
Ontario Superior Court of Justice [Commercial List]

Tucker v. Aero Inventory (UK) Ltd.

2011 CarswellOnt 8476, 2011 ONSC 4223, [2011] O.J. No. 3816, 206 A.C.W.S. (3d) 466, 338 D.L.R. (4th) 577, 80 C.B.R. (5th) 1

In the Matter of the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as Amended

And In the Matter of James Robert Tucker, Richard Heis and Allan Watson Graham of KPMG LLP, as Joint Administrators (Applicants)

And In the Matter of Aero Inventory (UK) Limited and Aero Inventory PLC (Respondents)

Application under Section 46 and following of the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as Amended

Morawetz J.

Judgment: August 18, 2011
Docket: 09-8456-00CL

Counsel: Orestes Pasparakis, Evan Cobb, Vasuda Sinha for Trustee
Sean F. Dunphy, Alexander D. Rose, Kathryn Esaw for Air Canada
John Porter for Lloyds TSB Commercial Finance Limited

Subject: Insolvency; Estates and Trusts

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy and insolvency --- Avoidance of transactions prior to bankruptcy — Practice and procedure — Who may bring application

Administration proceedings in respect of bankrupt company were commenced in foreign country — Administrators were recognized as foreign representatives under Companies' Creditors Arrangement Act ("CCAA") — Administrators assigned bankrupt into bankruptcy for purpose of pursuing preference action regarding certain transactions with airline — Trustee in bankruptcy brought motion to have such transactions declared void as fraudulent preferences pursuant to s. 95 of Bankruptcy and Insolvency Act ("BIA") — Hearing of threshold issue regarding priority of preferences proceeds was held — Trustee in bankruptcy was only party that could bring preference action in bankruptcy proceedings — Proceeds recovered were brought into estate, but distribution was subject to rights of secured creditors — Section 95 of BIA made it clear transaction declared to be preference was void as against trustee — Trustee had cause of action to

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

declare preference to be void — Proceeds from preferential transaction were returned to estate but subject to rights of secured creditors.

Bankruptcy and insolvency --- Avoidance of transactions prior to bankruptcy — Fraudulent preferences — Miscellaneous

Priority of proceeds from preferences action — Administration proceedings in respect of bankrupt company were commenced in foreign country — Administrators were recognized as foreign representatives under Companies' Creditors Arrangement Act ("CCAA") — Administrators assigned bankrupt into bankruptcy for purpose of pursuing preference action regarding certain transactions with airline — Trustee in bankruptcy brought motion to have such transactions declared void as fraudulent preferences pursuant to s. 95 of Bankruptcy and Insolvency Act ("BIA") — Hearing of threshold issue regarding priority of preferences proceeds was held — Trustee in bankruptcy was only party that could bring preference action in bankruptcy proceedings — Proceeds from preferential transaction were returned to estate, subject to rights of secured creditors — Ability of trustee to recover monies for estate for benefit of creditors was subject to right of secured creditors — To extent that secured party had rights in collateral in hands of third party, such remedy and priority were not altered because trustee brought preference action — Focus was on whether or not secured creditor had rights in collateral at time of suspect transaction — It was premature to determine whether secured party had rights to recover proceeds from this preferences action.

Bankruptcy and insolvency --- Companies' Creditors Arrangement Act — General principles — Application of Act — Relationship between Act and Bankruptcy and Insolvency Act

Administration proceedings in respect of bankrupt company were commenced in foreign country — Administrators were recognized as foreign representatives under Companies' Creditors Arrangement Act ("CCAA") — Administrators assigned bankrupt into bankruptcy for purpose of pursuing preference action regarding certain transactions with airline — Trustee in bankruptcy brought motion to have such transactions declared void as fraudulent preferences pursuant to s. 95 of Bankruptcy and Insolvency Act ("BIA") — Hearing of threshold issue regarding priority of preferences proceeds was held — Trustee in bankruptcy was only party that could bring preference action in bankruptcy proceedings — Proceeds recovered were brought into estate, but distribution was subject to rights of secured creditors — Preference action should proceed under BIA — Section 36.1(1) of CCAA provided preferential provisions in BIA applied in respect of compromise or arrangement — There was no compromise proposed to creditors, nor was any expected to be forthcoming — CCAA could operate in tandem with BIA to return matters to status quo — Procedural order in CCAA proceedings would transition matter to BIA so trustee would not have to start again.

Bankruptcy and insolvency --- Administration of estate — Trustees — Miscellaneous

Duty to comply with obligations under Bankruptcy and Insolvency Act.

Table of Authorities

Cases considered by *Morawetz J.*:

Agricultural Credit Corp. of Saskatchewan v. Featherstone (Trustee of) (1996), 1996 CarswellSask 344, (sub nom. *Agricultural Credit Corp. of Saskatchewan v. Featherstone (Bankrupt))* 145 Sask. R. 161, [1996] 8 W.W.R. 281, 11 P.P.S.A.C. (2d) 194, 45 C.B.R. (3d) 113 (Sask. Q.B.) — considered

Anderson, Re (1911), [1911] 1 K.B. 896 (Eng. K.B.) — referred to

Anron Mechanical Ltd. v. L'Abbé Construction (Ontario) Ltd. (Trustee of) (1991), 5 C.B.R. (3d) 133, 46 C.L.R. 49, 1991 CarswellOnt 181 (Ont. Gen. Div.) — considered

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

ASI Acoustical Supplies Inc., Re (2000), 22 C.B.R. (4th) 174, 2000 CarswellBC 2585, 2000 BCSC 1838 (B.C. S.C.) — considered

Bayley v. National Australia Bank Ltd. (1995), 16 A.C.S.R. 38, [1995] TASSC 13, 4 Tas. R. 226 (Tasmania S.C.) — considered

Beeston, Re (1899), [1899] 1 Q.B. 626 (Eng. C.A.) — referred to

Beetown Honey Products Inc., Re (2003), 2003 CarswellOnt 3755, 46 C.B.R. (4th) 195, 67 O.R. (3d) 511 (Ont. S.C.J.) — referred to

Beetown Honey Products Inc., Re (2004), 3 C.B.R. (5th) 204, 2004 CarswellOnt 4316 (Ont. C.A.) — referred to

Bibra Lake Holdings Pty. Ltd. v. Firmadoor Australia Pty. Ltd. (1992), 7 A.C.S.R. 380 (Western Australia S.C.) — considered

Canadian Imperial Bank of Commerce v. Canotek Development Corp. (1997), 35 O.R. (3d) 247, 48 C.B.R. (3d) 161, 103 O.A.C. 302, 1997 CarswellOnt 3216, 152 D.L.R. (4th) 261, 13 R.P.R. (3d) 187 (Ont. C.A.) — followed

Cooper, Re (1875), (1874-75) L.R. 10 Ch. App. 510 (Eng. Ch. App.) — considered

Fresjac Pty. Ltd. v. Michael Mount PPB (1995), [1995] SASC 5378, 65 S.A.S.R. 334 (South Australia S.C.) — considered

Giffen, Re (1998), 45 B.C.L.R. (3d) 1, 1998 CarswellBC 147, 1998 CarswellBC 148, [1998] 1 S.C.R. 91, (sub nom. *Giffen (Bankrupt), Re)* 101 B.C.A.C. 161, (sub nom. *Giffen (Bankrupt), Re)* 164 W.A.C. 161, 155 D.L.R. (4th) 332, 222 N.R. 29, 1 C.B.R. (4th) 115, [1998] 7 W.W.R. 1, 13 P.P.S.A.C. (2d) 255 (S.C.C.) — referred to

Homburg v. S-Marque Inc. (1999), 1999 CarswellNS 73, (sub nom. *S-Marque Inc. v. Homburg Industries Ltd.)* 176 N.S.R. (2d) 218, (sub nom. *S-Marque Inc. v. Homburg Industries Ltd.)* 538 A.P.R. 218 (N.S. C.A.) — referred to

Hudson v. Benallack (1975), [1975] 6 W.W.R. 109, 7 N.R. 119, 59 D.L.R. (3d) 1, 1975 CarswellAlta 157, 1975 CarswellAlta 139, [1976] 2 S.C.R. 168, 21 C.B.R. (N.S.) 111 (S.C.C.) — considered

Innovation Credit Union v. Bank of Montreal (2010), 500 W.A.C. 1, (sub nom. *Bank of Montreal v. Innovation Credit Union)* [2010] 3 S.C.R. 3, 362 Sask. R. 1, 2010 SCC 47, 2010 CarswellSask 723, 2010 CarswellSask 724, 72 C.B.R. (5th) 23, 407 N.R. 294, 325 D.L.R. (4th) 605, 17 P.P.S.A.C. (3d) 1, [2011] 2 W.W.R. 581 (S.C.C.) — considered

Johnson v. Smiley (1853), 51 E.R. 1019, 17 Beav. 223 (Eng. Ch.) — referred to

Lefebvre, Re (2004), (sub nom. *Lefebvre (Bankrupt), Re)* 326 N.R. 253 (Eng.), (sub nom. *Lefebvre (Bankrupt), Re)* 326 N.R. 353 (Fr.), 2004 SCC 63, 2004 CarswellQue 2831, 2004 CarswellQue 2832, (sub nom. *Lefebvre (Trustee of), Re)* 244 D.L.R. (4th) 513, (sub nom. *Lefebvre (Trustee of), Re)* [2004] 3 S.C.R. 326, 7 C.B.R. (5th) 243, 1 B.L.R. (4th) 19 (S.C.C.) — referred to

Mapleback Ex p. Caldecott, Re (1876), (1876-77) L.R. 4 Ch. D. 150 (Eng. C.A.) — referred to

Maybank Foods Inc., Re (1990), 72 O.R. (2d) 93, 78 C.B.R. (N.S.) 79, 1990 CarswellOnt 167 (Ont. S.C.) — considered

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

MC Bacon Ltd. (No.2), Re (1990), [1991] Ch. 127, [1990] 3 W.L.R. 646 (Eng. Ch. Div.) — followed

Mohawk Sports Equipment Ltd. (No. 2), Re (1972), 17 C.B.R. (N.S.) 115, 1972 CarswellOnt 72 (Ont. S.C.) — considered

N.A. Kratzmann Pty. Ltd. v. Tucker (No. 2) (1968), 123 C.L.R. 295 (Australia H.C.) — considered

N.W. Robbie & Co. v. Witney Warehouse Co. (1963), [1963] 3 All E.R. 613, [1963] 1 W.L.R. 1324 (Eng. C.A.) — referred to

Oasis Merchandising Services Ltd., Re (1996), [1997] 2 W.L.R. 764, [1997] 1 All E.R. 1009, [1998] Ch. 170 (Eng. C.A.) — considered

Pratchler Agro Services Inc. (Trustee of) v. Cargill Ltd. (1999), 11 C.B.R. (4th) 104, 1999 CarswellSask 295 (Sask. Q.B.) — referred to

Ramgotra (Trustee of) v. North American Life Assurance Co. (1996), 1996 CarswellSask 212F, 1996 CarswellSask 418, [1996] 3 W.W.R. 457, 37 C.B.R. (3d) 141, 10 C.C.P.B. 113, 13 E.T.R. (2d) 1, [1996] 1 C.T.C. 356, (sub nom. *Ramgotra (Bankrupt), Re)* 193 N.R. 186, (sub nom. *Ramgotra (Bankrupt), Re)* 141 Sask. R. 81, (sub nom. *Ramgotra (Bankrupt), Re)* 114 W.A.C. 81, (sub nom. *Royal Bank v. North American Life Assurance Co.)* 132 D.L.R. (4th) 193, (sub nom. *Royal Bank v. North American Life Assurance Co.)* [1996] 1 S.C.R. 325, (sub nom. *Royal Bank v. North American Life Assurance Co.)* 96 D.T.C. 6157 (S.C.C.) — considered

Royal Bank v. Sparrow Electric Corp. (1997), 193 A.R. 321, 135 W.A.C. 321, [1997] 2 W.W.R. 457, 208 N.R. 161, 12 P.P.S.A.C. (2d) 68, 1997 CarswellAlta 112, 1997 CarswellAlta 113, 46 Alta. L.R. (3d) 87, (sub nom. *R. v. Royal Bank)* 97 D.T.C. 5089, 143 D.L.R. (4th) 385, 44 C.B.R. (3d) 1, [1997] 1 S.C.R. 411 (S.C.C.) — considered

S-Marque Inc. v. Homburg Industries Ltd. (September 2, 1998), Doc. 113589, 113762, 116298 (N.S. S.C.) — considered

Shapland Inc., Re (1998), [2000] B.C.C. 106 (Eng. Ch. Div.) — considered

St. Anne-Nackawic Pulp Co. (Trustee of) v. Logistec Stevedoring (Atlantic) Inc. (2005), 9 B.L.R. (4th) 1, 2005 NBCA 55, 2005 CarswellNB 285, 2005 CarswellNB 286, 255 D.L.R. (4th) 137, (sub nom. *St. Anne-Nackawic Pulp Co. (Bankrupt), Re)* 286 N.B.R. (2d) 95, (sub nom. *St. Anne-Nackawic Pulp Co. (Bankrupt), Re)* 748 A.P.R. 95, 13 C.B.R. (5th) 125 (N.B. C.A.) — considered

Ted Leroy Trucking Ltd., Re (2010), (sub nom. *Century Services Inc. v. Canada (A.G.))* [2010] 3 S.C.R. 379, [2010] G.S.T.C. 186, 12 B.C.L.R. (5th) 1, (sub nom. *Century Services Inc. v. A.G. of Canada)* 2011 G.T.C. 2006 (Eng.), (sub nom. *Century Services Inc. v. A.G. of Canada)* 2011 D.T.C. 5006 (Eng.), (sub nom. *Leroy (Ted) Trucking Ltd., Re)* 503 W.A.C. 1, (sub nom. *Leroy (Ted) Trucking Ltd., Re)* 296 B.C.A.C. 1, 2010 SCC 60, 2010 CarswellBC 3419, 2010 CarswellBC 3420, 409 N.R. 201, (sub nom. *Ted LeRoy Trucking Ltd., Re)* 326 D.L.R. (4th) 577, 72 C.B.R. (5th) 170, [2011] 2 W.W.R. 383 (S.C.C.) — followed

Tolcher v. National Australia Bank Ltd. (2003), [2003] NSWSC 207, 44 A.C.S.R. 727 (New South Wales S.C.) — considered

Tucker v. Aero Inventory (UK) Ltd. (2010), 2010 CarswellOnt 1094, 2010 ONSC 1196, 65 C.B.R. (5th) 314 (Ont. S.C.J. [Commercial List]) — considered

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Warran Whillans Enterprises Inc. (Trustee of) v. Gazzola (1989), 38 B.C.L.R. (2d) 27, 4 R.P.R. (2d) 153, [1989] 5 W.W.R. 740, 75 C.B.R. (N.S.) 151, (sub nom. *Thorne Ernst & Whinney Inc. v. Gazzola)* 60 D.L.R. (4th) 590, 1989 CarswellBC 354 (B.C. C.A.) — followed

Willmott (1886), L.R. 31 Ch. D. 425 (Eng. Ch. Div.) — considered

Wily v. St. George Partnership Banking Ltd. (1999), 161 A.L.R. 1, [1999] FCA 33 (Australia Fed. Ct.) — considered

Yagerphone Ltd., Re (1935), [1935] 1 Ch. 392 (Eng. Ch. Div.) — followed

Statutes considered:

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

s. 13.4 [en. 1992, c. 27, s. 9(1)] — referred to

s. 38 — referred to

s. 67 — considered

s. 69.3 [en. 1992, c. 27, s. 36(1)] — referred to

s. 70(1) — referred to

s. 71 — referred to

s. 91 — referred to

s. 95 — considered

s. 95(1) — referred to

s. 96 — referred to

s. 96(1) — referred to

s. 136 — considered

s. 136(1) — referred to

s. 136(1)(f) — referred to

s. 141 — referred to

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — referred to

Pt. IV — referred to

s. 11 — considered

s. 11.7 [en. 1997, c. 12, s. 124] — referred to

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

s. 20 — considered

s. 36.1 [en. 2007, c. 36, s. 78] — referred to

s. 42 — referred to

Excise Tax Act, R.S.C. 1985, c. E-15
Generally — referred to

s. 222(3) — referred to

Insolvency Act, 1986, c. 45
Generally — referred to

Personal Property Security Act, R.S.O. 1990, c. P.10
Generally — referred to

Statute of Elizabeth, 13 Eliz. 1, c. 5
Generally — referred to

HEARING of threshold issue regarding proceeds of preferences transactions in motion by trustee in bankruptcy for declaration certain transactions were void as fraudulent preferences.

***Morawetz J.*:**

1 KPMG Inc., as Trustee in Bankruptcy (the "Trustee") for Aero Inventory (UK) Limited and Aero Inventory plc (together, "Aero") brings this motion to have certain transactions (the "October Transactions") entered into between Aero and Air Canada declared void pursuant to s. 95 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, ("*BIA*"). The Trustee seeks the return of value in the amount of U.S. $75 million from Air Canada (the "Preference Proceeds").

2 A threshold issue has been identified. The Trustee takes the position that the Preference Proceeds, once recovered, would be subject to the rights of Aero's secured creditors. Air Canada takes the position that any proceeds resulting from this preference motion should only benefit Aero's unsecured creditors.

3 Therefore, at this point, the central issue is a question of law: are the proceeds of a preference action under s. 95 of the *BIA* subject to the rights of secured creditors?

4 In addition to the direction sought with respect to the priority of the Preference Proceeds, Air Canada also seeks an order regularizing the proceedings under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, ("*CCAA*"), the parallel proceedings under the *BIA* and the preference motion.

Background Information

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

5 In its factum, Air Canada has provided an account of the events leading up to the October Transactions. In view of the threshold question of law, in my view, it is premature to focus on the facts in respect of the October Transactions. A brief overview of the background is, however, helpful, to put matters into context.

6 On November 11, 2009, Administration proceedings in respect of Aero were commenced in the High Court of Justice of England and Wales (Chancery Division, Companies Court) (the "Foreign Proceedings"). Messrs. Tucker, Heis and Graham of KPMG LLP were appointed as joint administrators (the "Administrators") of Aero.

7 On the same day, this court recognized the appointment of the Administrators as foreign representatives of Aero (the "Foreign Representatives") under Part IV of the *CCAA*.

8 Aero reported that its secured creditors would face a shortfall of approximately £150 million, while its unsecured creditors, who are owed approximately £60 million, would receive virtually nothing at all.

9 Following the November 11, 2009 filings, the Foreign Representatives met with Air Canada and discussed, *inter alia*, the October Transactions. From the Foreign Representatives' standpoint, a concern arose that the October Transactions might constitute an unlawful preference.

10 The October Transactions arose out of a relationship between Air Canada and Aero in respect of maintenance required for Air Canada's aircraft. In December 2008 Air Canada and Aero executed an agreement (the "Line Maintenance Agreement") under which Aero became Air Canada's exclusive supplier for practically all of its Category 3 Inventory used for line maintenance.

11 In early 2009, Aero and Air Canada entered into an agreement (the "January Purchase Agreement") under which Aero sold to Air Canada a pool of Category 3 Inventory. Over the course of the year, Aero was expected to purchase parts from this pool of inventory.

12 In return, Air Canada provided Aero with nine U.S. $10 million principal Bills of Exchange (#1 - 9) and one similar Bill of Exchange (#10) for approximately U.S. $10.7 million (collectively, the "Bills of Exchange"). Each of the Bills of Exchange was payable to Aero and drawn on Air Canada. Air Canada contends that with the exception of transfers of the Bills of Exchange to Deutche Forfait (which never, in fact, occurred), the January Purchase Agreement required Air Canada's consent to any transfer of the Bills of Exchange.

13 Air Canada contends that Aero ultimately failed to comply with the most significant provisions of the January Purchase Agreement. Ultimately, Aero and Air Canada reached an agreement under which certain Bills of Exchange were delivered back by Aero to Air Canada. It is this series of transactions as between Aero and Air Canada that the Trustee refers to as the October Transactions.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

14 In January 2010, the Foreign Representatives brought a motion to assign the Aero companies into bankruptcy expressly "for the purpose of pursuing a preference action under s. 95(1) or 96(1) of the *BIA*. On January 22, 2010, the court authorized the Administrators to assign Aero into bankruptcy and temporarily lifted the stay for that purpose (the January 2010 "Order").

15 In seeking the January 22, 2010 Order, the Administrators advised the court that they wished to assign Aero into bankruptcy to preserve the right to pursue any reviewable preferences that may have taken place during the statutory review period prescribed by the *BIA*. The Administrators further advised that their security searches had revealed two secured creditors, Lloyds (asserting a general security interest in Aero's assets) and Air Canada.

16 On February 4, 2010, the Trustee reported that although no claims process had been conducted, all creditors had been advised of the Administrators' view that the secured creditors would suffer a significant shortfall and that there would be no funds available for distribution to unsecured creditors. The Trustee further reported its expectation that the secured creditors' security would extend to any funds generated from a preference claim under ss. 95 or 96 of the *BIA*.

17 The Trustee also reported that, in light of the expectation that there would be no recoveries to unsecured creditors, it saw no value in incurring the expense associated with the discharge of its statutory obligations under the *BIA*.

18 On February 4, 2010, the Trustee filed a motion seeking to dispense with certain obligations of the Trustee under the *BIA*. The court granted the order sought by the Trustee (the "February 2010 Order"). Air Canada did not oppose the relief sought. The court issued the February 2010 Order in the *CCAA* proceedings extending the time period for the Trustee to perform its statutory obligations under the *BIA* (including convening a meeting of creditors and holding a vote of the unsecured creditors) until further order. The February 2010 Order further authorized the Administrators to provide direction to, and supervise the Trustee in pursuing the contemplated preference motion, subject to the review of the court.

19 On April 27, 2010, the Trustee brought a motion in the *CCAA* proceedings seeking a declaration that the October Transactions between Air Canada and Aero constituted a preference within the meaning of s. 95(1) of the *BIA*.

20 On June 30, 2010, the Trustee filed a report which included opinions from independent counsel on the validity and enforceability of the security held by a syndicate of secured lenders (the "Lenders") over Aero's assets.

21 Aero financed its business with the U.S. $500 million revolving facility which it obtained from the Lenders. The Lenders hold:

(a) a general security interest and fixed mortgage over all the personal property of Aero in Canada, which has been duly registered; and

(b) a deed of Hypothec also duly registered in the Province of Quebec.

The Issues

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

22 Three issues need to be determined on this threshold motion:

(a) Whether secured creditors are entitled to assert priority over the proceeds of a preference action. Put another way, can the Trustee pursue the preference action solely on behalf of, and for the benefit of, a secured creditor?

(b) Is the preference motion properly brought within the *CCAA* proceedings, or should it be reconstituted in the bankruptcy proceedings?

(c) Should the February 2010 Order be varied to provide that the Trustee has to comply with certain obligations under the *BIA*?

23 As the Trustee points out in its factum, on several occasions, Canadian courts have had to consider whether a secured creditor has the right to assert its priority claim over the proceeds of a preference action. The Trustee acknowledges the body of jurisprudence appears unclear, inconsistent and conflicting.

24 It is the Trustee's position that jurisprudence and policy considerations underlying the *BIA* lead to the conclusion that the Preference Proceeds should be paid over to the Lenders by the Trustee.

25 Air Canada, not surprisingly, takes a different position. Air Canada does not contest the Trustee's ability to pursue preference claims in the bankruptcy proceedings. However, Air Canada takes the position that the Trustee cannot pursue a preference claim as an advocate for Lloyds or for Lloyd's exclusive benefit.

The Parties' Positions

1. Are secured creditors entitled to assert priority over the proceeds of a preference action and can the Trustee pursue a preference action solely on behalf of, and for the benefit of, a secured creditor?

Air Canada's Position

26 Air Canada takes the position that a trustee cannot pursue a preference action where the proceeds would accrue to the sole benefit of a secured creditor as to do so is inconsistent with the jurisprudence holding that fraudulent preferences that do not benefit unsecured creditors cannot be pursued. Instead, the right to pursue a fraudulent preference action is a statutory right of the trustee only, and where appropriate to pursue, such preferences are only void as against the trustee, such that the recovered property accrues to the benefit of the general body of unsecured creditors. Finally, Air Canada submits that the proposed preference action is inconsistent with the role of a trustee.

The purpose of a preference action

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

27 Air Canada submits that the purpose of a preference action is to allow for the equal distribution of the debtor's assets among the general body of creditors such that a trustee cannot pursue a preference action for the sole benefit of a secured creditor.

28 Further, the purpose of s. 95 of the *BIA* is to ensure that the debtor's money is divisible equally among unsecured creditors, subject to the priorities in s. 136 of the *BIA*. In support of this proposition, counsel to Air Canada cites the Supreme Court of Canada in *Hudson v. Benallack* (1975), [1976] 2 S.C.R. 168 (S.C.C.) at p. 175, where it is noted that the purpose of preference actions is to put all creditors on an equal footing.

29 Counsel further submits that s. 95 of the *BIA* permits a trustee to challenge the debtor's transactions occurring on the eve of bankruptcy, as such transactions reduce the money available for distribution to creditors and presumably fail to treat all of the creditors equally. Conversely, where there would be no benefit to unsecured creditors from the pursuit of a preference action, the Trustee may not undertake a preference action.

30 In this case, the Trustee's position is that the proceeds of the preference action accrue to the benefit of the secured creditor. Counsel to Air Canada submits that this would not constitute a benefit to the general body of creditors such that this action cannot be pursued. Instead, secured creditors' rights are to be exercised outside of bankruptcy as a function of their security agreement and provincial law: *BIA*, ss. 69.3, 70(1), 136(1) and 141.

31 Air Canada takes the position that the jurisprudence is replete with examples of the courts declining to allow a trustee to pursue a preference action where the proceeds would accrue to the sole benefit of secured creditors.

32 Air Canada submits that in *Cooper, Re* (1875), (1874-75) L.R. 10 Ch. App. 510 (Eng. Ch. App.) at p. 511-512, the court found that the trustee ought not to pursue a preference action for the benefit of a single creditor. Instead, preference actions are to be pursued for the benefit of all creditors. In that case, a creditor alleged that he had given the debtor an advance of £2000, secured by a consignment of the debtor's shipment of currants. However, once the shipment arrived, the debtor pledged the bills of lading for that shipment to a subsequent creditor, as security for advances made by that person. The Registrar declined to order the trustee to account to the estate for the value of the currants or take the necessary steps for their recovery, but did order that the first creditor was at liberty to use the trustee's name in any proceeding against the subsequent creditor or the debtor to enforce the delivery of the currants or payment of the proceeds to him. On appeal, the Divisional Court found that the trustee's name could not be used in a preference action by an encumbrancer, unless the secured creditor were to give up the claim on the property for the benefit of all creditors. There could be no fraudulent preference where the preference granted concerned property that did not belong to the bankrupt.

The right to bring a preference action is a statutory right of the Trustee

33 Air Canada takes the position that the Trustee's proposed preference action is incompatible with the fact that the right to pursue a preference action is a statutory right provided solely to the Trustee and a secured creditor cannot take advantage of the Trustee's statutory right. Instead, property recovered as a result of the exercise of the Trustee's statutory right is not subject to any security interest.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

34 Counsel to Air Canada referenced in *Yagerphone Ltd., Re*, [1935] 1 Ch. 392 (Eng. Ch. Div.) at p. 396, which counsel submits affirms the principle established in *Ex parte Cooper*. In *Yagerphone*, the liquidator sought to attack the provision of certain funds to a creditor, which funds were said to be subject to a debenture. The debenture holder was found to not be entitled to the proceeds of the preference action as he held a general or floating security interest in the debtor's property, rather than a fixed charge over those funds. As a result, the preference action could be pursued and the transfer was considered to be void solely as against the liquidator, with the recovered funds impressed with a trust in favour of the creditors generally.

Bennett J. stated at pp. 395-96:

> There have been two cases which establish quite clearly that, whether in bankruptcy or in the liquidation of a company, a secured creditor has no right to enforce for his benefit the remedy which is given to a trustee in bankruptcy or the liquidator of the company of avoiding a payment or setting aside a transaction made or entered into with a view to preferring a creditor of the bankrupt or a company in liquidation. The authorities are *Ex parte Cooper and Willmott v. London Celluloid Co.*
>
> Neither of these cases, as I have said, decides the point which arises on the summons. I propose to decide it in favour of the liquidators on this ground - namely, that, at the time when the securities contained in the debenture issued to H. Yager (London), Ld., crystallised, the 240*l.* 11s. 2d. was not the property of Yagerphone, Ld., the company which issued the debenture.
>
> . . .
>
> The right to recover a sum of money from a creditor who has been preferred is conferred for the purpose of benefitting the general body of creditors, and I think Mr. Montgomery White was right when he said that the sum of money, when recovered by the liquidators by virtue of s. 265 of the Companies Act, 1929, and s. 44 of the Bankruptcy Act, 1914, did not become part of the general assets of Yagerphone, Ld., but was a sum of money received by the liquidators impressed in their hands with a trust for those creditors amongst whom they had to distribute the assets of the company.
>
> [Emphasis added; Citations omitted.]

35 Air Canada submits that the reasoning of *Yagerphone* was adopted in *Maybank Foods Inc., Re* (1990), 72 O.R. (2d) 93 (Ont. S.C.), and *Oasis Merchandising Services Ltd., Re* (1996), [1998] Ch. 170 (Eng. C.A.). In *Maybank Foods*, the respondent had conceded that the proceeds of a preference action are held in trust for the general body of creditors. Air Canada frames the distinction drawn in *Oasis* as between assets which were the debtor's property upon liquidation and may be subject to a charge, and those that were conveyed away to another creditor but recovered pursuant to a preference action, which are not subject to a charge. In other words, the court in *Oasis* drew a distinction between assets over which a secured creditor possesses a fixed charge at the time of liquidation, which are subject to the security, and assets which were conveyed to another creditor and recovered pursuant to a preference action, which were subject to a floating charge and, as such, not subject to the secured creditor's security. *Oasis* dealt with the proceeds of a wrongful trading claim, but the court nevertheless noted that the proceeds of preference actions are not company property, but rather, exist by virtue of liquidation and the liquidator's right of action, and are impressed with a trust in favour of the unsecured creditors. At pp. 181, the Court stated:

> Thus a right of action against directors for misfeasance which the liquidator (amongst others) can enforce under section 212 of the Act of 1986 and the fruits of such an action are property of the company capable of being charged by a debenture, because the right of action arose and was available to the company prior to the winding up. But with this can be contrasted the right of action by a liquidator, and the fruits of such an action, for fraudulent preference or fraudulent or wrongful trading, which are not the property of the company and are not caught by a debenture: see *Gough, Company*

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Charges, 2nd ed. (1996), p. 122.

36 Similarly, Air Canada notes that Millet J. in *MC Bacon Ltd. (No.2), Re* (1990), [1991] Ch. 127 (Eng. Ch. Div.), a case concerning whether the liquidator was entitled to recover its fees for the pursuit of a preference action, continued to apply *Yagerphone* to the determination of whether that preference action was properly brought so as to constitute an expense of the winding up payable out of the assets of the company. In making that determination, Millet J. noted that a preference action can only be made by a liquidator or administrator, and not a debentureholder because a debenture holder is bound by payments in the ordinary course of business even if the payment is preferential, whereas the liquidator is not. Millet J. wrote at p. 137:

> It was thus established long before 1986 that any sum recovered from a creditor who has been wrongly preferred enures for the benefit of the general body of creditors, not for the benefit of the company or the holder of a floating charge. It does not become part of the company's assets but is received by the liquidator impressed with a trust in favour of those creditors amongst whom he has to distribute the assets of the company: see In Yagerphone Ltd. [1935] Ch. 392.

Fraudulent preferences are only void as against the trustee

37 Counsel to Air Canada submits that fraudulent preferences under s. 95 of the *BIA* are declared to be void *as against the Trustee* and not as against any other party, including secured creditors. Property recovered pursuant to a preference action is held by the Trustee for the benefit of the general body of creditors.

38 Air Canada submits that the judgment of Hood J. in *S-Marque Inc. v. Homburg Industries Ltd.*, [1998] N.S.J. No. 550 (N.S. S.C.) aff'd for diff't reasons *Homburg v. S-Marque Inc.*, [1999] N.S.J. No. 94 (N.S. C.A.), endorses this view. In that case the deficit in the security of the secured creditor could not be paid in priority from the proceeds of a preference action. Rather the secured creditor could claim for the deficit as an unsecured creditor. Hood J. reviewed the jurisprudence relating to the entitlement to the proceeds of preference actions and concluded at para. 147:

> The effect of all these decisions is that overturning a fraudulent preference puts the property back in the hands of the trustee. The transaction is void as against the trustee in bankruptcy. The property does not, however, revert to the bankrupt to be available as part of the security over which a secured creditor has rights of seizure.
>
> [Emphasis added.]

39 To similar effect, Air Canada submits that the court in *Canadian Imperial Bank of Commerce v. Canotek Development Corp.* (1997), 35 O.R. (3d) 247 (Ont. C.A.) ("*Canotek*"), stated at p. 256 that "[s]ection 95 renders a fraudulent preference void as against the trustee in bankruptcy; it does not render it void as against a secured creditor".

40 In *Canotek*, the bank held a general security agreement and chattel mortgage on the assets of F. Inc. (the debtor), which went bankrupt, but C. Corp, (the landlord of F. Inc.) levied distress against F. Inc without granting sufficient time for the tenant to rectify the situation. The court found that there was a fraudulent preference against the trustee, but not as against the bank. However, the landlord might still have rights under s. 136(1)(f) as a preferred creditor.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

41 The court rejected the bank's argument regarding the reversal of priorities, stating at p. 251:

> However, the bank says that but for the premature sale the property distrained would have been property of the bankrupt and, thus, subject to the bankruptcy. In that case, the bank argues, it would have been entitled to its security as against the trustee. In short, the bank argues that it has been deprived of the right to take advantage of the assignment in bankruptcy to gain priority in the goods and their proceeds over the trustee in bankruptcy. Since the trustee would have priority over the landlord's distraint, the bank would thus have priority over the landlord as secured creditor in the bankruptcy. This is a tail-chasing type of priority problem which must be resolved by looking at the relationship between the true parties to the dispute. In this case, the bank never did have a priority over the landlord once the landlord distrained against the goods. <u>The artificiality of looking to the bankruptcy proceedings to give the bank something the law never intended it to have is obvious, and should not be countenanced by the court</u>.

42 Intriguingly, the Court while noting, at p. 256, that "[g]enerally, *provincial law governs priorities between various secured creditors, and also between secured creditors and landlords*", went on to state that ...outside bankruptcy the landlord prevails in facts such as these, and the incidence of bankruptcy *should in no way alter this situation*."[Emphasis added.]

The Trustee is an impartial officer of the court

43 Air Canada takes the position that the Trustee's position in respect of the proposed preference action is inconsistent with its role as an impartial officer of the court submitting that a trustee should not act as an advocate for any particular class of creditors. Instead, its role is to gather in the assets of the bankrupt and divide the proceeds in accordance with the scheme of the *BIA*: See *Beetown Honey Products Inc., Re* (2003), 46 C.B.R. (4th) 195 (Ont. S.C.J.) at para. 22, aff'd (2004), 3 C.B.R. (5th) 204 (Ont. C.A.).

44 Air Canada submits that in bringing this preference action, the Trustee seeks to realize a benefit solely for Lloyd's, a secured creditor. The Trustee has also failed to involve the unsecured creditors and it has failed to disclose competing considerations that might indicate that this preference action is unwarranted. While the Trustee may act for a secured creditor pursuant to s. 13.4 of the *BIA*, Air Canada contends that the record does not indicate that it has met the statutory preconditions to assisting a secured creditor. Air Canada submits that the purpose of s. 13.4 is to protect unsecured creditors' rights: See *Pratchler Agro Services Inc. (Trustee of) v. Cargill Ltd.* (1999), 11 C.B.R. (4th) 104 (Sask Q.B.) at para. 9.

45 Section 13.4 of the *BIA* provides:

> (1) No trustee may, while acting as the trustee of an estate, act for or assist a secured creditor to assert a claim against the estate or to realize or otherwise deal with a security that the secured creditor holds, unless the trustee has obtained a written opinion from independent legal counsel that the security is valid and enforceable against the estate.
>
> (1.1) Forthwith on commencing to act for or assist a secured creditor of the estate in the manner set out in subsection (1), a trustee shall notify the Superintendent and the creditors or the inspectors
>
> > (a) that the trustee is acting for the secured creditor;
> >
> > (b) of the basis of any remuneration from the secured creditor; and
> >
> > (c) of the opinion referred to in subsection (1).

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(2) Within two days after receiving a request therefor, a trustee shall provide the Superintendent with a copy of the opinion referred to in subsection (1) and shall also provide a copy to each creditor who has made a request therefor.

46 Air Canada submits that the record before the court does not indicate that the Trustee has obtained a written opinion from independent legal counsel that the security in issue is valid and enforceable against the estate. There is also no evidence that the Trustee has notified the Superintendent in Bankruptcy and other creditors of such an opinion (if it exists), its intention to act for Lloyd's, or the details of any remuneration it may be receiving from the secured creditor.

The Trustee's Position

47 The Trustee's position is that the jurisprudence is somewhat unclear, but the weight of jurisprudence favours granting the proceeds of preference action to secured creditors possessing a fixed, rather than floating charge, a finding that is reinforced by the structure of the *BIA* and the policy considerations underlying the *BIA*. As a result, the proceeds of this preference action ought to be paid to the secured creditor.

The distinction between fixed and floating charges

48 The Trustee submits that Air Canada avoided a long-standing and obvious distinction between fixed and floating charges. Floating charges have been held to not attach to property that is the subject of a preference action. Conversely, fixed charges do: *Yagerphone*. This is because the secured creditor has no title when a charge is floating, yet gains priority where it is specific: *Innovation Credit Union v. Bank of Montreal*, [2010] 3 S.C.R. 3 (S.C.C.) at para. 46.

49 Counsel to the Trustee submits that certain courts have interpreted *Yagerphone* overbroadly. *Yagerphone* concerned a dispute as to the priority as between a liquidator and a debentureholder over the proceeds of a preference action. The court held that the debentureholder's security did not attach to the assets at the time that they were transferred such that, in that case, the secured creditor had no greater claim to those assets than any other creditor.

50 The Trustee acknowledges that *Maybank Foods* goes beyond the ratio in *Yagerphone*, yet contends that the overbroad interpretation of *Yagerphone* was based on a concession made by the respondent.

51 The Trustee submits that the weight of case law favours the view that floating charges do not attach to assets recovered pursuant to a preference action; but, fixed charges do. In support of this position, the Trustee notes that: *MC Bacon Ltd.* (which found that preference action proceeds enure to the benefit of the general body of creditors) concerned a floating, rather than fixed charge; *Oasis* is the product of a technical reading of UK legislation; and *S-Marque Inc.* was affirmed for different reasons at the Court of Appeal, namely, that the debenture had not crystallized at the time that the asset was transferred away, such that the secured creditor was not entitled to the proceeds of a preference action. This is the same finding as the court in *Mohawk Sports Equipment Ltd. (No. 2), Re* (1972), 17 C.B.R. (N.S.) 115 (Ont. S.C.), at paras. 16-17, which prevented the proceeds of a preference action being claimed by the holder of security that had not crystallized at the time of transfer.

52 The Trustee points out that this distinction is found throughout the case law. Roy Goode in *Principles of Corporate*

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Insolvency Law, 3d ed. (London: Sweet & Maxwell, 2005) notes at s. 11-140:

> All these cases assume that what is recovered by the liquidator either was never the property of the chargee or ceased to be so prior to the winding up as the result of the fact that the transfer in question overrode the charge. In such a case the chargee is not entitled to use the avoidance provisions to recover what he had lost or had never had. Where however, the charge was not overridden by the transfer and the property transferred is recovered, the charge continues to attach to the recovered property. [Emphasis added]

53 The Trustee further submits that in *N.A. Kratzmann Pty. Ltd. v. Tucker (No. 2)* (1968), 123 C.L.R. 295 (Australia H.C.), the court noted in obiter at p. 302 that "if specific property, to which a charge, validly created by the bankrupt prior to his bankruptcy, has attached prior to the time of its disposition, is subsequently recovered as a preference the trustee's title will be no higher or better than that of the bankrupt to which he has succeeded". In arriving at this conclusion, the court draws the distinction between specific property, that is subject to a charge, and over which the secured creditor will enjoy priority even if recovered pursuant to a preference, whereas property subject to a floating charge will not be subject to the charge when recovered by the trustee. The court reasoned at pp. 300-01:

> Now in bankruptcy the property of a bankrupt vests in his trustee upon the making of the sequestration order. The property which so vests is, of course, subject, in the hands of the trustee, to any charges validly created in relation to it by the bankrupt prior to the bankruptcy. The position of a secured creditor who has a charge on specific property is, of course, not in question; such property in the hands of the trustee will still remain subject to the charge. But where security has been given by a bankrupt over all of his assets and a payment to a creditor is made by him out of moneys subject to the charge and the payment is, as against the trustee, subsequently declared void as a preference the moneys paid, when recovered, will not be subject to the charge. In such a case it may be said that although the moneys paid as a preference were at the time of payment subject to the charge, the moneys recovered by the trustee are not the same moneys and that they do not, by virtue of payment to the trustee, become moneys of the bankrupt or in any way subject to the charge; when recovered they become the moneys of the trustee and his title to them does not depend upon his succession to any title which the bankrupt had. It was, we think, in this sense that Bennett J meant in the passage that we have first cited that, applying the bankruptcy rules in a winding up,
>
> > ...the sum of money, when recovered by the liquidators by virtue of s 265 of the Companies Act, 1929, and s 44 of the Bankruptcy Act 1914, did not become part of the general assets of Yagerphone Ltd, but was a sum of money received by the liquidators impressed in their hands with a trust for those creditors amongst whom they had to distribute the assets of the company.
>
> The view which we have formed is, we think, borne out by the observations of Russell L.J. concerning the decision in *Yagerphone* case where, in *N.W. Robbie & Co. Ltd. v Witney Warehouse Co. Ltd.* he said:
>
> > ...that a claim by the liquidator for repayment to him of a fraudulent preference was not subject to the debenture-holder's charge; a statutory right in and only in the liquidator to make such a claim could never have been property of the company subject to the charge.
>
> It is of significance that his Lordship did not think that the decision in any such case could depend upon whether or not the charge had crystallized at the time when the payment to the creditor was made.
>
> The case would be otherwise, of course, where a preference consists of the disposition of specific and identifiable property subject to a charge validly created in relation thereto by a bankrupt prior to his bankruptcy and where the avoidance of the disposition affects title to such property. That this is so seems to us to be clear as a matter of principle....
>
> In such a case the result of the avoidance of the disposition is to revest the property in the trustee subject to the charge

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> which the bankrupt had validly created prior to the bankruptcy. [Emphasis added; Footnotes omitted.]

The Structure of the BIA

54 The Trustee submits that the structure of the *BIA* favours giving the proceeds of a preference action to the secured creditor. Successful preference actions render transactions void as against the trustee as per s. 95 of the *BIA*. The property then vests in the Trustee as per ss. 67 and 71 of the *BIA*. However, the Trustee takes the property subject to the rights of secured creditors pursuant to s. 71, as the Trustee cannot obtain a greater interest in the goods than that enjoyed by the bankrupt: *Giffen, Re*, [1998] 1 S.C.R. 91 (S.C.C.) at para. 50; *Lefebvre, Re*, [2004] 3 S.C.R. 326 (S.C.C.) at para. 37. Further, the Trustee reasons that division of the estate is subject to the rights of secured creditors pursuant to s. 136 of the *BIA*. As a result, secured creditors retain priority in those assets over which they had perfected security interests.

55 The Trustee submits that the court in *ASI Acoustical Supplies Inc., Re* (2000), 22 C.B.R. (4th) 174 (B.C. S.C.), noted that the fact that only the trustee can bring a preference action does not disturb the priority rights of creditors to the proceeds of preference actions, stating at para. 20: "[i]n any event the fact that only a Trustee can make a claim alleging *a* fraudulent preference does not change the priority position of a secured creditor.

56 The Trustee further submits that in *Agricultural Credit Corp. of Saskatchewan v. Featherstone (Trustee of)* (1996), 145 Sask. R. 161 (Sask. Q.B.), the court recognized that "[m]onies owing to a bankrupt, when collected by the trustee continued to be the property of the bankrupt and continue to be subject to the existing security interests. This includes monies realized through the efforts of the trustee" (citations omitted).

57 The case of *Ramgotra (Trustee of) v. North American Life Assurance Co.*, [1996] 1 S.C.R. 325 (S.C.C.), cited by the Trustee, is not analogous, but potentially somewhat informative. The court found that s. 91 (dealing with whether settled property falls back into the estate) is subject to s. 67, insofar as s. 67 governs the disposition of assets in the estate. The court bifurcated the inquiry as follows at paras. 44, 45, 46, 48 and 49:

> In reconciling ss. 67(1)(b) and 91 BIA, it is important to remember that the general scheme through which a bankrupt's estate is divided by the trustee among creditors involves two distinct stages. First, the Act provides that an insolvent person "may make an assignment of all his property for the general benefit of his creditors" (s. 49(1)), or that creditors "may file in court a petition for a receiving order against a debtor" (s. 43(1)). At the time of the assignment or receiving order, the trustee in bankruptcy is obligated to take possession of the assets forming the estate of the bankrupt. Thus, by operation of s. 71(2), the bankrupt's property passes to and vests in the trustee...
>
> Once the bankrupt's property has passed into the possession of the trustee, the Act provides the trustee with the power to administer the estate...
>
> During the property-passing stage of bankruptcy, the trustee is empowered under s. 91 of the Act to set aside certain settlements which have reduced the size of the estate. Thus, s. 91 outlines the circumstances in which a settlement will be voidable at the behest of the trustee in bankruptcy. If a settlement is declared void against the trustee, then the settled property reverts back to the bankrupt's estate, and falls into the possession of the trustee in bankruptcy...
>
> . . .
>
> However, the trustee is barred from dividing two categories of property among creditors: property held by the bankrupt in trust for another person (s. 67(1)(a)), and property rendered exempt from execution or seizure under provincial

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> legislation (s. 67(1)(b)). While such property becomes part of the bankrupt's estate in the possession of the trustee, the trustee may not exercise his or her estate distribution powers over it by reason of s. 67.
>
> Thus, it can be seen that ss. 91 and 67 relate to two different stages of bankruptcy. Section 91 dictates that certain settled property will fall back into the estate of the bankrupt in the possession of the trustee, while s. 67 is directed at the exercise of administrative powers over the estate by the trustee. Where a settlement is void against the trustee under s. 91, then in normal circumstances, the trustee is empowered to administer the settled asset, and use it to satisfy the claims of creditors. However, in the special case where the asset is exempt under s. 67(1)(b), then the trustee is prohibited from exercising his or her distribution powers because the asset is not subject to division among creditors.

58 Counsel to the Trustee also references *Warran Whillans Enterprises Inc. (Trustee of) v. Gazzola* (1989), 60 D.L.R. (4th) 590 (B.C. C.A.). In determining whether a landlord would be entitled to the proceeds of a preference action the Court of Appeal outlined the scheme of distribution as follows:

> Under the Bankruptcy Act the trustee is charged with gathering the assets of the bankrupt for the benefit of creditors and then distributing those assets pursuant to the scheme of distribution set out in s. 136 of the Act. Section 95 is in that part of the Act that deals with schemes and preferences. Pursuant to s. 95 the trustee is entitled to consider any transaction involving a creditor of the bankrupt and if that transaction occurred within three months prior to the bankruptcy, the trustee can take steps to seek to establish that the transaction be deemed fraudulent and void as against the trustee...
>
> . . .
>
> In due course, depending on the claims of secured creditors and those standing in priority to the landlord under the scheme of distribution established by s. 136 of the Act, if there are sufficient assets in the estate the landlord will then receive payment pursuant to the provisions of that section.

59 The Trustee suggests that this reasoning was endorsed in *Canotek* at p. 256 where the Court of Appeal held that provincial law governs priorities between secured creditors and landlords and the incidence of bankruptcy should not disturb the order of priority present outside bankruptcy.

The policy underlying the BIA

60 The Trustee submits that the policy underlying the *BIA* favours giving the proceeds of the preference action to the secured creditor, as this interpretation avoids altering priorities and nullifying a secured creditor's claim to collateral simply because a debtor has dealt with those assets preferentially. Otherwise, an insolvent person could defeat secured creditors' rights by granting a preference immediately prior to bankruptcy, with the resulting proceeds flowing to the benefit of unsecured creditors. This would be inconsistent with commercial sense, which the *BIA* seeks to protect.

61 The Trustee notes that the courts have disallowed attempts to alter priorities through unlawful means. In *Anron Mechanical Ltd. v. L'Abbé Construction (Ontario) Ltd. (Trustee of)* (1991), 5 C.B.R. (3d) 133 (Ont. Gen. Div.) at para. 9 (Ont. Gen. Div.), the specific and identifiable property (traceable moneys), that had been impressed with a trust did not lose that quality simply by virtue of being recovered as fraudulent payments:

> If this were not so, a general contractor could then easily divert monies, defeat the rights of the unpaid subcontractors and thwart the whole purpose of the trust section of the Construction Lien Act. If he cannot divert the monies lawfully, as by assignment, then surely he cannot do so unlawfully, as by a fraudulent preference.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

62 The Trustee submits that the proceeds of a preference action ought to be paid in accordance with the hierarchy established in the *BIA*. Unsecured creditors do share rateably under s. 141, yet their claim is expressly subordinate to preferred creditors under s. 136, whose claim is itself subject to the rights of secured creditors.

63 As a final point, the Trustee submits that this proposed action is not inconsistent with the role of the trustee. The trustee may act for secured creditors pursuant to s. 13.4 of the *BIA* if they have obtained a written opinion from independent legal counsel that the security is valid and enforceable. The Trustee contends that such an opinion was obtained and submitted in the Trustee's report filed on June 30, 2010.

64 The Trustee also contends that it provided notice to the Superintendent and notified creditors before any action was taken on behalf of the lenders in accordance with the February 2010 Order. Further, it has: provided notice of its independent security opinion; posted this notice; and provided notice that it was bringing a preference action with the expectation that it would pay over the proceeds of that action to the secured creditor, Lloyds. As the Trustee is not receiving any remuneration from secured creditors, it provided no notice that it was receiving remuneration from the secured creditor. Instead, the Trustee is funded by the Foreign Representatives who have been funded to date by monies in the estate.

2. Is the preference motion properly brought within the CCAA proceedings, or should it be reconstituted in the bankruptcy proceedings?

65 Air Canada submits that this preference action is improperly brought. A preference action pursuant to s. 95 of the *BIA* can only be taken in Bankruptcy proceedings or, pursuant to s. 36.1 of the *CCAA*, a monitor (appointed pursuant to s. 11.7) may pursue a preference action where a plan of compromise or arrangement has been proposed. This preference action is not brought in bankruptcy and is not brought pursuant to a plan of arrangement, while the Trustee, as an Information Officer, is unable to bring an action that is reserved to a monitor.

66 The Trustee submits that this Court dealt with this issue in its February 2010 Order dealt with this issue, with reasons reported at *Tucker v. Aero Inventory (UK) Ltd.*, 2010 ONSC 1196 (Ont. S.C.J. [Commercial List]). It held that concurrent *BIA* and *CCAA* proceedings are contemplated by Part IV; the preference motion is brought to maximize the Debtor Company's assets; failing to allow concurrent proceedings may preclude the review of what may in fact be a preferential transaction which is contrary to public policy; Air Canada commenced and then abandoned an appeal to this motion; such that, these issues are now *res judicata*. In any event, the Trustee contends that s. 42 of the *CCAA* intends for the *CCAA* to operate in tandem with the *BIA*: *Ted Leroy Trucking Ltd., Re*, [2010] 3 S.C.R. 379 (S.C.C.) at para. 76.

3. Should the February 2010 Order be varied to provide that the Trustee has to comply with certain obligations under the BIA?

67 Air Canada notes that the February 2010 Order ought to be varied to ensure that the Trustee complies with its statutory obligations. To date, no proofs of claim have been sought from unsecured creditors, and no meeting of creditors has been convened to either consider the bankrupt's affairs, or hold a vote of the unsecured creditors to affirm the appointment of the Trustee, or substitute another trustee in its place, or to appoint inspectors to give direction to the Trustee. As a result, Air Canada submits that an order directing the Trustee to comply with its obligations under the *BIA* ought to be granted.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Additional Commonwealth Jurisprudence

68 The case of *Willmott London Celluloid Co.* (1886), L.R. 31 Ch. D. 425 (Eng. Ch. Div.), appears to support the position of Air Canada, as the court held at pp. 435-36 that a preference action can only be pursued by a liquidator, while the proceeds are intended for the benefit of the general body of creditors: See also: *Quality Camera Co. Pty. Ltd., Re* (1965), 83 W.N. (Pt 1) 226 (N.S.W. S.C.); and *Bibra Lake Holdings Pty. Ltd. v. Firmadoor Australia Pty. Ltd.* (1992), 7 A.C.S.R. 380 (Western Australia S.C.).

69 Further support can be found in *Wily v. St. George Partnership Banking Ltd.* (1999), 161 A.L.R. 1 (Australia Fed. Ct.), in which no fraudulent preference was found as the payment was *to* a secured creditor, but the Federal Court of Australia helpfully mentioned three principles applicable to that context. The first being that a debtor is entitled to prefer creditors subject to the *Statute of Elizabeth* 13 Eliz 1 c 5. The second and third principles are detailed at p. 5 as follows:

> ...in insolvency, by which I mean bankruptcy in the case of a natural person and liquidation in the case of a company, legislation provides that, <u>with certain limited exceptions, all unsecured creditors of a bankrupt or an insolvent company are to be treated equally</u>: that is, their liabilities are to be discharged rateably. This principle can be found in bankruptcy statutes dating back to 1542 (see 34 & 35 Hen 8 c 4, s 1 which was concerned with absconding debtors) and in company statutes since the Winding Up Act of 1844 (7 & 8 Vict c 111); see now s 108 of the Bankruptcy Act and s 555 of the Corporations Law.
>
> The third principle is the recognition that certain dispositions made by a debtor who subsequently becomes bankrupt, or by a company that subsequently is wound up, should be recovered and be available to meet the claims of the creditors generally. Section 122 of the Bankruptcy Act is one example of the operation of this principle. Others are to be found in the Bankruptcy Act and the Corporations Law. Many other systems of law have comparable provisions.
>
> [Emphasis added.]

70 In *Wily*, the Court found that if there is no detriment to the unsecured creditors, there can be no preference. Consequently, it would be appear to be the case that if the proceeds of the preference action were to be co-opted entirely to the benefit of the secured creditors there would be no resulting benefit to the unsecured creditors, thereby precluding bringing a preference action in this situation. The Court in *Wily* stated at pp. 9-10:

> If one asks whether there is less money available for the general body of creditors by reason of the three payments to the bank the answer must be a clear No. The reason is that if the payments had not been made the property available for distribution among creditors would not have increased. The bank would have been entitled to receive payment out of the property in the hands of the liquidator in priority to the other creditors. Any payment out of property that is not available to meet the debts due to the other creditors cannot confer a preference in favour of the payee. <u>In this case then, the other creditors are not any the worse off by reason of the payments to the bank.</u>
>
> . . .
>
> the short answer to the liquidator's submission is that provisions such as s 122 are designed to protect the statutory order of priority established by the Bankruptcy Act and, when it applies in a winding up, the statutory order established by the Corporations Law, <u>the statutory order being the right to receive payments pari passu. Section 122 is not concerned to protect the rights of a creditor who is accorded priority by some other legislation</u>, whether State or federal.
>
> [Emphasis added.]

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(See also *St. Anne-Nackawic Pulp Co. (Trustee of) v. Logistec Stevedoring (Atlantic) Inc.* (2005), 255 D.L.R. (4th) 137 (N.B. C.A.), which stands for the proposition that where a secured creditor is paid first there can be no fraudulent preference).

71 Additionally, McPherson J.A., who expressed concurring reasons in *Starkey v. Deputy Commissioner of Taxation* (1993), 11 A.C.L.C. 558 (Qld. C.A.) stopped short of endorsing the view in *Yagerphone* that preference proceeds are impressed in the hands of the liquidators with a trust for unsecured creditors, but did accept that since a secured creditor cannot bring a preference action a trustee should not be allowed to bring a preference action for the sole benefit of a secured creditor. The rationale for preventing secured creditors from sharing in the benefits of a right of action of a trustee was elucidated at pp. 566-67:

> If a secured creditor may not set in motion for his own benefit a procedure for avoiding preferences that exists for the benefit of the unsecured creditors, it is a logical consequence that he should not be able to claim the proceeds of avoiding such a preference when recovered. But it is another matter to say that the liquidator holds those proceeds in trust for the unsecured creditors if what is meant by that is a 'trust' in the full sense of the word, under which the unsecured creditors are equitable owners of the assets in winding up. There is little in recent decisions to support that view of the rights of creditors....
>
> It is secured creditors who, under the decision in Re Yagerphone Ltd, are denied a share in the proceeds of avoiding preferences in winding up. Unlike the claimant in that case the Commissioner here is not a secured creditor with rights that are enforceable against identified property independently of winding up.
>
> [Emphasis added.]

72 In *Bibra Lake Holdings Pty. Ltd. (in liq.) v. Firmadoor Australia Pty. Ltd.* (1992), 10 A.C.L.C. 726 (W.A.S.C.A.), Ipp J., in concurring reasons, held that fraudulent preferences are rendered void as against the liquidator only and the proceeds thereof do not form part of the assets of the company, writing at pp. 731:

> Moneys paid in circumstances which create an undue preference, and which are recoverable under s 451(1), are moneys which are recoverable for the benefit of the creditors and contributories. Such moneys cannot be said to have been the property of the company.
>
> . . .
>
> Undue preferences are void as against liquidators, not as against companies. Section 451 confers upon liquidators the sole right to bring proceedings for the recovery of undue preferences. [Emphasis added.]

73 Since *Yagerphone*, the governing UK law has been amended, including, in particular, by the 1985-86 reforms to the *Insolvency Act* (U.K.), 1986, c. 45, with the consequence that the court can now make an order to restore the *status quo ante* as if there had never been a preference. Nevertheless, despite these broadened powers, Millet J. found in *M.C. Bacon Ltd. (No. 2)* that *Yagerphone* remained applicable at p. 137:

> It was thus established long before 1986 that any sum recovered from a creditor who has been wrongly preferred enures for the benefit of the general body of creditors, not for the benefit of the company or the holder of a floating charge. It does not become part of the company's assets but is received by the liquidator impressed with a trust in favour of those creditors amongst whom he has to distribute the assets of the company: see In re Yagerphone Ltd. [1935] Ch. 392....
>
> In my judgment that is still the law, notwithstanding section 239(3) of the Act of 1986 which empowers the court on finding a voidable preference proved to make such order as it thinks fit for "restoring the position to what it would have

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> been if the company had not given that preference," and section 241(1)(c) which empowers the court to "release or discharge ... any security given by the company." Those powers are not intended to be exercised so as to enable a debenture holder to obtain the benefit of the proceedings brought by the liquidator. [Emphasis added.]

74 In *Tolcher v. National Australia Bank Ltd.* (2003), 44 A.C.S.R. 727 (New South Wales S.C.) (N.S.W.S.C.), Palmer J. found that where a settlement was paid from the estate subject to a charge in the form of a general security agreement against all assets of the bankrupt (which was characterised as a floating charge, rather than a specific charge), the monies recovered pursuant to a preference action to impugn that settlement are not subject to the charge as the trustee's title is not dependent on the debtor's title, nor can it be in the case of a statutorily-provided right of action.

75 Somewhat more nuanced support for Air Canada's position can be found in the case of *N.W. Robbie & Co. v. Witney Warehouse Co.*, [1963] 1 W.L.R. 1324 (Eng. C.A.). In that case, which had to do with whether certain debts could be set off rather than whether preference proceeds could accrue to secured creditors, Russell L.J. at p. 1338 rejected the suggestion that *Yagerphone* stands for the proposition that a charge cannot attach to assets acquired after the date of crystallization, noting instead that it stands for the proposition that proceeds from a liquidator's right to pursue a preference action, being a liquidator's right, cannot be property of the company subject to the charge. Russell L.J. stated at p. 1338:

> We were referred, in the course of the argument that there is no charge on the post-receivership "future assets," to a phrase in Kerr on Receivers (1963), 13th ed., p. 327, which says the charge would not attach to assets of the company acquired subsequent to the date of crystallisation." The authority cited is In re Yagerphone Ltd. The quotation, divorced from its context, is too wide to be supported, and if so divorced is not justified by that decision, which was that a claim by the liquidator for repayment to him of a fraudulent preference was not subject to the debenture-holder's charge: a statutory right in and only in the liquidator to make such a claim could never have been property of the company subject to the charge. [Emphasis added.]

76 Further support can be found in the case of *Horn v. York Paper Co. Ltd.* (1991), 5 A.C.S.R. 112 (N.S.W.S.C.), McLellan J. stated at p. 113:

> Where a transaction is avoided as against a liquidator by virtue of the operation of s 451 of the Companies Code (or s 565 of the Corporations Law) the liquidator is a necessary party to proceedings for the recovery of property or money based on such avoidance: see Kent v La Communauté des Soeurs de Charité de la Providence [1903] AC 220 at 226. This is because the transaction is avoided only against the liquidator, and the proceeds of recovery do not necessarily form part of the general assets of the company: see; Re Quality Camera Co Pty Ltd [1965] NSWR 1330; 83 WN (Pt 1) (NSW) 226 and; *N A Kratzmann Pty Ltd (in liq) v Tucker (No 2)* (1968) 123 CLR 295." [Emphasis added; See also *Bibra Lake*, holding to the same effect.]

77 In *Bayley v. National Australia Bank Ltd.* (1995), 16 A.C.S.R. 38 (Tasmania S.C.), Wright J. was tasked with determining whether funds recovered via a s. 468 action under the Australian *Corporations Law* (which renders dispositions after a winding up void), as well as funds recovered pursuant to a preference action, were subject to a secured creditor's registered floating charge. Wright J. held that the disposition successfully challenged via s. 468 were void for all purposes, as if the payment had never occurred, such that the funds "remained the property of the company at all relevant times and upon being restored to the company by the liquidator's actions became once more subject to the respondent's floating charge." Wright J. then went on to deal with the question of whether the charge attached to the assets recovered pursuant to the preference action.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

78 Wright J. held that the proceeds of a preference action were for the benefit of the general body of creditors. Wright J. noted that "unlike dispositions affected by s 468(1), *preferences* coming within the ambit of s 565(1) *are not void in any absolute sense but are void as against the liquidator only.*" It was not necessary for Wright J. to decide whether this would mean that the recovered property could be said to be free and clear of any prior charges, (although it was noted that this may be true of specific property subject to a charge prior to a winding up order) since, in the circumstances of that case, the charge at issue was floating and had not crystallized prior to the liquidation proceedings, such that it did not attach to the funds that were preferred. Instead, those funds were held for the benefit of the general body of creditors. Wright J. concluded:

> ...irrespective of whether for some purposes the recovered funds may be viewed as the "property" of the company being wound up, in the present circumstances they are not property which was or could have been subject to the floating charge at the time that charge crystallised viz. the date upon which liquidation proceedings commenced. Thus, in my opinion, the fund constituted by those moneys is not available to the respondent, but is distributable to the general creditors subject only to the statutory priorities provided by the Corporations Law.

79 The import of the words "void as against the trustee" was the subject of judicial consideration by the New South Wales Court of Appeal in *National Acceptance Corporation Pty. Ltd. v. Benson & Ors* (1988), 13 A.C.L.R. 1 (N.S.W.S.C.A.), where the Court held that the use of the word "void" in s. 368 of the Companies Code in question (which is similar to s. 468 of the Corporations Law considered in *Bayley*) "...means at least void for all purposes related or incidental to the administration of the winding up of the company" in contrast to the use of the word "void against the trustee" in their *Bankruptcy Act* which is more narrow. On this point, the Court noted that in *Commercial Bank of Australia v. Carruthers* (1964), 6 F.L.R. 247 (F.C.A.), Manning J. "*held that the provision did not produce the result that the preferential payment was void against anyone else than the Trustee in Bankruptcy*" (emphasis added).

80 Andrew Keay in "The Effects of a Successful Action by a Liquidator to Avoid a Pre-Liquidation Transaction" (1996) 15 (2) U. Tasm. L. Rev. 236 notes that the Australian bankruptcy regime has changed such that now transactions are no longer said to be "void as against the liquidator" but rather "voidable", and further, recovery vests in the company. He submits at p. 241 that this is a difference without a distinction as in the U.K., where the *Insolvency Act* grants the court broad powers to void fraudulent preferences and restore the position to the *status quo ante*, the courts have continued to apply *Yagerphone*. For instance, in *MC Bacon Ltd.*, *Yagerphone* was again endorsed as holding that secured creditors cannot recoup the proceeds of a preference action despite a similar change in wording as Australia's under the U.K. *Insolvency Act.*

81 In that article, Andrew Keay also notes that *Yagerphone* has existed for a long period of time and the government had the option to disturb this judicial practice but did not do so, nor is there evidence in the speeches of Parliament or the Explanatory Memorandum relating to the U.K. Bill that changed the U.K. *Insolvency Act* most recently that a change in judicial practice was contemplated, let alone required.

82 In addition to Andrew Keay's comments, it should be recalled that s. 95 of the *BIA* is worded more restrictively than the U.K. or Australian preference provisions, rendering fraudulent preferences void against the trustee only.

83 Andrew Keay does not regard reversing priorities as a problem, so much as a function of the legislative scheme itself. He writes at p. 264, in relation to the reversal of priorities:

> With respect, it appears that this argument overlooks the fact that bankruptcy or liquidation changes everything. While the company continues to exist, it is no longer directed by directors, and it is not run for the benefit of the shareholders.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> A liquidator acts on behalf of the company and he or she does so for the general body of creditors. Liquidation produces a whole new set of relationships and duties. While a secured creditor may argue that the general creditors are sometimes unjustly enriched by receiving the benefits of a recovery, the rebuttal to that might be that those creditors were prejudiced before liquidation because they did not receive any benefit from the voidable transaction and, in any event, they have suffered losses as a result of the liquidation. [Citations omitted; emphasis added.]

84 It could be argued that while priorities may well be reversed, as held in the case law, this stems from the role of the trustee. The status of the trustee is tripartite: as a successor in title, as a representative of creditors and finally, and importantly, the trustee has independent status under either federal or provincial law to avoid certain transactions: *Roderick Wood, Bankruptcy and Insolvency Law* (Irwin Law: Toronto, 2009) at pp. 180-81. As such, as Professor Wood notes at p. 82 the principle that a trustee "steps into the shoes" of the bankrupt and acquires the bankrupt's property "warts and all" "does not operate where bankruptcy or other legislation gives the trustee a power to subordinate or avoid certain property rights of third parties. In such cases, the trustee may have a better right to the asset than that held by the bankrupt."

85 This may constitute an oddity, but the danger of legislative intrusion outweighs any possible unfortunate consequences from the reversal of priorities. While the legislative measure could be an oddity, this would not be anomalous. As Professor Ian Fletcher writes in *The Law of Insolvency*, 4th ed. (London: Sweet & Maxwell, 2009) of the legislative history of British bankruptcy law at pp. 796-97 as follows:

> ...the legislative history is scarcely homogeneous, but is more accurately described as one of almost perpetual accretion and revision amid shifting socio-political influences. It must be submitted that the current position, in terms of policy and principle, is both muddled and confusing. It has resulted from the historic lack of a co-ordinated, thought-through approach to our law of credit, security and insolvency, amounting to a persistent failure...to address the essentially interlocking and inter-dependent nature of these vital areas. Consequently, the law has become beset by anomalies and inconsistencies, particularly concerning the operation of the pari passu principle, which are in some instances squarely at odds with commercial and social realities....

86 However, there is also jurisprudence and commentary in support of the Trustee's position. Doyle C.J., for the majority, in *Fresjac Pty. Ltd. v. Michael Mount PPB* (1995), 65 S.A.S.R. 334 (South Australia S.C.), approved of *N.A. Kratzmann.* This was cited by counsel to the Trustee, and reconciled many of the prior Commonwealth cases mentioned above *by distinguishing the issue of who possesses the right to bring a preference action, from the issue of the entitlement to the proceeds of such actions*. The Court in *Fresjac* was faced with the issue of to whom the proceeds of a s. 468 action by the liquidator, which renders dispositions of property after the commencement of winding up void, accrue. Doyle C.J. noted that the purpose of this section is identical to the purpose underlying preference actions, writing at pp. 341-42 "...both have an eye to the preservation of assets, to the preservation of the *status quo*, and to a later orderly distribution of assets among creditors, *subject to the rights of secured creditors*" (emphasis added).

87 In *Fresjac*, Doyle C.J. disagreed with Wright J.'s conclusion in *Bayley* that funds rendered void under s. 468 were at all times the property of the company and became subject to the charge once restored to the company. Doyle C.J. opined that such a characterization is artificial. The funds recovered were not the same funds, and title could not be revested, although this could occur in the case of land or identifiable chattel. Instead, the company would have a claim to recover an equivalent amount of money and its entitlement to the funds of s. 468 is a separate question from the right to impugn a transaction. Wright J.'s reliance upon the fact that a s. 468 action is "void", whereas a preference action is "void as against the liquidator" is, in Doyle C.J.'s view at p. 344, misplaced, as those words "control who may invalidate the preference, and to identify the liquidator as the person with that right, not to decide or determine who is entitled to the proceeds."

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

88 In this regard, Doyle C.J.'s analytic framework is noteworthy and worth setting out. It was noted that there is a "need to distinguish between the avoiding effect of the section, the location of the right to recover property disposed of by the company in a transaction avoided by the section, and the entitlement apart from that to rely upon the avoiding effect of the section." Doyle C.J. wrote at p. 344-45:

> The preference cases indicate, in my opinion, that the right to recover property disposed of in a transaction avoided as a preference belongs to a trustee in bankruptcy or liquidator, and property recovered by the exercise of that right will not vest in a secured creditor unless the exercise of the right should cause the revesting of title in specific property subject to a security.
>
> . . .
>
> ...the location of the right to assert voidness does not also determine the location of the right to proceeds recovered after the cancellation of a void transaction.
>
> . . .
>
> The mere right to assert or rely upon voidness cannot, as a matter of logic, give rise to a right to recover the property disposed of by the void transaction.
>
> The right to recover property disposed of in a transaction voided by s 468 is not property of the company, and the proceeds of the exercise of the right do not fall to be treated as property of the company caught by pre-existing charges or security but, in my opinion, specific property the subject of a charge or security will, if recovered, again be subject to that charge or security.
>
> On this approach, the right to recover property the disposition of which is avoided by s 468 is not a right to which a charge or security will attach.
>
> In addition, in my opinion money recovered as the result of the avoidance of a preference or because a payment is void is not to be regarded as property of a company to which a charge or security can attach.
>
> These conclusions emphasise the similarity between the preference provisions and s 468, despite the difference of language (void as against the liquidator and void) and despite the difference in the stages before liquidation to which they apply and the differences in the manner in which they operate.
>
> On the other hand they avoid the oddity (as some would see it) of a better result for a secured creditor in respect of a void payment, and the oddity of a remedy conferred for the purposes of a liquidation working for the benefit of the secured creditor. I do not pretend the result which I have reached is obvious, or that the contrary arguments are lacking in substance. [Emphasis added.]

89 In addition, in *Bank of New Zealand v. Essington Developments Pty. Ltd. & Ors* (1991), 5 A.S.C.R. 86 (N.S.W.S.C.), it was held that a secured creditor has the benefit of a liquidator's recovery of assets *in specie* over which a secured creditor has a charge. McLelland J. wrote at pp. 89-90:

> The position of a creditor with a charge over all the assets of a company and a receiver appointed by that creditor appears to be that if as a result of the avoidance of the transactions property is recovered in specie, then that property is included in the assets of the company which are subject to the charge and which therefore are available to the receiver for the benefit of the secured creditor. On the other hand, moneys which are recovered merely because payments have been avoided as preferencesdo not come within the general assets of the company available for the secured creditor and the receiver, but may be utilised by the liquidator for the purposes of the liquidation, and in particular for the benefit of unsecured creditors. [Emphasis added.]

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

90 In *Shapland Inc., Re* (1998), [2000] B.C.C. 106 (Eng. Ch. Div.) (Ch.D.), the court appears to be of the view that a trustee can pursue a preference action for which the benefits will accrue to the secured creditor (although in that case unsecured creditors would actually benefit as well) in stating at p. 110:

> Mr Goodison submitted that I should make no such order, on the ground that it would benefit only the bank, which was a secured creditor, and the power under s. 239 was conferred to benefit unsecured creditors, not secured creditors. I am very doubtful that this submission would be correct, even if the bank's claim were fully secured. However, on the facts of this case, it is not: the indebtedness of Shapland to the bank greatly exceeds the value of the property, so that a large part of the bank's claim is unsecured. Furthermore, the bank's security has been challenged, so that it would be wrong for me to proceed on the assumption that it is unquestionably a secured creditor. Lastly, the bank and the liquidator, who is financed in these proceedings by the bank, have agreed that after payment of the costs and expenses of the winding up, ten per cent of the proceeds of sale of the property are to go to unsecured creditors. Accordingly, the setting aside of the charge will benefit unsecured creditors, and the factual basis for Mr Goodison's submission is not made out.
>
> [Emphasis added.]

91 In *The Law of Insolvency*, Professor Fletcher would appear to provide some support for the Trustee's position, in claiming that the purpose of a preference action is to restore the situation to the *status quo ante*, and that the court may make such order to achieve that purpose as it sees fit, such that the idea that the proceeds of the action are not subject to the rights of secured creditors would be put into doubt. The new broad power to strike down fraudulent preferences, declare them void, and make any order that is just, was introduced in the 1985-86 reforms to the *Insolvency Act* in England. However, as previously noted, this form of relief is not replicated in the *BIA*.

92 Professor Fletcher also notes that the trustee's title is subject to various equities. He states at p. 246 that in the individual debtor context, whereby preferences can be declared void to restore the *status quo ante* (much like in the company debtor context), "the trustee is essentially a *successor* to such title as the bankrupt actually had at the time of his adjudication, including any limitation or imperfections in that title, and can enjoy no better position in relation to the property than did the bankrupt himself formerly" (emphasis in original; citations omitted).relying on *Johnson v. Smiley* (1853), 51 E.R. 1019 (Eng. Ch.); *Mapleback Ex p. Caldecott, Re* (1876), (1876-77) L.R. 4 Ch. D. 150 (Eng. C.A.); *Garrud, Re* (1880), 16 Ch. D. 552 (Eng. C.A.), per James L.J.; *Beeston, Re*, [1899] 1 Q.B. 626 (Eng. C.A.) at p. 610 per Lindley M.R.

93 More forcefully, he states at p. 247 "[a]ll such rights as might have been exercised by third parties prior to bankruptcy may be exercised after adjudication, and no action by the trustee can be effective to gain priority over such vested rights: unless the property can be disclaimed, the rights remain undisturbed" relying on *Anderson, Re*, [1911] 1 K.B. 896 (Eng. K.B.).

94 The Trustee's position is supported by additional academic literature. Rebecca Parry in "The Destination of Proceeds of Insolvency Litigation" (2002) 23(2) Comp. Law. 49, is concerned about the reversal of priorities that occurs where secured creditors cannot recoup the benefits of a preference action brought by a trustee under English law, especially given the anomaly that many preference actions could be pursued as misfeasance claims that do not give rise to the same result. This is because in the misfeasance context, amounts recovered are recoverable by secured creditors: See *Re Produce Marketing Consortium Ltd. (No. 2)*, [1989] B.C.L.C. 520 (Ch.D.); *Re Asiatic Electric Co. Pty. Ltd. (in liq.)* (1970), 92 WN (N.S.W.S.C.) at pp. 362-64. The remainder of her article deals primarily with the particular wording of the U.K. law.

95 Lee Eng Beng in "The Avoidance Provisions of the Bankruptcy Act 1995 and their Application to Companies" (1995)

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Sing J. Legal Stud. 597 notes that even with respect to preferential dispositions of specific property, the right to recover the assets vests in the liquidator such that a chargee cannot be entitled to the fruits of that recovery, especially since the process itself is intended for the benefit of unsecured creditors rather than secured creditors, as the latter exist outside of the bankruptcy regime. Nonetheless, Lee Eng Beng acknowledges the rights of secured creditors to trace monies at p. 632:

> While the property which has been disposed of may have been validly charged, the fact of it being wrongfully disposed of gives rise to the chargee's right under the general law to trace against the disponee and nothing more. The rights and remedies of secured creditors are conferred by the general law and they are not to be reinforced by statutory provisions designed to provide an equitable debt collection system for unsecured creditors. Of course, any right of a secured creditor which exists at general law would override any right of the liquidator or trustee in bankruptcy to proceed against the assets by virtue of any statutory provision, as the latter cannot be in a better position than the company or bankrupt, as the case may be. It follows that if a secured creditor has the right to recover the assets transferred away in breach of his security rights and the liquidator or trustee in bankruptcy recovers the assets pursuant to the statutory provisions, any recovery by the latter must be held for the benefit of the former in so far as they would have been recoverable by the secured creditor. [Emphasis added.]

96 Gerard McCormack in "Swelling Corporate Assets: Changing What is on the Menu" (2006) 6 J. Corp. L. Stud. 39 advances five reasons at pp. 56-57 for doubting the line of cases affirming *Yagerphone*, two of which are not peculiar to the English context:

> 1. *Yagerphone* gives rise to the unprincipled anomaly that certain preference actions can also constitute misfeasance actions, yet only in the latter case are payments subject to the rights of secured creditors.
>
> 2. Too much emphasis is placed on the liquidator's independent status which is merely an administrative convenience. He states that "the fact that proceedings are brought by the liquidator or administrator might be seen as *largely procedural*. The liquidator or administrator are not acting in their own individual rights but rather by virtue of the office they hold in relation to a particular company. In a broad sense the proceedings are brought on behalf of the company in question." (Citations omitted; emphasis added.)

97 Nancy Sanborn supports this interpretation, admittedly in the U.K. context. She writes in "Avoidance Recoveries in Bankruptcy: For the Benefit of the Estate or the Secured Creditor?" (1990) 90 Colum. L. Rev. 1376 at 1399-1400 supports the above authors writing:

> The proposition that all amounts recovered must be available for administrative expenses and unsecured claims and interests, without recognition of any security interest in the recovery because avoidance powers are exercised for the benefit of the estate, fails to distinguish between two separate functions of the bankruptcy process. One function is to maximize the value of the pool of assets to which all claimants and interest holders will look for payment. Transfers are avoided, then preserved or recovered, to serve this function. The estate benefits from the exercise of these powers even if a creditor possesses a security or beneficial interest in the property.
>
> A separate issue, how entitlements to the accumulated pool of assets should be allocated, should be resolved primarily by nonbankruptcy law. A secured creditor should be afforded the same protections that would have been available to it under state law if no bankruptcy had ensued. [Citations omitted].

Analysis

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

98 The foregoing review of jurisprudence confirms the submission of the Trustee, namely, that the jurisprudence is unclear and inconsistent. However, it seems to me that, with a consistent application of (i) insolvency principles; and (ii) personal property security principles, the jurisprudence can be reconciled.

99 Both the Trustee and Air Canada make extensive reference to the English decision of *Yagerphone*. *Yagerphone* has been cited by some Canadian courts to stand for the proposition that secured creditors have no claim to the proceeds of a preference action.

100 Counsel to the Trustee submits that, read properly, the holding in *Yagerphone* is, in fact, narrower. I agree.

101 In *Yagerphone*, the court considered a priority dispute between the liquidator and a debenture holder over the proceeds of a preference action. In reaching its conclusion, the court focussed on the nature of the debenture holder's security. The court observed that at the time the preference was given, the debenture holder's charge was still floating and therefore had not attached to the assets of *Yagerphone*:

> On January 17, 1933, the creditor to whom the money was paid and from whom the money was recovered was a creditor Yagerphone, Ld. When Yagerphone, Ld. paid to the creditor the 240*l* 11 s. 2 d. that sum, in my judgment ceased to be the property of Yagerphone, Ld. The payment to that creditor could not have been attacked or impeached, unless within three months from the date of payment, the liquidation of Yagerphone, Ld. had begun, and, in my judgment, at the date when the security contained in the debenture crystallised, the sum of 2401 11 s. 2 d. was not the property of Yagerphone, Ld....

102 As counsel to the Trustee points out, at the time the preference was given by the debtor, the assets transferred were not subject to the debenture holder's security and when the debenture holder's security was crystallized, the debtor's estate did not extend to the assets that had already been transferred on account of the preference. On this basis, the court found that the debenture holder's security did not attach to those assets when they were eventually returned to the estate.

103 Counsel to the Trustee goes on to submit that, from a policy perspective, the holding in *Yagerphone* is not unreasonable, as, in particular, because the debenture holder's security was floating it had no claim to the assets. When these assets were brought back into the estate, the court's decision that all creditors share in those assets is consistent with the fact that the "fraud" occurred against all of the debtor's creditors.

104 In *Mohawk Sports Equipment* Houlden J. (as he then was) applied *Yagerphone* in circumstances which involved a floating charge that had not crystallized. The court held that the proceeds "cannot be claimed by the debenture holder as it was not part of the property of the debtor company at the time the security was crystallized".

105 Counsel to the Trustee further submits that in subsequent cases, the holding in *Yagerphone* has been summarized more broadly to apply to secured creditors generally. Reference was made to *Maybank Foods* where at paragraph 2 the court stated:

> It is conceded by the respondent that the monies recoverable by a trustee from a creditor who has been preferred do not

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> become part of the general assets of the bankrupt estate subject to the claims of secured creditors but rather are received by the trustee subject to a trust in favour of the creditors represented by the trustee: Re Yagerphone, Ltd. (1935) 1 Ch. 392 (Ch. D.).

106 It is the Trustee's submission that the concession in *Maybank Foods* goes beyond the ratio in *Yagerphone* as the reasoning in *Yagerphone* does not necessarily follow the circumstances in which a secured creditor holds a fixed charge over the assets of the debtor. Counsel goes on to submit that where the secured creditor holds a fixed charge, the policy considerations are different. Unlike a floating charge, a fixed charge gives the secured creditor a property interest in the debtor's collateral that attaches at the time the charge is granted. Reference was also made to the recent decision of the Supreme Court of Canada in *Innovation Credit Union v. Bank of Montreal*, [2010] 3 S.C.R. 3 (S.C.C.), which, in turn referred to the case of *Royal Bank v. Sparrow Electric Corp.*, [1997] 1 S.C.R. 411 (S.C.C.), in which the distinction between a fixed and a floating charge was explained at para. 46:

> The critical significance of the characterization of an interest as to being fixed or floating, of course, is that it describes the extent to which a creditor can be said to have a proprietary interest in the collateral. In particular, during the period in which a charge over inventory is floating, the creditor possesses no legal title to that collateral....However, if a security interest can be characterized as a fixed and specific charge, it will take priority over a subsequent statutory lien or charge; in such a case, all that the lien can attach to is the debtor's equity of redemption in the collateral....

107 The distinction between a fixed and floating charge and considering whether the charge has crystallized is not a new concept. The issue was also live in *Maybank Foods*.

108 In *Maybank Foods*, the respondent was a secured creditor of the estate. The estate had been engaged in three actions in Nova Scotia referred to as the Food Group Litigation, the Provisioners Litigation, and the Seaway Litigation, respectively. The trustee requested orders that the proceeds from such litigation were the property of the estate free and clear of the secured claim of the respondent.

109 At para. 2 of the decision, Saunders J. referenced the Provisioners Litigation and the Seaway Litigation as involving claims against preferred creditors. It was in this context that the concession was made by the respondent that the monies recoverable by the trustee would not form part of the general assets of the estate.

110 However, at para. 3 of the decision, Saunders J. addresses the claim against Food Group:

> The claim against Food Group was in respect of an account receivable. Food Group unsuccessfully defended the claim of the trustee on the basis of set-off. It was held that in the circumstances there was no mutuality, because at the time the bankrupt became indebted to Food Group, the receivable was being claimed by another secured creditor, Citibank under a crystallized charge. Upon the bankruptcy, the receivable of Food Group vested in the trustee subject to the secured claim of the predecessor in title of the respondent. Accordingly, the respondent may assert a right to the proceeds of the Food Group Litigation unless defeated by some principle or a statute. The situation is different from the other two actions where the respondent had no charge on the property being claimed by the trustee and the trustee was asserting a statutory right unavailable to the respondent. Here, the respondent has a charge on the receivable being claimed from Food Group. The trustee argued the respondent could not have successfully claimed against Food Group because Food Group would have been entitled to a set-off which in its submission made the situation analogous to the other two actions. I cannot accept that argument. The action of Citibank in crystallizing its charge foreclosed the Food Group from

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

successfully asserting the set-off defence. In my opinion, the respondent who also had a charge against that asset could assert along with the trustee that set-off is not available notwithstanding the charge to the respondent may not have crystallized before the claim of Food Group against the bankrupt arose. There is, in my opinion, no basis in statute or principle preventing the respondent from claiming the net proceeds of the Food Group action.

111 Justice Saunders endorsed the record as follows:

Net proceeds (after deducting of costs and disbursements) of Food Group Litigation are subject to the secured claim of the respondent. Proceeds of the Provisioners Litigation and the Seaway Litigation are free and clear of such claim. The costs and disbursements with respect to the Provisioners Litigation and the Seaway Litigation should not be paid out of the assets of the estate that are subject to the secured claim of the respondent unless that claim has been satisfied in full. Costs to the trustee and to the respondent out of the estate on a solicitor-and-client basis.

112 The distinction between a fixed charge and a floating charge was also the subject of the decision of the Nova Scotia Court of Appeal in *S-Marque*.

113 In *S-Marque*, the Nova Scotia Supreme Court found that the proceeds of a preference action will inure to the benefit of the unsecured creditors for two reasons:

(a) first, the court relied on the decision In *Yagerphone*; and

(b) second, the court cited a number of decisions to the effect that only a trustee can void a preference action.

114 The decision was affirmed on appeal but the Court of Appeal decided the priority issue for different reasons. The Court of Appeal focussed on the fact that the secured creditor held a floating charge and that the preference occurred "before the debenture crystallized". As counsel to the Trustee reasoned, as in *Mohawk Sports Equipment*, the court determined the matter on the basis that the secured creditor "never had a fixed charge on these assets when the debenture crystallized".

115 Counsel to the Trustee submits that the court considered the priority rights of secured creditors to proceeds from a preference action and that in the 2000 British Columbia Supreme Court decision, in *ASI Acoustical Supplies Inc., Re*, the court squarely addressed the fact that only a trustee can make a claim for fraudulent preference under the *BIA*. Counsel to the Trustee submits that the court noted that, while the *BIA* gave that right to the trustee, it did not change the priority rights of creditors to the proceeds.

116 In my view, the *ASI Acoustical* decision does not stand for the proposition put forth by counsel to the Trustee.

117 The matter came before the court by way of an appeal by the trustee for *ASI Acoustical* from a decision of the Registrar, refusing to approve the payment to the trustee of its fees and disbursements. The Bank of Nova Scotia took security in the form of a general security and assignment of accounts receivable. The security was ultimately assigned to Mr. Willsie.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

118 Prior to bankruptcy, ASI bought materials from Winrock and owed Winrock around $56,000. Winrock then bought a substantial amount of ASI inventory. Winrock owed ASI approximately $45,000 for the inventory, but resisted payment claiming a right of "contra account". The trustee wrote to Winrock noting that a subsidiary company Hubcity owed part of the money to ASI and therefore the claim of "contra account" could not be made out. The trustee also alleged that the Winrock claim was a preference on the basis that the sole reason Winrock bought the inventory from ASI was to reduce its claim in the bankruptcy.

119 Ultimately, the matter was settled. The position of the trustee was that the matter was settled on the basis that the purchase of inventory was a fraudulent preference under the provisions of the *BIA* and because this remedy is not available to the secured creditor, the money obtained from the settlement was an asset of the estate.

120 The registrar held that there was no dispute that the account receivable from Winrock was covered by the security interest, and the fact that there were negotiations and the claim was eventually paid because the trustee alleged that there was a fraudulent preference, did not convert the asset into some other kind of asset not subject to the security interest. The registrar therefore found that the proceeds of the claim should not appear on the statement of receipts and disbursements as an amount available to the estate.

121 At the hearing before Martinson J. on appeal, the creditors disputed the characterization of the transaction as a fraudulent preference. The only evidence before the registrar was that there had been an allegation of a fraudulent preference by the trustee, that no claim had been commenced by the trustee and that there was a negotiated settlement with Winrock.

122 Justice Martinson concluded that it was open to the Registrar, based on the material before her, to conclude that the settlement monies were accounts receivable and subject to the security interest. It was in this context that the reference which was cited by counsel to the Trustee: "[i]n any event, the fact that only a trustee can make a claim alleging a fraudulent preference does not change the priority position of a secured creditor" was made.

123 From my reading of *ASI Acoustical*, the significant point is that the court recognized that in the circumstances of that case, the fact that a fraudulent preference action had commenced, did not preclude the ability of a secured creditor to realize on security or to follow the proceeds from security in accordance with the specific security agreement.

124 This position is again recognized in *Agricultural Credit Corp. of Saskatchewan*, where the court noted:

> Monies owing to a bankrupt, when collected by the trustee continue to be the property of the bankrupt and continue to be subject to the existing security interests. This includes monies realized through the efforts of the Trustee. (*Holy Rosary Parish (Thorold) Credit Union Limited v. The Premier Trust Company*, (1965), S.C.R. 503); Re Stadnik (Bankrupt) (1991), 90 Sask. R. 12 (QB); Re Moore (Bankrupt) (1989), 79 Sask. R. 63 (C.A.).

125 Counsel to the Trustee submits that the conclusion of the court in *ASI Acoustical* is consistent with a long line of jurisprudence that holds that monies recovered by the trustee are subject to the rights of secured creditors.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

126 It seems to me that this statement is too broad. In my view, the focus has to be on whether or not the secured creditor had rights in the collateral at the time of the suspect transaction.

127 In *Yagerphone*, the debenture holder's security was floating and the debenture holder had no claim to the assets recovered by the liquidation.

128 In *Mohawk*, the floating charge had not crystallized.

129 In *Maybank Foods*, the court recognized that the secured creditor could have a claim, under a crystallized charge.

130 In *S-Marque*, the secured creditor held a floating charge and the preference "occurred before the debenture crystallized".

131 In *ASI Acoustical*, the court concluded that it was open to the registrar to conclude that the settlement monies were accounts receivable and subject to the security interest.

132 In *Agricultural Credit Corp.*, monies owing to a bankrupt on account of shares in the Saskatchewan Wheat Pool, when collected by the trustee continued to be the property of the bankrupt and subject to the existing security interest. It was not a preference action.

133 *Yagerphone* arose in the context of a regime dominated by fixed and floating charge debentures. In Ontario, since the enactment of the *Personal Property Security Act*, R.S.O. 1990, c. P-10 ("*PPSA*"), security agreement do not generally refer to fixed and floating security, but the concepts of fixed and floating charges is still recognized. (See *Bank of Montreal v. Innovation Credit Union, supra.*)

134 Under the *PPSA* regime, the issue that has to be analyzed is whether or not the debtor had the ability to transfer the collateral charged by the security agreement to a third party free and clear of the security interest.

135 It seems to me that, if the debtor was in a position to transfer the collateral free and clear of the interest of the secured party, the *Yagerphone* analysis and conclusions remains valid. Conversely, if the collateral remains subject to the claims of a secured party, the secured party may retain the ability to enforce its rights as against the collateral or any proceeds arising from the collateral.

136 It seems to me that this outcome is consistent with the views of Doyle C.J. in *Fresjac Pty. Ltd. (In liq), Re, supra*,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

which are summarized at [86] - [88] above. I am in agreement with the views and conclusions set out by Doyle C.J. in that case. The outcome is also consistent with the approach of Lee Eng Beng in the emphasized part of [95]. The outcome is also consistent with the approach outlined by Gerald McCormack at [96] and by Nancy Sanborn at [97].

137 Section 95 of the *BIA* makes it clear that a transaction that is declared to be a preference is void as against the trustee. This, in my view, makes it clear that it is the trustee that has the cause of action to declare a preference to be void. But, as stated in *Fresjac Pty. Ltd. (In Lq.), supra*, the issue of who possesses the right to bring a preference action does not necessarily determine entitlement to proceeds.

138 The s. 95 cause of action remedy is designed to ensure that there is *pari pasu* treatment as between unsecured creditors. The recipient of a preferential transfer is not entitled to keep the preferential proceeds if the elements of s. 95 are proven. The subject of the preference is returned to the estate but subject to the rights of secured creditors. In the words of Lee Eng Beng at [95] above, "...if a secured creditor has the right to recover the assets transferred away in breach of his security rights and the liquidator or trustee in bankruptcy recovers the assets pursuant to the statutory provisions, any recovery by the latter must be held for the benefit of the former in so far as they would have been recoverable by the secured creditor."

139 Ultimately, distributions of the bankrupt's estate are made pursuant to s. 136 of the *BIA* and again are preferenced with the *proviso*: "subject to the rights of secured creditors".

140 The ability of a trustee to recover monies for the estate for the benefit of creditors is, in its entirety, subject to the rights of secured creditors. If a secured creditor still has rights in the collateral, there is nothing in the fraudulent preference remedy regime that would appear to preclude the secured creditor from exercising its rights. To the extent that the secured party has rights in the collateral and has a remedy against the collateral in the hands of the third party, such remedy and the resulting priority is not, in my view, altered because a trustee embarks on a preference action.

141 This analysis is consistent, in my view, with the structure of the *BIA*. The *BIA* respects the rights of secured creditors. Over time, modifications have been made to the statute to harmonize it with statutes providing for remedies to secured creditors. But, the priority regime has not changed. If the secured creditor has rights to the collateral, the secured creditor takes priority over the claims of unsecured creditors.

142 Counsel to the Trustee also referenced *Thorne Ernst & Whinney and Gazzola, Re* in connection with an explanation as to the interplay of the preference provisions and priority distributions. The case involved a dispute between a landlord of a bankrupt tenant and the trustee. The landlord appealed from a judgment holding that a distress levied by the landlord was fraudulent and void as a preference as against the lessee's trustee.

143 Justice Hickson opined that under the *BIA*, the trustee is charged with gathering the assets of the bankrupt for the benefit of the creditors and then distributing those assets pursuant to the scheme of distribution set out in s. 136 of the Act. In the context of a preference, the trustee can bring an application under s. 95 and, if successful, the landlord would be required to pay over the proceeds of the transaction to the trustee. Hickson J.A. went on to state that "in due course, depending on the claims of secured creditors and those standing in priority to the landlord under the scheme of distribution established by s. 136 of the Act, if there are sufficient assets in the estate the landlord will then receive payment pursuant to the provisions of

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

that section".

144 Counsel to the Trustee went on to submit that in a similar case involving a preference action against the landlord, the Court of Appeal for Ontario considered and followed *Gazzola* and, citing concurring reasons in *Gazzola*, the court noted that the preference proceeds are to be distributed in accordance with the scheme in s. 136, which is subject to the rights of secured creditors: See *Canadian Imperial Bank of Commerce v. Canotek Development Corp., supra.*

145 In reviewing both the *Gazzola* decision and the *Canotek* decision, I do not see any finding that it is inconsistent with the views that I have expressed above. Simply put, a trustee can pursue a preference action. If the trustee recovers proceeds, they are to be distributed in accordance with s. 136. The reference "which is subject to the rights of secured creditors" restates the position that if secured creditors have rights in the collateral, such priority is to be respected by the trustee.

146 I do not read into the words "subject to the rights of secured creditors" as putting the position of the secured creditor at an even higher level. Specifically, I do not interpret this phrase as enabling a secured party to step into and occupy the position of the trustee. The trustee's rights are established under the *BIA*. The rights of a secured creditor are provided for in security agreements and the *PPSA* and the process by which realization takes place is provided for in court orders, security agreements, the *PPSA*, and in this case, the *BIA*.

147 Counsel to the Trustee also raises a number of policy considerations underlying the *BIA* in support of its position. Specifically, counsel submits that the proposition that unsecured creditors have priority to the proceeds of a preference action may lead to anomalous results insofar as an insolvent person could defeat the rights of a secured creditor by simply granting a preference immediately prior to assigning itself into bankruptcy. The consequences of reversing the preference would be such that the proceeds would benefit unsecured creditors. Counsel submits that it cannot be correct that by dealing with collateral in a preferential fashion, an insolvent person can alter bankruptcy priorities and nullify a secured creditor's exclusive claim to that collateral.

148 This theme has also been recognized in certain academic writings. For example, Professor Fletcher, in *The Law of Insolvency*, provides support for the trustee's position. In stating that the purpose of a preference action is to restore the situation to the *status quo ante*, he puts into doubt the notion that the proceeds of the action are not subject to the rights of secured creditors.

149 The answer to the concern posed by counsel to the Trustee is not easy. To some extent, secured creditors are protected by an ability to take action for recovery as a result of the provisions of their particular security agreement. The *BIA* does not extinguish the rights of secured creditors to follow collateral if circumstances are such that it is lawful and appropriate to follow the collateral.

150 If, for example, the transaction is out of the ordinary course of business or, if the recipient is on notice that it is an improper transaction, the secured party may very well have rights to recover the collateral or proceeds. However, if the debtor was in a position to lawfully dispose of the collateral free and clear of the security interest, and has done so, it could very well be that the only recovery for the secured creditor would be to participate in a distribution to unsecured creditors under s. 136 of the *BIA*. This, of course, would happen if the secured creditor declares part of its indebtedness to be unsecured. This outcome is a consequence, however, not of some realignment or readjustment of priorities under the *BIA*, but

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

rather, it is a consequence of a factual scenario under which the debtor could lawfully transfer the collateral. This outcome is, in my view, consistent with the *Yagerphone* analysis.

151 In the final analysis, I have concluded that:

(i) a trustee in bankruptcy (or a section 38 *BIA* assignee) is the only party that can bring a preference action in bankruptcy proceedings;

(ii) the proceeds recovered by the trustee are brought into the estate;

(iii) distribution under the *BIA* is subject to the rights of recovery of secured creditors;

(iv) the bringing of a preference action and the recovery of proceeds does not preclude secured creditors from pursuing whatever remedies they may have under the provisions of the security agreement and relevant statutes.

152 There is also nothing, in my view, that would preclude a secured creditor from pursuing appropriate remedies in conjunction with the trustee pursuing its remedies. For example, at the outset of a proceeding, when investigations may not have been complete, it may be difficult to pinpoint a specific remedy. This would likely require a cooperative effort as between secured creditors and a trustee and some sort of formal agreement to recognize how matters are to be prosecuted and how proceeds of litigation are to be allocated. An example of such an arrangement is referenced in *Re Sharpland Inc., supra.*

153 Overall, the objective of the preference action is to void preferential transactions for the benefit of creditors, while recognizing legitimate security interests.

154 Air Canada has taken issue with the role of the Trustee in this case and makes specific reference to s. 13.4 of the *BIA* which explicitly contemplates that a trustee may act for or assist a secured creditor in certain circumstances. These submissions from counsel to Air Canada have been put forth in an effort to persuade the court that the Trustee should, in this case, be following the requirements of the *BIA*. Counsel to Air Canada also questions whether this court has the jurisdiction to allow a trustee to pursue a *BIA* preference action within the context of a *CCAA* proceeding.

155 The *CCAA* does address the issue of preferences and transfers under value. Section 36.1(1) provides that the preferential provisions of the *BIA* apply, with any modifications that the circumstances require, in respect of a compromise or arrangement, unless the compromise or arrangement provides otherwise.

156 In this case, there is no compromise or arrangement that has been proposed to creditors, nor is it expected to flow from the type of proceeding that is currently before the court.

157 This leads to a straight-forward conclusion, in my view, that the preference action should proceed under the *BIA*.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

158 However, this conclusion leads to the subject of coordination of proceedings under the *CCAA* and the *BIA*. This subject was addressed by the Supreme Court of Canada in *Ted Leroy Trucking Ltd., Re*, [2010] 3 S.C.R. 379 (S.C.C.).

159 In *Century Services*, the majority noted that the *CCAA* is a flexible statute designed to preserve the value of a business as a going-concern through a court supervised re-organization. In that case, a re-organization under the *CCAA* had failed and the Crown brought a motion for payment of its statutory deemed trusts pursuant to s. 222(3) of the *Excise Tax Act*, R.S.C. 1985, c. E-15. Brenner C.J. denied the motion and allowed the assignment of the company into bankruptcy. The British Columbia Court of Appeal had found that while the Crown could not seek repayment of GST source deductions in priority to other claims during a *CCAA* or *BIA* proceeding, it could do so after the reorganization efforts had failed and prior to the commencement of a *BIA* proceeding, such that the trial judge was bound to allow the motion and apply the provisions of the *Excise Tax Act*. The majority of the Supreme Court rejected this reasoning noting at para. 47 that an interpretation giving the *Excise Tax Act* priority over the *CCAA* would result in a "strange asymmetry" which would encourage statute shopping.

160 Justice Deschamps, writing for the majority, rejected the contention that Brenner C.J. had exceeded his authority by continuing the stay of the Crown's GST claims while temporarily lifting the general stay to allow for the assignment in bankruptcy. Section 11 of the *CCAA*, subject to certain restrictions, provides the court with broad authority to make an order that is appropriate in the circumstances — a power which is not subject to explicit temporal limitations and is buttressed by the court's inherent jurisdiction, as well as s. 20 (now s. 42) of the *CCAA*.

161 At para. 76 of *Century Services*, it is noted that the *CCAA*'s objectives permit for a bridge between the *CCAA* and *BIA* proceedings. As recently noted by the Supreme Court of Canada regarding section 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*. <u>Section 20 clearly indicates the intention of Parliament for the *CCAA* to operate in tandem with other insolvency legislation, such as the *BIA*</u>.

162 Further, Deschamps J. wrote at para. 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.

163 This passage from *Century Services* clearly states, in my view, that the courts should be taking a pragmatic approach in determining issues which arise in proceedings where the *CCAA* overlaps with the *BIA*. This is one such proceeding. The overall objective should be to create a system under which the court can review transactions entered into between the debtor

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

and creditors in the period just prior to formal insolvency proceedings. The policy should be to ensure that there is an appropriate review mechanism in place to challenge transactions that are not consistent with ordinary course activities and have had the effect of unfairly transferring value to a third party during the review period. It seems to me that the *CCAA* can operate in tandem with the *BIA* in an effort to return matters to the *status quo*.

164 Applying the principles of *Century Services*, it seems to me, that the preference motion should proceed in the *BIA* proceedings. However, in my view, this can be accomplished by a procedural order in *CCAA* proceedings which transitions the matter to the *BIA*. There is no necessity or principled reasons to require the trustee to start from square one. This outcome is consistent with my endorsement of February 24, 2010 at paras. 29 - 32.

165 It is also appropriate, at this time, and in view of the contemplated continuation of the preference motion, that proceedings be regularized with the Trustee taking the necessary steps to comply with its obligation under the *BIA*.

Disposition

166 In the result, a declaration shall issue to incorporate the conclusions set out at [151] which, for ease of reference, is repeated:

> (i) a trustee in bankruptcy (or a Section 38 *BIA* assignee) is the only party that can bring a preference action in bankruptcy proceedings;
>
> (ii) the proceeds recovered by the trustee are brought into the estate;
>
> (iii) distribution under the *BIA* is subject to the rights of recovery of secured creditors;
>
> (iv) the bringing of a preference action and the recovery of proceeds does not preclude secured creditors from pursuing whatever remedies they may have under the provisions of the security agreement and relevant statutes.

167 I have also concluded that, if it is determined that the transaction is void as being a preference, at that point, the appropriate determination can be made as to which party, be it either the trustee or the secured party, is entitled to the proceeds. This determination should be based on whether the secured party has the right to recover the assets transferred, or any proceeds resulting from such transfer. In my view, it is premature to comment on this issue, in the circumstances of this case, as the factual record has not been fully determined.

168 In the context of this particular case, if it is the intention of the secured party to work in conjunction with the Trustee and for the Trustee to utilize the preference provisions, the appropriate notifications should be provided in accordance with s. 13.4 of the *BIA* and the Trustee should move forward to fulfill its statutory obligations in the conduct of its administration.

169 To the extent that further directions are required in respect of this endorsement, the parties may contact the Commercial List Office to set up a 9:30 a.m. appointment.

Order accordingly.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 9

2011 ONSC 5820
Ontario Superior Court of Justice [Commercial List]

Verdellen v. Monaghan Mushrooms Ltd.

2011 CarswellOnt 11612, 2011 ONSC 5820, 207 A.C.W.S. (3d) 553, 97 C.P.R. (4th) 196

Jack Verdellen, Applicant and Monaghan Mushrooms Ltd., Pricewaterhousecoopers Inc., Respondents

Newbould J.

Heard: September 27, 2011
Judgment: October 7, 2011
Docket: CV-11-9162-CL

Proceedings: additional reasons at *Verdellen v. Monaghan Mushrooms Ltd.* (2011), 2011 ONSC 6506, 2011 CarswellOnt 12810 (Ont. S.C.J.)

Counsel: Patrick J. Cotter, for Applicant
Paul J. Martin, Sarah J. Armstrong, for Respondent, Monaghan Mushrooms Ltd.
T. Van Klink, for Respondent, PricewaterhouseCoopers Inc.

Subject: Intellectual Property

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Intellectual property --- Patents — Transfer of interest — Assignment

Invention was said to have occurred while JV was employed by R Ltd. — JV claimed ownership under agreement between him and R Ltd. said to have been negotiated orally and put in writing dated December 1, 2008 — Business of R Ltd. was sold to M Ltd. — Applicant JV applied for declaration that he was owner of certain patent rights outside of North America for invention which involved method of inhibiting green mould in mushrooms — Application dismissed — It was declared that purported agreement of December 1, 2008 between JV and R Ltd. and any purported oral agreement between them regarding same matters, was void as against M Ltd. as bona fide purchaser for value from R Ltd. without notice of any such agreements — It was clear from evidence that prior to closing of purchase of business by M Ltd. from R Ltd., M Ltd. was never provided, nor did it learn of, any information of JV's alleged interest in patent, in spite of M Ltd.'s due diligence process.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Table of Authorities

Cases considered by *Newbould J.*:

Apotex Inc. v. Wellcome Foundation Ltd. (2000), 2000 CarswellNat 2643, 195 D.L.R. (4th) 641, [2001] 1 F.C. 495, 2000 CarswellNat 3414, 10 C.P.R. (4th) 65, 186 F.T.R. 274 (note), 262 N.R. 137 (Fed. C.A.) — considered

DiGuilo v. Boland (1958), [1958] O.R. 384, (sub nom. *Di Guilo v. Boland)* 13 D.L.R. (2d) 510, 1958 CarswellOnt 102 (Ont. C.A.) — considered

Grant Forest Products Inc., Re (2009), 58 C.B.R. (5th) 127, 2009 CarswellOnt 6099 (Ont. S.C.J. [Commercial List]) — referred to

Grant Forest Products Inc., Re (2010), 276 O.A.C. 43, 101 O.R. (3d) 383, 67 C.B.R. (5th) 23, 2010 CarswellOnt 3001, 2010 ONCA 355, 318 D.L.R. (4th) 598 (Ont. C.A.) — considered

R. Griggs Group Ltd. v. Evans (No. 2) (2004), [2004] EWHC 1088, [2005] Ch. 153, [2005] 2 W.L.R. 513, [2004] F.S.R. 48 (Eng. Ch. Div.) — referred to

Society of Composers, Authors & Music Publishers of Canada v. Canadian Assn. of Internet Providers (2004), (sub nom. *SOCAN v. Canadian Assn. of Internet Providers)* 240 D.L.R. (4th) 193, 2004 SCC 45, 2004 CarswellNat 1919, 2004 CarswellNat 1920, 322 N.R. 306, (sub nom. *Socan v. Canadian Assn. of Internet Providers)* [2004] 2 S.C.R. 427, (sub nom. *SOCAN v. Canadian Assn. of Internet Providers)* 32 C.P.R. (4th) 1 (S.C.C.) — referred to

Tucker v. Aero Inventory (UK) Ltd. (2011), 2011 CarswellOnt 8476, 2011 ONSC 4223, 80 C.B.R. (5th) 1 (Ont. S.C.J. [Commercial List]) — referred to

Statutes considered:

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3
s. 38 — considered

s. 95 — considered

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — referred to

s. 36.1 [en. 2007, c. 36, s. 78] — referred to

Patent Act, R.S.C. 1985, c. P-4
Generally — referred to

s. 49(2) — considered

s. 50(2) — considered

s. 51 — considered

Patents Act, 1977, c. 37
Generally — referred to

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Patents Act 1990, No. 83, 1990
Generally — referred to

Rules considered:

Patent Rules, SOR/96-423
Generally — referred to

s. 59 — considered

APPLICATION by JV for declaration that he was owner of certain patent rights outside of North America for invention which involved method of inhibiting green mould in mushrooms.

Newbould J.:

1 The applicant Jack Verdellen applies for a declaration that he is the owner of certain patent rights outside of North America for an invention which involves a method of inhibiting green mould in mushrooms. The invention was said to have occurred while Mr. Verdellen was employed by Rol-land Farms Limited ("Rolland"). Mr. Verdellen claims ownership under an agreement between him and Rolland said to have been negotiated orally and put in writing dated December 1, 2008

2 Rolland applied for protection under the CCAA on December 10, 2008 and the Initial Order was made that day. A sale process in the CCAA proceedings was undertaken and the respondent Monaghan Mushrooms Ltd. ("Monaghan") purchased the business of Rolland under an agreement of purchase and sale dated September 21, 2009. That agreement closed on November 6, 2009 under an amended vesting order dated October 27, 2009. Monaghan takes the position that Mr. Verdellen cannot establish an agreement between him and Rolland and that Monaghan acquired the patent rights in question in good faith for value without notice of any rights of Mr. Verdellen to the patent rights under a court ordered process that provided Monaghan with a vesting order. Monaghan also takes the position that if there were an agreement, it would be void under s. 51 of the Patent Act and as a preference under s. 95 of the BIA.

Existence of agreement

3 Mr. Verdellen's evidence is that he commenced work at Rolland as a consultant in 1994- 1995 and became Vice-President, Production in November 2006. His evidence is that at that time, he orally agreed with Mr. Vander Pol, the president and chief executive officer of Rolland, that he would own the rights to whatever he invented provided that Rolland was able to get the benefit of the rights in North America. In July 2007 he and another Rolland employee invented materials and methods to be used for the prevention and/or control of green mould in the production of mushrooms.

4 Mr. Verdellen's further evidence is that in late 2008 he told Mr. Vander Pol that he intended to leave the company and go back to Holland but that in order to keep him, a proposal was made by Rolland in writing in a document dated December 1, 2008 which confirmed his ownership of the invention and the patent rights outside of North America. The contractual rights claimed by Mr. Verdellen are contained in a document dated December 1, 2008 signed by Mr. Vander Pol on behalf of Rolland and by Mr. Verdellen. Mr. Verdellen is unable to say when he signed the document. He has never produced the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

original document. The date of December 1, 2008 is three days after BMO delivered a notice of intention to enforce security against Rolland and shortly before Rolland commenced its CCAA proceedings.

5 The December 1, 2008 document includes the following:

> The information below summarizes how the R&D findings are to be handled to the mutual benefit of Rol-land Farms and Jack Verdellen:
>
> It is jointly recognized that the R&D activities carried on to date would not have been possible without the combined efforts of Jack Verdellen, Nader Gheshlaghi and Rol-land Farms. Jack has provided the ideas, Nader has carried out the research and Rol-land has funded the activities.
>
> . . .
>
> Given Jack's contributions to Rol-land's operations over the past 3 years, and given Rol-land's contributions to the R&D program over that same time period, Rol-land and Jack agree to the following settlement:
>
> • Rol-land will transfer the world rights to "Pepe" to Jack to continue with a world application.
>
> • Rol-land must retain the North American rights to "Pepe" in order to protect its competitive advantage.
>
> . . .
>
> This agreement is not transferable without the written consent of both Jack Verdellen and Rol-land Farms

6 Monaghan refers to several pieces of evidence and suspicious circumstances to assert that there was never any agreement between Mr. Verdellen and Rolland. It also asserts that there was no agreement on all essential terms, there was no consideration flowing to Rolland and there is no evidence of communication of any acceptance by Mr. Verdellen to Rolland.

7 This is an application. In my view there are too many contested factual issues to determine at this stage whether or not there was a binding agreement between Mr. Verdellen and Rolland. During the course of the oral argument I made that determination.

8 What remains is whether on the assumption that a binding agreement as claimed by Mr. Verdellen was made, there are any grounds available to support a declaration of the rights of the parties.

Purchase agreement and vesting order

9 The agreement of purchase and sale dated September 21, 2009 between Rolland and Monaghan closed on November 6, 2009. Approval to the agreement and a vesting order was made on October 5, 2009 and an amended approval and vesting order was made on October 27, 2009. Mr. Verdellen takes the position that the agreement of purchase and sale did not transfer to Monaghan the rights to the patent outside of North America and further takes the position that if necessary, the vesting order should be amended to make that clear.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

10 The agreement of purchase and sale provided for the sale of a number of assets, including the Intellectual Property. Intellectual Property was broadly defined as follows, in part:

> "Intellectual Property" means all of the intellectual property of whatever nature and kind owned by or licensed to the Vendor in respect of or associated with the Business as presently constituted, including all domestic and foreign trademarks,... and all patents... whether registered or unregistered, and all applications for registration thereof, and... inventions...; in which, for further certainty, includes... all products, processes and inventions developed by or for or used by the Business in connection with the control or eradication of green mould disease, including any patent applications for strains of biological control for green mould for the treatment of spawn;

11 It is to be noted that this definition of Intellectual Property is in respect of the "Business". Mr. Verdellen asserts that the definition of Business in the agreement of purchase and sale excludes any patent rights outside of North America. Business is defined in the agreement to have the meaning set out in the recitals. The recital refers to the order under which the Monitor was authorized and directed to conduct a sale process for offers for the sale "of the mushroom production and marketing business" of Rolland. Mr. Verdellen asserts that because Rolland only carried on its mushroom business in North America, any patent rights outside of North America were not included in the agreement of purchase and sale.

12 I cannot accept that contention. The definition of Business in the agreement of purchase and sale as being "the mushroom production and marketing business" of Rolland by its language did not restrict that business to any particular locality or jurisdiction. The business of Rolland included making patent applications for the invention in question, being an invention to control or eradicate green mould disease. Prior to the sale, Rolland had filed an international PCT application, which was an application to commence exploiting patent rights throughout the world. That was part of its business.

13 On the day of the closing, Rolland executed and delivered to Monaghan an assignment of patent rights that specifically contained worldwide rights to the invention in question. The recitals in the assignment referred to the invention for which PCT and U.S. applications had been filed and recited that under the agreement of purchase and sale Rolland had agreed to sell that invention to Monaghan. The operative provisions of the assignment contained, in part, the following:

> The Assignor does hereby sell, assign and transfer to Monaghan and its successors and assigns:
>
>> (i) all of Assignor's entire right, title and interest to the Patent, including any and all inventions described therein, and in any and all national phase patent applications, continuations-in-part, continuations, divisions, substitutes, re-issues, re-examinations, or extensions thereof, and all other applications for the Patent relating thereto which have been filed, or hereafter shall be filed in all the countries of the world, including in Canada;

14 It is clear in my view that the agreement of purchase and sale covered the worldwide patent rights for the invention in question.

15 The vesting order as amended vested in Monaghan the assets described in the agreement of purchase and sale. This included the worldwide patent rights for the invention in question. Thus the vesting order should not be amended.

Purchaser for value without notice

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

16 The evidence appears clear that prior to the closing of the purchase of the mushroom business by Monaghan from Rolland, the publicly available information regarding ownership of the invention in question and any related patent applications disclosed Rolland as the owner.

17 On February 26, 2008, a U.S. patent application was filed in which Mr. Verdellen and another Rolland employee named Nader Gheshlaghi were named as the applicants and inventors and Rolland was named as the assignee for the patent application. On March 18, 2008 Mr. Verdellen and Mr. Gheshlaghi executed a written assignment in favour of Rolland in which they assigned to Rolland Farms their entire right, title and an interest throughout the world in the inventions which were the subject of the U.S. patent application. This assignment was recorded in the U.S. patent office on May 13, 2008. Also on March 18, 2008 a power of attorney was signed by Rolland as assignee which indicated that Rolland was the owner of the U.S. application and this power of attorney was also recorded in U.S. patent office on May 13, 2008.

18 Prior to the closing of the purchase, Monaghan and its advisers conducted due diligence regarding the business to be acquired, including information on patents. All of the information provided to Monaghan was consistent with the publicly available information that Rolland held the ownership interest in the patent rights in question. Also, at no relevant time was the Monitor aware of any interest of any third party, including Mr. Verdellen, in the patent rights and Mr. Verdellen never told the Monitor of his alleged interest even though a representative of the Monitor met with Mr. Verdellen on a number of occasions. At no relevant time did representatives of Rolland advice the Monitor or Monaghan of any alleged interest of Mr. Verdellen in the patent, including at a meeting on November 2, 2009, four days before the closing of the sale, which was held in part to address an issue of an apparent deletion of research and development from Rolland's computer system.

19 Counsel for Mr. Verdellen refers to evidence that on October 2, 2009 Mr. Verdellen met with a lawyer at Gowlings, the solicitors for Rolland dealing with patent applications for the invention in question, and told the lawyer that an international patent application filed under the Patent Cooperation Treaty by Rolland belonged to him. The lawyer, who was a junior lawyer not acting on the matter, advised Mr. Verdellen that there was a conflict and that the firm could not act for him. The lawyer made a memorandum to file. Although Rolland had authorized Gowlings to disclose all of the information in their patent files to Monaghan prior to closing, the physical files were not received by Monaghan until early December 2009, at least one month after the sale transaction closed. There is no evidence, however, that Monaghan was told by Gowlings or anyone else prior to the closing of Mr. Verdellen's alleged ownership interest in the patent.

20 In my view, it is clear from the evidence that prior to the closing of the purchase of the business by Monaghan from Rolland, Monaghan was never provided, nor did it learn of, any information of Mr. Verdellen's alleged interest in the patent, in spite of Monaghan's due diligence process.

21 Monaghan contends that if there is a binding agreement between Mr. Verdellen and Rolland regarding patent rights, the interest of Mr. Verdellen is equitable and that as Monaghan, is a *bona fide* purchaser for value without notice of the agreement between Mr. Verdellen and Rolland, it took title to the patent rights free and clear of any equitable interest of Mr. Verdellen.

22 The doctrine of *bona fide* purchaser for value without notice is described by Prof. Ziff in B. Ziff, *Principles of Property Law*, 5th ed. (Carswell: Toronto, 2010) at page 460 as follows:

> Equity acts on the conscience of the relevant parties; that is why a *bona fide* purchaser for value of the legal title who

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> buys land without notice of an equitable interest will not be bound by that interest. The good faith purchaser has what we would now call a clear conscience, and the present of such a person can alter the ordering of rights.

23 Although this statement refers to land, there is no principled reason why the principle would not apply to any form of property. A contractual right to intellectual property is property not taken by physical possession. It is a chose in action. This is made clear from the judgment of Morden J.A. in *DiGuilo v. Boland*, [1958] O.R. 384 (Ont. C.A.) in which he sated the following:

> To determine the legal issue thus presented, it is necessary to consider the law relating to choses in action and their assignability, first in England then in Ontario. In *Torkington v. Magee*, [1902] 2 K.B. 427, Channell, J., said, at p. 430:-
>
> > 'Chose in action' is a known legal expression used to describe all personal rights of property which can only be claimed or enforced by action, and not in taking physical possession.
>
> The term covers multifarious rights, many diverse in their essential nature, such as debts, company shares, negotiable instruments and rights of action founded on tort or breach of contract.
>
> . . .
>
> The nature of the rights of a purchaser under an agreement of sale of land should, at this point, be briefly considered. His rights are choses in action and are capable of assignment in equity: *Wood v. Griffith* (1818), 1 Swan. 43, at pp. 55-6. The right to specific performance was and is an equitable chose and the right to damages a legal chose in action.

24 See also Prof. Ziff at p. 76 in which he states that the right to assign choses took a long time to mature but eventually the scope of the category was extended to include a wide range of other intangibles, including copyrights, trademarks, patents etc.

25 Gordon Henderson, Q.C., at one time the undoubted leader of the intellectual property bar in Canada, described the doctrine of a *bona fide* purchaser for value without notice as it related to patents in G. Henderson, "Problems Involved in the Assignment of Patents and Patent Rights", *Canadian Patent Reporter*, Vol. 60, p. 237 at pp. 248-9 as follows:

> An equitable assignment exists where there is an agreement rather than a complete and absolute assignment.
>
> In equity (and therefore apart from s. 53 of the Patent Act) an assignee of a patent takes title subject to the equities. Accordingly, a subsequent purchaser of a patent who has knowledge of a prior equitable assignment takes title subject to the prior equitable interest. But an assignee who purchases a patent for valuable consideration without notice of a prior equitable assignment takes free and clear of it.

26 The doctrine of *bona fide* purchaser for value without notice has been applied in intellectual property cases. See *R. Griggs Group Ltd. v. Evans (No. 2)* (2004), [2005] Ch. 153 (Eng. Ch. Div.), [2004] at para. 54.

27 What is the interest of Mr. Verdellen in his contract with Rolland, assuming the contract to exist? Mr. Verdellen takes the position that the agreement transferred the patent rights to him with no necessity for any further transfer, and he has attempted to have his rights under the agreement recognized in the European Patent Office based on that agreement.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

28 Monaghan contends that Mr. Verdellen's interest under the agreement, assuming it to exist, is an equitable interest as the agreement states that Rolland "will transfer" the world patent rights to Mr. Verdellen. That is, it is an agreement to transfer those rights rather than an agreement under which the rights have been transferred to Mr. Verdellen. Monaghan compares the contract with an agreement of purchase and sale of land in which it is clear that the interest of the purchaser before closing is an equitable interest.

29 The agreement between Mr. Verdellen and Rolland is not as clear as a typical agreement of purchase and sale in which a future closing date is specified. However in my view, in the circumstances in which the agreement was made, and taking into account the express language "The information below summarizes how the R&D findings are to be handled..." and "Rol-and will transfer...to Jack", the agreement was an executory agreement in that the transfer did not take place in the agreement itself but rather was a promise that it would take place at some time in the future. Thus the interest of Mr. Verdellen under the contract was a chose in action and the right to specific performance was, as stated by Morden J.A., an equitable chose an action. That is, Mr. Verdellen rights under the contract, assuming they existed, were equitable rather than legal.

30 This notion of Mr. Verdellen's interest being an equitable interest is captured by the maxim when something is to be done under an agreement that "equity considers done what ought to be done". See *Grant Forest Products Inc., Re* (2010), 101 O.R. (3d) 383 (Ont. C.A.), aff'g (2009), 58 C.B.R. (5th) 127 (Ont. S.C.J. [Commercial List]).

31 In the circumstances, in my view, Monaghan is correct in its position that even if Mr. Verdellen had a binding contract with Rolland covering the patent rights in issue, Monaghan acquired those patent rights as a good faith purchaser without notice of Mr. Verdellen's rights and thus acquired them free and clear of any interest Mr. Verdellen might otherwise have had in them.

Section 51 of the Patent Act

32 Apart from the doctrine of being a bona fide purchaser for value without notice, Monaghan relies upon section 51 of the Patent Act to defeat any interest that Mr. Verdellen might otherwise have in the patent rights in dispute. That section, and the preceding two sections provide:

> **49.** (2) Where an applicant for a patent has, after filing the application, assigned his right to obtain the patent, or where the applicant has either before or after filing the application assigned in writing the whole or part of his property or interest in the invention, the assignee may register the assignment in the Patent Office in such manner as may be determined by the Commissioner, and no application for a patent may be withdrawn without the consent in writing of every such registered assignee.
>
> **50.** (2) Every assignment of a patent, and every grant and conveyance of any exclusive right to make and use and to grant to others the right to make and use the invention patented, within and throughout Canada or any part thereof, shall be registered in the Patent Office in the manner determined by the Commissioner.
>
> **51.** Every assignment affecting a patent for invention, whether it is one referred to in section 49 or 50, is void against any subsequent assignee, unless the assignment is registered as prescribed by those sections, before the registration of the instrument under which the subsequent assignee claims.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

33 The effect of section 51 of the Patent Act seems obvious. In *Apotex Inc. v. Wellcome Foundation Ltd.*, [2000] F.C.J. No. 1770 (Fed. C.A.) Rothstein J.A. stated at para. S00:

> Having regard to both sections [Sections 50(2) and 51], it is clear that a purpose of registration under subsection 50(2) is to secure an assignee's priority as against subsequent assignees. Failure to register will deprive an assignee of priority against subsequent assignees and, as between them, an unregistered assignment is "void".

> 34 Mr. Verdellen takes the position that section 51 has no application to the patent rights in question, being the worldwide rights outside of North America, as he asserts that the section deals only with registration in Canada.

35 Monaghan looks to the process in which a foreign patent application was made and then brought into Canada and contends that the effect of the Patent Rules under the Patent Act makes section 51 of the Patent Act applicable to the foreign patent rights outside of North America.

36 The Patent Cooperation Treaty ("PCT") is an international patent law treaty to which Canada is a signatory providing a unified procedure for filing patent applications to protect inventions in each of its contracting states. A patent application filed under the PCT is called an international application, or PCT application. The PCT provides for the filing of one patent application, in one language, with effect in each of its contracting states, instead of filing several separate national and/or regional patent applications. A PCT application does not itself result in the grant of a patent, since there is no such thing as an "international patent" or a "PCT patent". A PCT application, which establishes a filing date in all contracting states, must be followed up with the step of entering into national and/or regional phases in order to proceed towards the grant of national and/or regional patents.

37 On February 26, 2009, a PCT application was filed by Rolland in the Canadian Intellectual Property Office. On August 10, 2010, after the completion of its purchase from Rolland, Monaghan caused the PCT application to enter the national phase in Canada so as to become a Canadian patent application. This was filed with the Canadian Intellectual Property Office. At the same time Monaghan registered with that office the assignment of patent rights that it had acquired from Rolland on the closing of its purchase from Rolland.

38 Section 59 of the Patent Rules under the Patent Act provide:

> 59. When an international application becomes a PCT national phase application, the application shall thereafter be deemed to be an application filed in Canada and the Act and these Rules shall thereafter apply in respect of that Application.

39 Thus by virtue of that section, when the PCT application became a Canadian national phase application on August 10, 2010, the application was deemed to be an application filed in Canada and the Patent Act thereafter applied to it.

40 Monaghan asserts that once engaged, section 51 does not merely prohibit a prior unregistered assignment from

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

affecting title to a Canadian patent or application in respect of which a subsequent assignment has been registered but rather renders the entire prior unregistered assignment "void as against any subsequent assignee". Therefore, Monaghan asserts, the December 1, 2008 agreement relied upon by Mr. Verdellen, which was not registered before August 10, 2010, is void as against the assignment from Rolland registered on that day by Monaghan both in respect of Canadian patent or application rights and such rights elsewhere in the world.

41 It is understandable that when an international PCT application becomes a national phase application in Canada, the national phase application becomes subject to the Patent Act and a contest between two claimants to those Canadian patent rights would be governed by the registration provisions in section 51 of the Patent Act. Can it be said, however, that a contest between those two claimants to foreign patent rights would be governed by section 51 of the Patent Act? In my view it cannot.

42 While the Parliament of Canada has the legislative competence to enact laws having extraterritorial effect, it is presumed not to intend to do so, in the absence of clear words or necessary implication to the contrary. See *Society of Composers, Authors & Music Publishers of Canada v. Canadian Assn. of Internet Providers*, [2004] 2 S.C.R. 427 (S.C.C.) at para. 54 per Binnie J. Neither section 51 of the Patent Act nor section 59 of the Patent Rules expressly state that the provisions of section 51 are applicable to a contest between patent claimants in a foreign jurisdiction, nor can it be said that it is a necessary implication to come to that result. In my view it would be in the interests of international comity to leave such foreign contests to the laws of the foreign states in question.

43 Monaghan refers to the European Patent Convention which provides that the applicable law in each Contract State in Europe governs a patent application and to the provisions of the U.K. Patent Act which contain provisions similar to section 51 of the Canadian Patent Act. It also refers to similar provisions in the Australian Patent Act. It does so because Mr. Verdellen has asserted ownership of the patent rights in both Europe and in Australia. Monaghan asserts that the application of section 51 of the Patent Act would thus be consistent with international patent practice. To my mind the fact that these other jurisdictions have provisions governing a contest between patent claimants in those jurisdictions is all the more reason based on principles of international comity to construe section 59 of the patent rules and section 51 of the Patent Act as not being applicable to disputes between patent claimants in those jurisdictions.

44 Thus in my view Monaghan gains no protection for its patent rights against Mr. Verdellen under section 51 of the Patent Act insofar as those rights involve the rights to Europe or elsewhere outside of Canada.

S. 95 preference

45 Monaghan takes the position that the purported agreement relied upon by Mr. Verdellen is dated December 1, 2008, within three months of the filing of the CCAA application, and is therefore void under section 95 of the BIA. Section 95 of the BIA is applicable to a proceeding under the CCAA by virtue of section 36.1 of the CCAA.

46 In my view Monaghan has no status to act under section 95 the BIA. The right under section 95 to commence an application is one that in bankruptcy can only be brought by a trustee in bankruptcy. See *Tucker v. Aero Inventory (UK) Ltd.*, [2011] O.J. No. 3816 (Ont. S.C.J. [Commercial List]) per Morawetz J. at paras. 137 and 166. By virtue of section 36.1 of the CCAA, it is the Monitor who would have the right to make an application under section 95 of the BIA. Monaghan is not a creditor and thus would not be in a position to apply under section 38 of the BIA, also applicable to a CCAA proceeding, to

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

acquire any right of action under section 95 of the BIA from the Monitor.

47 Even if Monaghan had status to act under section 95 the BIA, it would not be possible on an application to make a determination of the matter as there are facts in dispute.

Conclusion

48 The application of Mr. Verdellen is dismissed. The cross-application of Monaghan is allowed in part. It is declared that the purported agreement of December 1, 2008 between Mr. Verdellen and Rolland and any purported oral agreement between them regarding the same matters, is void as against Monaghan as a *bone fide* purchaser for value from Rolland without notice of any such agreements,

49 Monaghan is entitled to its costs. If the costs cannot be agreed, Monaghan may make written submissions, not exceeding three pages in length, along with a proper cost outline, within 10 days and Mr. Verdellen may make reply submissions, no longer than three pages in length, within a further 10 days.

Application dismissed.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 10

2013 ONSC 578
Ontario Superior Court of Justice [Commercial List]

Dilollo, Re

2013 CarswellOnt 781, 2013 ONSC 578, 225 A.C.W.S. (3d) 913, 97 C.B.R. (5th) 182

In the Matter of the bankruptcy of Cosimo Dilollo

D.M. Brown J.

Heard: January 17, 2013
Judgment: January 29, 2013
Docket: 31-OR-207435-T

Counsel: H. Chaiton, D. Bourassa for Moving Parties, I.F. Propco Holdings (Ontario) 36 Ltd.
P. Cho for msi Spergel Inc., Trustee in bankruptcy of the estate of Cosimo Dilollo

Subject: Insolvency; Contracts; Corporate and Commercial; Estates and Trusts; Torts

Headnote

Bankruptcy and insolvency --- Avoidance of transactions prior to bankruptcy — Fraudulent preferences — Miscellaneous

Creditor obtained default judgment against debtor — Creditor began bankruptcy proceedings against debtor — Parties reached settlement order, which was paid although bankruptcy application remained — Debtor was forced into bankruptcy — Debtor appealed order, which was ultimately dismissed — Trustee brought motion for order that settlement was fraudulent preference, creditor brought motion to dismiss trustee's motion — Trustee's motion dismissed; creditor's motion granted — Trustee's motion was barred by limitation period — Limitation period began to run from date of Bankruptcy Order — Two year limitation period set out in s. 4 of Limitations Act, 2002 governed — Limitation period expired well before trustee initiated motion — Stay pending appeal did not alter conclusion of limitation period — It was open to trustee to seek lifting of stay if trustee thought preference motion might be prejudiced by appeal — Trustee had ample time following the dismissal of appeal to commence its preference motion.

Table of Authorities

Cases considered by *D.M. Brown J.*:

Bank of Montreal v. Bray (1997), 1997 CarswellOnt 3903, 36 O.R. (3d) 99, 153 D.L.R. (4th) 490, 14 R.P.R. (3d) 139, 50 C.B.R. (3d) 1, 104 O.A.C. 351, 33 R.F.L. (4th) 335 (Ont. C.A.) — distinguished

Bernard Motors Ltd., Re (1960), 38 C.B.R. 162, 22 D.L.R. (2d) 689, 1960 CarswellNB 3, [1960] S.C.R. 385

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(S.C.C.) — referred to

C.C. Petroleum Ltd. v. Steinberg, Morton & Frymer (2003), 2003 CarswellOnt 1085, 41 C.B.R. (4th) 10 (Ont. S.C.J.) — referred to

Canada (Attorney General) v. Fekete (1999), 242 A.R. 196, 1999 CarswellAlta 297, 10 C.B.R. (4th) 102, 1999 ABQB 262 (Alta. Master) — considered

Dilollo, Re (2010), 62 C.B.R. (5th) 223, 2010 CarswellOnt 104, 2010 ONSC 129 (Ont. S.C.J. [Commercial List]) — referred to

Dilollo, Re (2010), 2010 CarswellOnt 7217, 2010 ONCA 624, 69 C.B.R. (5th) 207 (Ont. C.A.) — referred to

Edwards, Re (2011), 79 C.B.R. (5th) 264, 2011 CarswellOnt 6139, 2011 ONCA 497, 336 D.L.R. (4th) 719 (Ont. C.A.) — referred to

Employers' Liability Assurance Corp. v. Ideal Petroleum (1959) Ltd. (1976), 1976 CarswellQue 32, [1978] 1 S.C.R. 230, 26 C.B.R. (N.S.) 84, 75 D.L.R. (3d) 63, (sub nom. *Employers' Liability Assurance Corp. v. Ideal Petroleum (1969) Ltd.)* 14 N.R. 503, 1976 CarswellQue 25 (S.C.C.) — referred to

Gingras v. General Motors Products of Canada Ltd. (1974), 13 N.R. 361, 1974 CarswellQue 59, 1974 CarswellQue 59F, [1976] 1 S.C.R. 426, 57 D.L.R. (3d) 705 (S.C.C.) — referred to

Homburg v. S-Marque Inc. (1999), 1999 CarswellNS 73, (sub nom. *S-Marque Inc. v. Homburg Industries Ltd.)* 176 N.S.R. (2d) 218, (sub nom. *S-Marque Inc. v. Homburg Industries Ltd.)* 538 A.P.R. 218 (N.S. C.A.) — considered

Hudson v. Benallack (1975), [1975] 6 W.W.R. 109, 7 N.R. 119, 59 D.L.R. (3d) 1, 1975 CarswellAlta 157, 1975 CarswellAlta 139, [1976] 2 S.C.R. 168, 21 C.B.R. (N.S.) 111 (S.C.C.) — referred to

Joseph v. Paramount Canada's Wonderland (2008), 2008 CarswellOnt 3495, 2008 ONCA 469, 90 O.R. (3d) 401, 294 D.L.R. (4th) 141, 56 C.P.C. (6th) 14, 241 O.A.C. 29 (Ont. C.A.) — referred to

Lakehead Newsprint (1990) Ltd. v. 893499 Ontario Ltd. (2001), 2001 CarswellOnt 34, 23 C.B.R. (4th) 170 (Ont. S.C.J.) — considered

Lawrason's Chemicals Ltd., Re (1999), (sub nom. *Lawrason's Chemicals Ltd. (Bankrupt), Re)* 127 O.A.C. 51, 1999 CarswellOnt 392, 87 C.P.R. (3d) 213 (Ont. C.A.) — distinguished

Mawji, Re (2011), 2011 CarswellOnt 1313, 2011 ONSC 1432 (Ont. S.C.J.) — considered

Piikani Nation v. Piikani Energy Corp. (2012), 58 Alta. L.R. (5th) 219, 88 C.B.R. (5th) 1, 2012 ABQB 187, 2012 CarswellAlta 459 (Alta. Q.B.) — considered

Principal Group Ltd. (Trustee of) v. Anderson (1997), (sub nom. *Principal Group Ltd. (Bankrupt) v. Anderson)* 146 W.A.C. 169, (sub nom. *Principal Group Ltd. (Bankrupt) v. Anderson)* 200 A.R. 169, [1997] 8 W.W.R. 689, 1997 CarswellAlta 463, 32 B.L.R. (2d) 42, [1997] 7 W.W.R. 336, (sub nom. *Ernst & Young Inc. v. Anderson)* 147 D.L.R. (4th) 229, 46 C.B.R. (3d) 101, 51 Alta. L.R. (3d) 45 (Alta. C.A.) — considered

Tucker v. Aero Inventory (UK) Ltd. (2011), 2011 CarswellOnt 8476, 2011 ONSC 4223, (sub nom. *Tucker (Re))* 338 D.L.R. (4th) 577, 80 C.B.R. (5th) 1 (Ont. S.C.J. [Commercial List]) — referred to

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Statutes considered:

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

s. 38 — considered

s. 95 — considered

s. 95(1) — considered

s. 95(1)(a) — considered

s. 136 — referred to

s. 195 — considered

Fraudulent Conveyances Act, R.S.O. 1990, c. F.29
Generally — referred to

s. 2 — considered

Limitations Act, 2002, S.O. 2002, c. 24, Sched. B
Generally — referred to

s. 4 — considered

s. 5 — considered

s. 19 — considered

s. 19(1) — considered

s. 20 — considered

Words and phrases considered:

stay of proceedings

A stay of proceedings pending the hearing of an appeal is not the functional equivalent of a limitation period. Limitation periods set deadlines by which a person must initiate legal process in respect of a cause of action. Stays pending appeal are engaged following the initial disposition of the legal process in which the cause of action was asserted. Limitation periods and stays pending appeal conceptually are quite different creatures.

MOTIONS by trustee for declaration that transaction was fraudulent preference and by creditor to set aside trustee's motion.

D.M. Brown J.:

I. Motion to dismiss Trustee's fraudulent preference motion as statute-barred

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

1 On August 24, 2013, msi Spergel Inc., the trustee in bankruptcy of the estate of Cosimo Dilollo, initiated a motion under section 95 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, for a declaration that $1.136 million in payments made by the bankrupt to I.F. Propco Holdings (Ontario) 36 Ltd., pursuant to minutes of settlement, constituted a preference, and the Trustee sought an order that Propco repay that sum to the Trustee (the "Preference Motion").

2 Propco, in turn, has brought this motion seeking an order that the relief sought by the Trustee is statute-barred by operation of the *Limitations Act, 2002*, S.O. 2002, c. 24, Sch. B., and its motion should be dismissed. Alternatively, Propco seeks an order that in the event the Trustee's motion is not statute-barred, Propco is entitled to file a proof of claim in the bankrupt's estate for the full amount of its $22,031,787.67 judgment against the bankrupt.

II. Facts

3 The facts are not in dispute. On July 6, 2006, Propco obtained default judgment against Dilollo in the amount of $22,031,787.67 (the "Judgment"). On December 15, 2006 Propco commenced a bankruptcy application against Dilollo, which the latter opposed. Settlement discussions resulted in Propco and Dilollo entering into Minutes of Settlement on August 30, 2007 under which Dilollo agreed to pay Propco $1.2 million (the "Settlement").

4 Between August and December, 2007, Dilollo paid Propco $1,136,500 pursuant to the Settlement.

5 It was a term of the Settlement that if Dilollo paid Propco the $1.2 million, both parties would consent to a dismissal of the bankruptcy application brought against Dilollo and the parties would exchange full and mutual releases. No dismissal of the bankruptcy application was obtained, and the parties did not exchange releases.

6 As a result, come early 2008, Propco's bankruptcy application against Dilollo remained outstanding. By order dated May 22, 2008, Es-Lea Holdings Limited, Rino De Piero and Sam Stern were added as applicants to the bankruptcy application.

7 Morawetz, J. granted the bankruptcy application on January 11, 2010, and Schwartz Levitsky Feldman Inc. was appointed Trustee. Nine days later, on January 20, 2010, Dilollo initiated an appeal from the Bankruptcy Order. The Court of Appeal dismissed his appeal on September 27, 2010 [2010 CarswellOnt 7217 (Ont. C.A.)].

8 The first meeting of creditors was held on May 31, 2011, at which time SLF was replaced as Trustee by msi Spergel Inc. On August 24, 2012 the Trustee initiated its Preference Motion to set aside the payments under the Settlement.

III. Positions of the parties on the limitations issue

9 Propco submitted that the two-year limitation period contained in the *Limitations Act, 2002* governed. Propco argued that the fact of the Settlement was known to the Trustee on January 11, 2010, the date of the Bankruptcy Order, so time started to run at that point. The two-year limitation period expired on January 11, 2012, some seven months before the

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Trustee initiated its Preference Motion and, consequently, that motion was statute-barred.

10 The Trustee accepted that the limitation period to bring the Preference Motion commenced on the date of the Bankruptcy Order, but the Trustee argued that the bankrupt's launching of an appeal of the Order suspended the running of the limitation period until the Court of Appeal disposed of the appeal. Accordingly, the Trustee submitted, the two-year limitation period did not expire until September 18, 2012, several weeks *after* the Trustee had initiated its Preference Motion.

11 The narrow issue for determination, therefore, is whether the stay of proceedings on the filing of an appeal contained in section 195 of the *BIA* operated to suspend the running of the limitation period under the *Limitations Act, 2002* for the Trustee's Preference Motion.

IV. Analysis on the limitations issue

12 General limitation periods in provincial statutes apply to bankruptcy proceedings,[1] and the Court of Appeal has held that no conflict exists between the general limitations provision contained in section 4 of the *Limitations Act, 2002* and section 95 of the *BIA*.[2] Section 4 of the *Limitations Act, 2002* provides:

> Unless this Act provides otherwise, a proceeding shall not be commenced in respect of a claim after the second anniversary of the day on which the claim was discovered.

The discoverability rules are set out in section 5 of the *Limitations Act, 2002*. As mentioned, the Trustee accepted that the claim was discovered on, and the limitation period began to run on, January 11, 2010, the date of the Bankruptcy Order. In his Reasons released that date, Morawetz J. specifically referred to the fact of the Settlement between Propco and the bankrupt.[3]

13 Section 195 of the *BIA* provides for a stay pending an appeal from an order or judgment made under the *BIA*:

> Except to the extent that an order or judgment appealed from is subject to provisional execution notwithstanding any appeal therefrom, all proceedings under an order or judgment appealed from shall be stayed until the appeal is disposed of, but the Court of Appeal or a judge thereof may vary or cancel the stay or the order for provisional execution if it appears that the appeal is not being prosecuted diligently, or for such other reason as the Court of Appeal or a judge thereof may deem proper.

Does the stay of an order pending appeal pursuant to *BIA* s. 195 affect the running of the limitation period under the *Limitation Acts, 2002*?

14 Two provisions of the *Limitations Act, 2002* consider the impact of limitation periods contained in other legislation on the running of limitation periods prescribed by that Act. Specifically, sections 19(1) and 20 provide:

> 19.(1) A limitation period set out in or under another Act that applies to a claim to which this Act applies is of no effect unless,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(a) the provision establishing it is listed in the Schedule to this Act; or

(b) the provision establishing it,

(i) is in existence on January 1, 2004, and

(ii) incorporates by reference a provision listed in the Schedule to this Act.

20. This Act does not affect the extension, suspension or other variation of a limitation period or other time limit by or under another Act.

15 Section 19 does not apply in this case because the Schedule to the *Limitations Act, 2002* does not refer to the *BIA*. Turning to section 20, does section 195 of the *BIA* provide for the suspension of a limitation period? The Trustee submitted that the automatic stay of proceedings under *BIA* s. 195 tolled the operation of the limitation period because the stay meant that no person could take any step in respect of the bankrupt's estate, including bringing the Preference Motion.

16 I disagree. To engage section 20 of the *Limitations Act, 2002* requires that some other statute provides for a limitation period and also provides for the "extension, suspension or other variation of a limitation period or other time limit by or under another Act".[4] Section 195 of the *BIA* does not contain any limitation period or provide for the "extension, suspension or other variation" of a limitation period. Since *BIA* s. 195 does not purport to extend, suspend or vary a limitation period contained in the *BIA*, section 20 of the *Limitations Act, 2002* does not apply. Since no other suspension provision contained in the *Limitations Act, 2002* would apply in the circumstances of this case, the basic two year limitation period set out in section 4 governs. The parties agreed that time started to run on the day the Bankruptcy Order was made, so the basic two-year limitation period expired on January 11, 2012, well before the Trustee initiated the Preference Motion. That motion, therefore, is statute-barred.

17 That a stay pending appeal might prevent a person from taking some step does not alter that conclusion. A stay of proceedings pending the hearing of an appeal is not the functional equivalent of a limitation period. Limitation periods set deadlines by which a person must initiate legal process in respect of a cause of action. Stays pending appeal are engaged following the initial disposition of the legal process in which the cause of action was asserted. Limitation periods and stays pending appeal conceptually are quite different creatures. If a stay might operate to prejudice a person's legal rights, recourse generally is available to seek a lifting of the stay from the court. Section 195 of the *BIA* specifically provides that "the Court of Appeal or a judge thereof may vary or cancel the stay...for such other reason as the Court of Appeal or judge thereof may deem proper". In the present case it was always open to the Trustee to seek a lifting of the stay from the Court of Appeal if the Trustee thought that its ability to initiate a preference motion might be prejudiced by the appeal.[5] As matters transpired, the Trustee was left with ample time following the dismissal of the appeal to commence its Preference Motion.

18 For these reasons, I grant the motion of Propco, declare that the Preference Motion is statute-barred by operation of the *Limitations Act*, and I dismiss the Preference Motion.

V. Alternative Issue: The effect of voiding the Settlement as a preference

A. The issue stated

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

19 That conclusion is sufficient to deal with Propco's motion. However, both parties filed and made extensive arguments on the alternative issue — the effect of a voiding of the Settlement on Propco's ability to file a proof of claim. The Trustee did not take the position that it would be premature to consider that issue nor did it oppose the determination of that issue at this time. From the materials I gleaned that the reason for the Trustee's position was that the estate lacks any funds, and if Propco could file a proof of claim for the amount of its Judgment, its *pro rata* share of any distribution essentially would overwhelm the shares of the other creditors. Consequently, the practical reality of the financial circumstances of the estate supports proceeding to determine the alternative issue, so I will decide that issue in the event that it is later found I erred in my determination of the limitations issue.

20 To recall the facts, Propco obtained a $22,031,787.67 Judgment against Dilollo, which it compromised in the Minutes of Settlement for payments totaling $1.2 million. Propco submitted that in the event the Trustee succeeded in voiding the Settlement under *BIA* s. 95, then Propco should be entitled to file a proof of claim in the bankruptcy for the full amount of its Judgment. The Trustee disagreed, arguing that in the event the payment of $1,136,500 under the Settlement was declared void, then Propco would be limited to filing a proof of claim for the amount of the Settlement, not the much larger amount of the Judgment.

B. The legal positions of the parties

21 The Trustee submitted that a finding that a payment made to a creditor was void as against the trustee as a preference under section 95 of the *BIA* did not affect the transaction as between the parties to it — the creditor and the bankrupt - with the result that the parties to the transaction remained bound by the bargain which they had struck. Accordingly, in the event that the payment made under the Settlement was found to be void as against the Trustee and the payment ordered returned, the Trustee argued that the other terms of the Settlement between Propco and the bankrupt would remain valid and binding. The Trustee submitted that one such term would include Propco's compromise of its claim under its $22 million Judgment down to $1.2 million.

22 On its part, Propco contended that if the payment made under the Settlement were to be declared void and set aside as a preference, then the Settlement would be void for all purposes. As a result, upon the repayment of the Settlement amount to the Trustee, Propco would be entitled to file a claim for the full amount of its Judgment.

23 Counsel stated they had been unable to find any authorities bearing directly on this issue.

C. Analysis

C.1 The purpose of the BIA's preference provisions

24 Section 95 of the *BIA* is one of several sections comprising a system under which a court can review transactions entered into between a debtor and its creditors in the period just prior to formal insolvency proceedings.[6] The Supreme Court of Canada described the place of the *BIA*'s preference provisions in the overall bankruptcy scheme as follows:

> The object of the bankruptcy law is to ensure the division of the property of the debtor rateably among all his creditors in the event of his bankruptcy. Section 112 of the Act provides that, subject to the Act, all claims proved in the bankruptcy shall be paid *pari passu.* The Act is intended to put all creditors upon an equal footing. Generally, until a

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> debtor is insolvent or has an act of bankruptcy in contemplation, he is quite free to deal with his property as he wills and he may prefer one creditor over another but, upon becoming insolvent, he can no longer do any act out of the ordinary course of business which has the effect of preferring a particular creditor over other creditors. If one creditor receives a preference over other creditors as a result of the debtor acting intentionally and in fraud of the law, this defeats the equality of the bankruptcy laws.[7]

25 As put by the Alberta Court of Queen's Bench in *Piikani Nation v. Piikani Energy Corp.*:

> The aim of s. 95 of the *BIA* is to prevent one creditor or group of creditors from getting an unfair advantage over other creditors when a debtor is insolvent. The remedy is not to "punish" the benefiting creditor, but rather to require it to repay the monies received so that payments out of the debtor's estate can be made respecting priorities *and shared properly amongst all creditors.*[8]

In *Tucker v. Aero Inventory (UK) Ltd.*, Morawetz J. stated:

> The s. 95 cause of action remedy is designed to ensure that there is *pari pasu* treatment as between unsecured creditors. The recipient of a preferential transfer is not entitled to keep the preferential proceeds if the elements of s. 95 are proven. The subject of the preference is returned to the estate but subject to the rights of secured creditors.[9]

26 The cause of action to declare a transaction void as a preference rests with the trustee.[10] The right of the trustee in respect of a preferential payment is "to have such payment declared void and the consequential right to recover the amount of the payment".[11] A fraudulent preference claim by a trustee is not a claim that sounds in damages but rather, pursuant to s. 95(1) of the *BIA*, to a declaration that such payments be deemed fraudulent and void as against the trustee.[12]

C.2 The case law on the effect of voiding a preference-type transaction

27 By its terms section 95(1)(a) of the *BIA* renders an offending transaction void as against the Trustee:

> 95. (1) A transfer of property made, a provision of services made, a charge on property made, a payment made, an obligation incurred or a judicial proceeding taken or suffered by an insolvent person
>
> > (a) in favour of a creditor who is dealing at arm's length with the insolvent person, or a person in trust for that creditor, with a view to giving that creditor a preference over another creditor is void as against - or, in Quebec, may not be set up against - the trustee if it is made, incurred, taken or suffered, as the case may be, during the period beginning on the day that is three months before the date of the initial bankruptcy event and ending on the date of the bankruptcy...

28 If section 95 of the *BIA* is designed to ensure the class equality of the bankruptcy laws and to prevent a form of "queue-jumping" amongst unsecured creditors during a stipulated period prior to the date of the bankruptcy, what happens when the trustee successfully challenges the queue-jumper under section 95, requires it to repay the preference it received and, in effect, forces it to go back and stand, *pari passu*, with the other creditors of the debtor to await a distribution of the estate under *BIA* s. 136? The parties brought to my attention three sets of cases.

Whether secured creditors share in the proceeds of a voided preference

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

29 First, Propco referred to the decision of Morawetz J. in *Tucker v. Aero Inventory (UK) Ltd.*, and the Trustee referred to the Nova Scotia Court of Appeal decision in *Homburg v. S-Marque Inc.* [1999 CarswellNS 73 (N.S. C.A.)],[13] (which Morawetz J. considered in the *Tucker* case), but those cases principally dealt with the question of the entitlement of secured creditors to the proceeds obtained by a trustee as a result of a successful preference claim. Those cases did not consider the position of an unsecured creditor who has been required to return a payment found to be a preference.

Reviving rights in the property of a voided transaction: the *Bray* and *Lawrason's Chemicals Ltd., Re* cases

30 Second, the Trustee pointed to the Court of Appeal decision in *Bank of Montreal v. Bray* [1997 CarswellOnt 3903 (Ont. C.A.)][14] for the proposition that the voiding of a transaction as a fraudulent one does not affect the transaction as between the parties to the transaction. That case involved a proceeding under section 2 of the Ontario *Fraudulent Conveyances Act* ("*FCA*") which rendered a conveyance of real property made with the intent to defeat creditors "void as against such persons and their assigns". The husband, Mr. Bray, had guaranteed the indebtedness of his company to a bank. His company encountered financial difficulties. Mr. Bray held title to the matrimonial home as a joint tenant with his wife. He conveyed his interest in the matrimonial home to his wife for one dollar thereby severing the joint tenancy. Several months later the bank made a demand on his guarantee and then commenced an action under the *FCA*. Mr. Bray died. The bank obtained default judgment on the guarantee. The parties agreed that the conveyance contravened the *FCA*. The issue then became: if the conveyance was set aside under the *FCA*, was Mr. Bray's one-half interest available for execution by the bank, or did Mrs. Bray enjoy title to the matrimonial home on the basis that by setting aside the fraudulent conveyance, the joint tenancy was restored?

31 The Court of Appeal held that the conveyance from Mr. Bray to his wife severed the joint tenancy. The Court noted that section 2 of the *FCA* made a fraudulent conveyance void as against the debtor's creditors, but the section did not render the transaction void as against the parties to the transaction. Section 2 of the *FCA* rendered a transaction voidable; the impugned transaction was not void *ab initio*. The Court of Appeal stated:

> Cartwright J. writing for the Court in *Re Bernard Motors Ltd.* [1960] S.C.R. 385 at 390 considering language in the former s. 64(1) of the *Bankruptcy Act*, which deemed certain transactions "fraudulent and void as against the trustee in the bankruptcy", adopted the following statement from Halsbury, 3rd ed., vol. 2, p. 560:
>
> > If a payment or other disposition of property, otherwise valid, be made in circumstances that amount to a fraudulent preference, the payment, at the time it is made, is a good payment, and so remains unless and, until it is set aside as a fraudulent preference. [Emphasis added.]
>
> Similarly, in this case the transaction although void against creditors was otherwise valid and remained so until it was set aside. Accordingly, I am unable to adopt the course suggested by Schulman J. and in effect notionally reinstate the joint tenancy between Mrs. Bray and her deceased husband so as to allow Mrs. Bray to take the property as the surviving joint tenant free of any claim by the Bank. To do so, in my view, would stretch the concept of legal fiction beyond all reasonable bounds.[15]

32 The Nova Scotia Court of Appeal, in the *Homburg v. S-Marque Inc.* case, also held that when a transaction is found to constitute a preference, the transaction is voidable, not void *ab initio*, with the result that the transactions were valid as between the parties "until set aside".[16]

33 Building on the *Bray* case, the Trustee relied on the decision of the Court of Appeal in *Lawrason's Chemicals Ltd., Re* [1999 CarswellOnt 392 (Ont. C.A.)].[17] The bankrupt company, Lawrason's Chemicals Ltd., owed money to Min-Chem.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Pursuant to a general security agreement, the latter held a security interest in all of Lawrason's assets, including trademarks. Lawrason's transferred a trademark to Min-Chem for nominal consideration. Within a year a petition had been filed against Lawrason's and subsequently a receiving order was made. Min-Chem sold all of Lawrason's assets pursuant to its security; Min-Chem contended that it had suffered a shortfall. Another creditor of Lawrason's, Hydrotech Chemical, obtained a *BIA* s. 38 order to commence an action to set aside the transfer of the trademark. Min-Chem consented to an order finding that the transfer of the trademark was void as against creditors under the *Fraudulent Conveyances Act*. The parties agreed to sell the trademark at public auction.

34 Min-Chem took the position that in the event the transfer of the trademark was set aside, then its former security interest in the trademark would revive. Hydrotech argued that although the transfer was void under the *FCA*, it was still a valid and subsisting transfer between the original parties to it. The Court of Appeal agreed with Hydrotech's position, following its earlier decision in *Bray*:

> If the trustee had sued and recovered pursuant to the provisions of s. 2 of the *Fraudulent Conveyances Act*, he could only have sued on behalf of those creditors whose interests were defeated, hindered, delayed or defrauded by the transfer of the trademark. However, because of the specific provisions of s. 38(3), the benefit derived from the action would belong to the estate to be shared by all creditors, and not just those whose interests were affected. *As between the parties to the transaction, the transfer would be a good and valid one. That being the case, there could be no revival of the respondent's security interest in the trademark: it could not be the owner of and a secured creditor in the same property. Nonetheless, in my opinion, it would be entitled to share in the estate as an unsecured creditor.*[18]

In the result, the Court of Appeal found that Min-Chem did not have a security interest in the proceeds of the sale of the trademark, but Min-Chem was entitled to claim as an unsecured creditor for any amount of the indebtedness to it not recovered on the realization of other assets over which it held security.

35 The decisions in *Bray* and *Lawrason's* are binding on me. I would note, however, that the Alberta Court of Appeal has expressed a somewhat different view about the effect of a declaration that a transaction is void under *BIA* s. 95, albeit in quite different circumstances than those considered in the *Bray* and *Lawrason's* cases. The case of *Principal Group Ltd. (Trustee of) v. Anderson* involved the payment out by an investment fund of monies to investors less than three months before the fund went into bankruptcy. The trustee sued to recover the payments as preferences. Some investors argued that it would be inequitable to permit the recovery of such funds because they had changed their position by spending or disposing of the payments before the trustee had initiated suit. In the course of rejecting such a defence to a preference action the Alberta Court of Appeal stated:

> The *Act* does more than forbid preferences and allow a suit to recover them. It makes such payments fraudulent and void: s. 95(1). *If they are void, then no property passed, and the payees are in possession of some of the bankrupt's property.* The duty of the trustee to collect the property of the bankrupt is elementary.[19]

The Alberta Court of Appeal did not discuss what recourse the investors might have against the estate of the bankrupt fund after having repaid the preference amounts.

Remedies available to the creditor in a voided preference: Re Bernard Motors

36 Finally, Propco referred to the decision of the Supreme Court of Canada in *Bernard Motors Ltd., Re.*[20] In that case a company had borrowed money from a bank on the strength of a promissory note. Four individual guarantors provided a guarantee to the bank of the company's indebtedness. At a time when the company was insolvent, it deposited money into its bank account sufficient to satisfy the company's indebtedness to the bank. Two of the guarantors, who were involved in the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

management of the company, asked the bank to satisfy what was owed to it out of the company's bank account and then to return the guarantee to them. The bank did so. About two months later the company went into bankruptcy. The trustee sought to set aside the payment to the bank as a preference under the *BIA*.

37 In light of the positions taken by the parties on the disposition of the issues by the lower courts, the Supreme Court of Canada held that since it was *res judicata* as between the bank and the trustee that the payment was good, then the guarantors were discharged because the debt to the bank for which they stood as sureties had been paid in full. In *obiter*, however, the Supreme Court of Canada stated:

> With respect, I incline to the view that it having been found as a fact that the intention of the insolvent was to prefer both the bank and the guarantors and that the intention of the latter, although not of the former, was to be preferred, it should have been held that the payment was void, *the bank should have been ordered to repay the $10,000 to the trustee and left to exercise its rights against the guarantors.* I do not, however, have to reach a final conclusion as to this because it is too late to make any such order.

This *obiter* would suggest that having repaid the preference amounts to the trustee, the debtor's indebtedness to the bank would remain, and the bank could proceed to recover that debt from the guarantors. The Supreme Court of Canada made no comment on what rights the bank would have to file a proof of claim in the bankrupt's estate.

C.3 Application to the facts of the present case

38 As the cases reveal, section 95(1)(a) of the *BIA* creates a mechanism by which a trustee may recover property of the bankrupt which had been transferred or paid out to an arm's-length creditor, in preference to other creditors, during the period which starts three months immediately prior to the date of the initial bankruptcy event and ends on the date of the bankruptcy. The property or payment recovered then stands available for sharing by all unsecured creditors, on a *pari passu* basis, subject to the rights of secured creditors as described in the *Tucker v. Aero Inventory (UK) Ltd.* case.

39 For the purpose of this part of the motion Propco has accepted that the payments made to it by Dilollo under the Settlement constituted a preference pursuant to section 95(1)(a) of the *BIA*. In those circumstances Propco would be required to repay the settlement amounts to the Trustee.

40 What claim would Propco then have against the estate? Under the analysis set out in the *Bray* and *Lawrason's* cases, the Settlement was voidable and therefore remained valid up until the time it was set aside. Unlike the transactions at issue in the *Bray* and *Lawrason's* cases, in this case the impugned transaction — the Settlement - did not convey title in real or personal property. Instead, under the Settlement Propco agreed to compromise its claim against Dilollo, and Dilollo agreed to pay $1.2 million to Propco. When he did so, Propco would consent to the dismissal of the bankruptcy application and Propco would provide Dilollo with a full, mutual release. Although Dilollo did not pay the full $1.2 million, Propco accepted what he did pay as the full discharge of his payment obligations, as can be seen from the letter dated April 11, 2011 from counsel for Propco which stated that:

> On December 18, 2007, Propco received a CIBC bank draft in the amount of $85,000 which it agreed to accept in lieu of the $150,000 which Dilollo previously agreed to pay.

From this it follows that Dilollo fulfilled his promises to pay the settlement amount as set out in sections 1 and 2 of the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Settlement.

41 Although the parties to the Settlement never exchanged mutual releases, under the terms of the Settlement Propco was obligated to deliver, and Dilollo was entitled to receive, a full release. That would have included a release of the amounts due under the Judgment. In light of that obligation of Propco, I think the analysis must proceed on the basis that upon receipt of the $1.136 million Propco must be taken to have released Dilollo from the amount of the Judgment.

42 In sum, the Settlement enabled Propco, during the period beginning three months before the date of the initial bankruptcy event and ending on the date of bankruptcy, to jump the queue over other creditors and obtain a preference by securing payment of part of Dilollo's indebtedness to it. To achieve that result Propco was prepared to compromise its Judgment by a significant amount. Propco received some value for its Judgment, while the amount of the bankrupt's property available for other creditors was reduced.

43 The effect of a declaration that the Settlement payment was void under *BIA* s. 95(1) should be to return Propco to the position it was in before it received the preferential payments. That is, Propco would be denied the preferential benefit represented by the settlement payments because it would have to return those payments to the Trustee. But, as stated in the *Piikani Nation* case, the purpose of section 95 is not to punish a benefiting creditor, but to prevent that creditor from securing an unfair advantage over other creditors. Requiring the preferred creditor to repay the monies achieves that goal, and then "payments out of the debtor's estate can be made respecting priorities *and shared properly amongst all creditors*."[21]

44 Following that reasoning, if the Settlement payments were voided as preferences under *BIA* s. 95(1)(a), then the Settlement as a whole would be void, and Propco then would be left to file a proof of claim, like all other unsecured creditors, for the amount of the debt it was owed. That would mean that Propco could submit a proof of claim for the amount of its Judgment which the Trustee would then have to review in the ordinary course of the administration of the estate with the other proofs of claims filed by unsecured creditors.

45 The Trustee submitted that any proof of claim by Propco should be limited to the amount agreed upon in the Settlement. I do not accept that submission for three reasons. First, the Trustee, in which all property of the bankrupt has now vested, cannot seek to set aside part of a transaction in order to recover some of the bankrupt's property, but then attempt to rely on another part of the impugned transaction to block or reduce a claim against the estate by the creditor. That would smack of cherry-picking.

46 Second, when I asked Trustee's counsel during argument whether the Trustee's position that Propco must be held to its compromise meant that effect had to be given to the full release of the Judgment agreed to in the Settlement and therefore Propco should not be allowed to file a proof of claim for *any* amount, the Trustee stated it was not taking that position. That was a reasonable submission by Trustee's counsel. It would be a very harsh result indeed were a creditor required to repay the entire consideration for its compromise of rights, yet be held strictly to its release of those rights. The purpose of section 95 of the *BIA* would be fulfilled simply by denying the creditor the benefit of the preference transaction and requiring the creditor to assert the amount of its pre-preference transaction claim by way of proof of claim with the other unsecured creditors. That would unwind the queue-jumping engaged in by the preferred creditor.

47 Third, I do not see this result as inconsistent with the reasoning of the Court of Appeal in the *Bray* and *Lawrason's* cases. In both those cases the impugned conveyances were done for nominal consideration, whereas the present case involved

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

the compromise of approximately $20 million in debt. Care must be taken when analogizing from the well-established legal consequences of severing a joint tenancy to the effect of other transactions which may be found void as a fraudulent conveyance or a preference. Moreover, *Bray* involved an action under the *Fraudulent Conveyances Act* where the impugned transaction was rendered void as against other creditors. In the present case, a finding of a preference under section 95 of the *BIA* would void the Settlement as against the Trustee, the person in whom all property of the bankrupt has vested. It is interesting to observe that in the *Lawrason's* case that while the Court of Appeal was not prepared to unwind the transfer of the trademark so as to restore Min-Chem's original position as possessing a security interest in the trademark, it did state that Mid-Chem would be entitled to share in the estate as an unsecured creditor to the extent of its shortfall. Since the transfer of the trademark was done for nominal consideration, no issue arose about Min-Chem's ability to file a claim for the consideration it had paid for the trademark.

48 For these reasons, I conclude that in the event the Trustee's claim under section 95(1)(a) of the *BIA* was not statute-barred and in the event it was found that the Settlement was void under that section, then Propco would be entitled to file, for review by the Trustee, a proof of claim for the full amount of its Judgment, together with applicable interest.

VI. Summary and Costs

49 By way of summary, I grant Propco's motion and dismiss the Trustee's Preference Motion as statute-barred.

50 As part of its motion Propco requested an order that the Trustee should be liable personally for costs awarded against it in the Preference Motion. I deferred argument on that point. Having now determined the first two issues raised by Propco, I would encourage the parties to try to settle the costs of this motion. I would observe that both issues raised by Propco were novel in the sense that neither counsel was able to find any cases directly on point. The parties might well wish to take into account the novelty of the issues in their discussions about the costs of the motion. If the parties cannot agree on costs, Propco may serve and file with my office written cost submissions, together with a Bill of Costs, by February 8, 2013. The Trustee may serve and file with my office responding written cost submissions by February 22, 2013. The costs submissions shall not exceed three pages in length, excluding the Bill of Costs.

Order accordingly.

Footnotes

1 *Gingras v. General Motors Products of Canada Ltd.* (1974), [1976] 1 S.C.R. 426 (S.C.C.); *Employers' Liability Assurance Corp. v. Ideal Petroleum (1959) Ltd.* (1976), [1978] 1 S.C.R. 230 (S.C.C.).

2 *Edwards, Re*, 2011 ONCA 497 (Ont. C.A.), para. 6.

3 2010 ONSC 129 (Ont. S.C.J. [Commercial List]), paras. 58 and 73.

4 *Joseph v. Paramount Canada's Wonderland*, 2008 ONCA 469 (Ont. C.A.), paras. 8and 9.

5 The case of *Lakehead Newsprint (1990) Ltd. v. 893499 Ontario Ltd.* [2001 CarswellOnt 34 (Ont. S.C.J.)], 2001 CanLII 28443 does not assist the Trustee, dealing as it did with the effect of a bankruptcy order on the running of the limitations period in respect of a debt, not the effect of a stay pending appeal on the right of the trustee to initiate a claim following the making of a bankruptcy order. Nor does the case of *Canada (Attorney General) v. Fekete*, 1999 ABQB 262 (Alta. Master), para. 9, which did not deal with the comprehensive limitations scheme created by the Ontario *Limitations Act, 2002. Mawji, Re*, 2011 ONSC 1432 (Ont. S.C.J.) relied on the *Fekete* decision and did not conduct any specific analysis under the *Limitations Act, 2002*.

6 *Tucker v. Aero Inventory (UK) Ltd.* (2011), 338 D.L.R. (4th) 577 (Ont. S.C.J. [Commercial List]), para. 163.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

7 *Hudson v. Benallack* (1975), [1976] 2 S.C.R. 168 (S.C.C.), para. 21.

8 (2012), 88 C.B.R. (5th) 1 (Alta. Q.B.), para. 118.

9 *Tucker, supra.*, para. 138.

10 *Ibid.*, para. 137.

11 *Bernard Motors Ltd., Re*, [1960] S.C.R. 385 (S.C.C.), at 390.

12 *C.C. Petroleum Ltd. v. Steinberg, Morton & Frymer* (2003), 41 C.B.R. (4th) 10 (Ont. S.C.J.), para. 3.

13 1999 CanLII 1591.

14 1997 CanLII 545.

15 *Bank of Montreal v. Bray, supra.*, paras. 26 and 27.

16 *Homburg, supra.*, para. 83.

17 1999 CanLII 4635.

18 *Ibid.*, para. 8, emphasis added.

19 *Principal Group Ltd. (Trustee of) v. Anderson* (1997), 147 D.L.R. (4th) 229 (Alta. C.A.), para. 11.

20 [1960] S.C.R. 385 (S.C.C.).

21 (2012), 88 C.B.R. (5th) 1 (Alta. Q.B.), para. 118.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 11

2011 MBCA 41
Manitoba Court of Appeal

Keith G. Collins Ltd. v. Canadian Imperial Bank of Commerce

2011 CarswellMan 196, 2011 MBCA 41, [2011] 7 W.W.R. 458, 203 A.C.W.S. (3d) 695, 268 Man. R. (2d) 30, 333 D.L.R. (4th) 740, 77 C.B.R. (5th) 180

Keith G. Collins Ltd. (Applicant / Appellant) and Canadian Imperial Bank of Commerce (Respondent / Respondent)

Barbara M. Hamilton, Martin H. Freedman, Holly C. Beard JJ.A.

Heard: November 2, 2010
Judgment: May 9, 2011
Docket: AI 10-30-07303

Proceedings: reversing *Keith G. Collins Ltd. v. Canadian Imperial Bank of Commerce* (2010), 63 C.B.R. (5th) 32, [2010] 5 W.W.R. 56, 2010 MBQB 2, 2010 CarswellMan 15, (sub nom. *Forbes (Bankrupt), Re)* 248 Man. R. (2d) 206 (Man. Q.B.)

Counsel: R.W. Schwartz for Appellant
I.D. Perlov for Respondent

Subject: Insolvency; Estates and Trusts

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy and insolvency --- Avoidance of transactions prior to bankruptcy — Fraudulent preferences — Insolvency of debtor at time of transaction

On September 29, bankrupt settled his credit card account with respondent bank out of proceeds of new mortgage on his house — On October 27, bankrupt made assignment in bankruptcy citing indebtedness on three other credit cards (other cards) — Trustee in bankruptcy demanded repayment from bank — Bank refused to repay amount it received from bankrupt — Trustee brought unsuccessful application to have payment received by bank declared invalid as fraudulent preference under s. 95 of Bankruptcy and Insolvency Act — Application judge concluded there was insufficient evidence to prove bankrupt was insolvent at time of payment to bank or that bankrupt's intention was to prefer bank over other creditors — Trustee appealed — Appeal allowed — Payment to bank was void as fraudulent preference — Application judge erred when he failed to consider evidence of indebtedness and concluded evidence was insufficient to establish bankrupt was insolvent on date of payment to bank — This was palpable and overriding error — Review of evidence properly included bankrupt's declarations as to his assets and liabilities — Facts spoke to bankrupt's inability to pay his credit card indebtedness as it became due — Evidence established, at least on prima facie basis, that other three credit card debts existed on September 29 — None of bank's evidence rebutted this prima facie evidence — Only

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

reasonable inference to be drawn from all evidence, when considered in totality, was that bankrupt's accounts for other credit cards existed on September 29 and were unpaid — Given that bankrupt lacked sufficient assets to pay those debts on September 29, trustee did establish on balance of probabilities that on that date, bankrupt was unable to meet his obligations as they became due.

Bankruptcy and insolvency — Avoidance of transactions prior to bankruptcy — Fraudulent preferences — View to prefer — Intention other than to prefer — Miscellaneous

On September 29, bankrupt settled his credit card account with respondent bank out of proceeds of new mortgage on his house — On October 27, bankrupt made assignment in bankruptcy citing indebtedness on three other credit cards (other cards) — Trustee in bankruptcy demanded repayment from bank — Bank refused to repay amount it received from bankrupt — Trustee brought unsuccessful application to have payment received by bank declared invalid as fraudulent preference under s. 95 of Bankruptcy and Insolvency Act — Application judge concluded there was insufficient evidence to prove bankrupt was insolvent at time of payment to bank or that bankrupt's intention was to prefer bank over other creditors — Trustee appealed — Appeal allowed — Payment to bank was void as fraudulent preference — Application judge erred in concluding that evidence did not establish bankrupt had intention to prefer bank to other creditors — Judge made palpable and overriding errors — Judge wrongly focussed on absence of evidence — Judge placed too much emphasis on bankrupt's subjective intention — Payment to bank had effect of preferring bank over other three creditors — There was preference in fact — In such circumstances, s. 95(2) of Act comes into play — Presumed intent to prefer arising from preference in fact in favour of bank was not rebutted — Plan by insolvent person to reorganize his or her financial affairs must be objectively reasonable to rebut presumption — Bankrupt's conduct, viewed objectively, was that he preferred bank to other three creditors that existed on September 29 — Bankrupt's plan was not objectively reasonable.

Table of Authorities

Cases considered by *Barbara M. Hamilton J.A.*:

Black & White Hat Shop Ltd., Re (1925), [1925] 1 W.W.R. 1121, 35 Man. R. 9, [1925] 3 D.L.R. 670, 5 C.B.R. 690, 1925 CarswellMan 1 (Man. C.A.) — referred to

Canada (Director of Investigation & Research) v. Southam Inc. (1997), 50 Admin. L.R. (2d) 199, 144 D.L.R. (4th) 1, 71 C.P.R. (3d) 417, [1997] 1 S.C.R. 748, 209 N.R. 20, 1997 CarswellNat 368, 1997 CarswellNat 369 (S.C.C.) — referred to

Coast Wire Rope & Supply Ltd. (Trustee of) v. Trans Pacific Hardware Inc. (1999), 1999 CarswellBC 638, (sub nom. *Coast Wire Rope & Supply Ltd. (Bankrupt) v. Trans Pacific Hardware Inc.)* 122 B.C.A.C. 257, (sub nom. *Coast Wire Rope & Supply Ltd. (Bankrupt) v. Trans Pacific Hardware Inc.)* 200 W.A.C. 257, 1999 BCCA 217, 9 C.B.R. (4th) 255 (B.C. C.A.) — considered

Dubois-Vandale (Trustee of) v. MBNA Canada Bank (2006), (sub nom. *Dubois-Vandale (Bankrupt) v. MBNA Canada Bank)* 209 Man. R. (2d) 268, 26 C.B.R. (5th) 261, 2006 CarswellMan 377, 2006 MBQB 258 (Man. Q.B.) — considered

Holt Motors Ltd., Re (1966), 56 W.W.R. 182, 57 D.L.R. (2d) 180, 1966 CarswellMan 3, 9 C.B.R. (N.S.) 92 (Man. Q.B.) — considered

Housen v. Nikolaisen (2002), 10 C.C.L.T. (3d) 157, 211 D.L.R. (4th) 577, 286 N.R. 1, [2002] 7 W.W.R. 1, 2002

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

CarswellSask 178, 2002 CarswellSask 179, 2002 SCC 33, 30 M.P.L.R. (3d) 1, 219 Sask. R. 1, 272 W.A.C. 1, [2002] 2 S.C.R. 235 (S.C.C.) — referred to

Knock v. Dumontier (2006), 2006 MBCA 99, 2006 CarswellMan 311, 208 Man. R. (2d) 121, 383 W.A.C. 121, 56 C.L.R. (3d) 1, [2006] 11 W.W.R. 148 (Man. C.A.) — referred to

Krawchenko (Trustee of) v. Minister of National Revenue (2005), (sub nom. *Krawchenko (Bankrupt), Re)* 198 Man. R. (2d) 120, 2005 CarswellMan 172, 2005 MBQB 97, 11 C.B.R. (5th) 238, [2006] 6 W.W.R. 575 (Man. Q.B.) — referred to

L. (H.) v. Canada (Attorney General) (2005), 2005 SCC 25, 2005 CarswellSask 268, 2005 CarswellSask 273, 333 N.R. 1, 8 C.P.C. (6th) 199, 24 Admin. L.R. (4th) 1, 262 Sask. R. 1, 347 W.A.C. 1, [2005] 8 W.W.R. 1, 29 C.C.L.T. (3d) 1, 251 D.L.R. (4th) 604, [2005] 1 S.C.R. 401 (S.C.C.) — referred to

Lotito Estate v. Scantlebury-MacDougall (1996), (sub nom. *Lotito v. Scantlebury)* 146 Nfld. & P.E.I.R. 337, 456 A.P.R. 337, 1996 CarswellPEI 107, 43 C.B.R. (3d) 23 (P.E.I. C.A.) — considered

Norris, Re (1996), 45 Alta. L.R. (3d) 1, [1997] 2 W.W.R. 281, (sub nom. *Norris (Bankrupt), Re)* 193 A.R. 15, 135 W.A.C. 15, 44 C.B.R. (3d) 218, 1996 CarswellAlta 884 (Alta. C.A.) — considered

Robinson v. Countrywide Factors Ltd. (1977), 1977 CarswellSask 5, [1978] 1 S.C.R. 753, 72 D.L.R. (3d) 500, 14 N.R. 91, 23 C.B.R. (N.S.) 97, [1977] 2 W.W.R. 111, 1977 CarswellSask 138 (S.C.C.) — referred to

St. Anne-Nackawic Pulp Co. (Trustee of) v. Logistec Stevedoring (Atlantic) Inc. (2005), 9 B.L.R. (4th) 1, 2005 NBCA 55, 2005 CarswellNB 285, 2005 CarswellNB 286, 255 D.L.R. (4th) 137, (sub nom. *St. Anne-Nackawic Pulp Co. (Bankrupt), Re)* 286 N.B.R. (2d) 95, (sub nom. *St. Anne-Nackawic Pulp Co. (Bankrupt), Re)* 748 A.P.R. 95, 13 C.B.R. (5th) 125 (N.B. C.A.) — referred to

Van der Liek, Re (1970), 14 C.B.R. (N.S.) 229, 1970 CarswellOnt 82 (Ont. S.C.) — referred to

West End Furniture Co. (Trustee of) v. Sinnott's Ltd. (1989), 75 C.B.R. (N.S.) 209, (sub nom. *Janes Noseworthy Ltd. v. Sinnott's Ltd.)* 81 Nfld. & P.E.I.R. 302, (sub nom. *Janes Noseworthy Ltd. v. Sinnott's Ltd.)* 255 A.P.R. 302, 1989 CarswellNfld 11 (Nfld. C.A.) — referred to

Statutes considered:

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

s. 2 "insolvent person" — considered

s. 2 "person" — referred to

s. 95 — considered

s. 95 [rep & sub. 2007, c. 26, s. 42] — considered

s. 95(1)(a) — considered

s. 95(2) — considered

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

APPEAL by trustee in bankruptcy from judgment, reported at *Keith G. Collins Ltd. v. Canadian Imperial Bank of Commerce* (2010), 63 C.B.R. (5th) 32, [2010] 5 W.W.R. 56, 2010 MBQB 2, 2010 CarswellMan 15, (sub nom. *Forbes (Bankrupt), Re)* 248 Man. R. (2d) 206 (Man. Q.B.), dismissing trustee's application to have payment made to bank declared invalid as fraudulent preference.

***Barbara M. Hamilton J.A.*:**

1 The appellant trustee in bankruptcy (the trustee) appeals the dismissal of its application to have a payment received by the respondent bank (CIBC) declared invalid as a fraudulent preference under s. 95 of the *Bankruptcy and Insolvency Act* (the *BIA*).

2 On September 29, 2006, Franklin Forbes (the bankrupt) settled his TD and CIBC Visa accounts out of the proceeds of a new mortgage on his house. One month later, on October 27, 2006, he declared bankruptcy, citing indebtedness on three other credit cards.

3 After the trustee's demand for repayment, TD Visa repaid the amount it received from the bankrupt to the bankrupt's estate. CIBC refused, taking the position that the payment was not a preference under s. 95.

4 The application judge dismissed the trustee's application. He concluded that the evidence was insufficient to prove that the bankrupt was insolvent at the time of the payment to CIBC or that the bankrupt's intention was to prefer CIBC over other creditors.

5 The trustee's appeal of this decision is accompanied by its motion to have fresh evidence considered by this court.

The BIA

6 The pertinent portions of s. 95 read as follows:

> **Preferences**
>
> **95. (1)** ... [A] payment made ... by an insolvent person
>
> > (a) in favour of a creditor who is dealing at arm's length with the insolvent person ... with a view to giving that creditor a preference over another creditor is void as against ... the trustee if it is made ... during the period beginning on the day that is three months before the date of the initial bankruptcy event and ending on the date of the bankruptcy; ...
>
> . . . . .
>
> **Preference presumed**
>
> **(2)** If the ... payment ... has the effect of giving the creditor a preference, it is, in the absence of evidence to the contrary,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

presumed to have been made ... with a view to giving the creditor the preference — even if it was made ... under pressure — and evidence of pressure is not admissible to support the transaction.

7 Section 2 of the *BIA* defines "insolvent person" by three different tests:

Definitions

2. In this Act,

.....

"insolvent person" means a person who is not bankrupt and who resides, carries on business or has property in Canada, whose liabilities to creditors provable as claims under this Act amount to one thousand dollars, and

(a) who is for any reason unable to meet his obligations as they generally become due,

(b) who has ceased paying his current obligations in the ordinary course of business as they generally become due, or

(c) the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due;

.....

8 Amendments to s. 95 were proclaimed in force while this case was on reserve in the court below. See S.C. 2007, c. 36, s. 42, proclaimed in force on September 18, 2009. The judge cited the current version of s. 95 in his reasons and counsel agreed that he was correct to do so. Because no substantive changes were made to s. 95 that must be considered for this appeal, I have cited the current version as well.

The Section 95 Application and the Evidence

9 In support of its application, the trustee filed the affidavit of Douglas Collins. He attached various documents and correspondence to his affidavit, including the bankrupt's Assignment for the General Benefit of Creditors and Statement of Affairs (Non-Business Bankruptcy), as well as correspondence related to the settlement and payment of the bankrupt's CIBC Visa account. In his affidavit, Mr. Collins referred to the bankrupt's "three other credit card accounts":

As appears from his Statement of Affairs, the Bankrupt had at least three other credit card accounts, none of which were paid any of the refinancing proceeds. Given that CIBC and TD VISA were paid only one month prior to bankruptcy, then, it appeared to me that those two creditors had been preferred.

10 In response, CIBC filed the affidavit of Jeffrey Loranger, an employee of CBV Collection Services Ltd., the collection agent for CIBC. Mr. Loranger outlined the dealings that he had with respect to the settlement of the CIBC Visa account. He concluded his affidavit by stating:

Based on my conversations with [the bankrupt] and [the mortgage broker], I do verily believe that [the bankrupt] had carried out an arrangement to restructure debts of his to make his situation more manageable with his creditors, and that the payment of $15,000.00 to CIBC was part of that arrangement.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

11 Mr. Loranger attached to his affidavit a copy of the summary of account from CIBC Credit Card Services for the bankrupt's CIBC Visa account for the period from September 14, 2006, to October 13, 2006.

12 Neither party cross-examined on the other's affidavit and neither party provided evidence directly from the bankrupt.

The Evidence from the Affidavits

13 The bankrupt, who was retired, made his assignment in bankruptcy on the basis of "being unable to pay my debts as they become due." He declared a modest pension income of less than $1,000 monthly and unsecured indebtedness of $22,001 to three creditors, identified as follows:

1) Bank One - Visa ($8,795);

2) Citibank Canada Mastercard ($6,715); and

3) Hudson's Bay Company - Recovery Department ($6,491).

14 He also declared that he owed Sun Mortgage Company $45,000, which was secured by the new mortgage (shown on title to be in the amount of $39,000) against his house, which he valued at $55,000. His other assets (cash, furniture and personal assets) were minimal, totalling only $1,459.

15 In the information accompanying his Statement of Affairs, he declared that he had not "[m]ade payments in excess of the regular payments to creditors" within the 12 months prior to the date of the bankruptcy.

16 By September 29, 2006, TD Visa had obtained judgment against the bankrupt (for an amount not made known to the judge) and the summary of account for the CIBC Visa account showed that the "[t]otal minimum payment due" was $18,223:

Account summary		
Previous balance		$17,902.42
	....	
Interest	320.59	
Total debits		+ 320.59
New Balance		**=$18,223.01**
Minimum payment due		
You must immediately pay the greater of:		
The amount over your credit limit	$1,723.01	
or		
The amount past due from last month	17,902.42	17,902.42
Please pay the current Amount due by Nov 8		+ 320.59
Total minimum payment due		**= $18,223.01**

17 At the time of the bankrupt's discharge in June 2007, the trustee was unaware of any potential payments offending s.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

95.

18 After investigating the payments made to TD Visa and CIBC Visa in the spring of 2008, the trustee demanded that the payments be repaid to the bankrupt's estate. After CIBC refused, the trustee brought its application under s. 95.

The Law

19 Section 95 applies to a payment that was made by a bankrupt (described as "the debtor" in the rest of this section on "The Law") prior to bankruptcy, provided that: 1) it was made within the prescribed period of time prior to the date of bankruptcy; 2) the debtor was insolvent on the date of the impugned payment; and 3) the debtor had the intention to prefer one creditor over another. On this appeal, there is no issue that the bankrupt's payment to CIBC fell within the applicable three-month period prescribed by s. 95.

20 The trustee has the initial burden to prove the debtor was insolvent by establishing that at least one of the three tests set out in the definition of insolvent person existed on the date of the impugned payment. The court is not to presume insolvency. See *Black & White Hat Shop Ltd., Re* (1925), 35 Man. R. 9 (Man. C.A.), and *Van der Liek, Re* (1970), 14 C.B.R. (N.S.) 229 (Ont. S.C.). Some cases describe the need for the evidence of insolvency to be "clear and convincing." For example, see *Krawchenko (Trustee of) v. Minister of National Revenue*, 2005 MBQB 97 (Man. Q.B.) at para. 11, (2005), 198 Man. R. (2d) 120 (Man. Q.B.).

21 While I have no quarrel with that description, it must be understood in its proper context of a shifting evidentiary onus. Once the trustee establishes a *prima facie* case of insolvency, the onus shifts to the defendant creditor to adduce evidence to rebut that *prima facie* case. See *Robinson v. Countrywide Factors Ltd.* (1977), [1978] 1 S.C.R. 753 (S.C.C.). McQuaid J.A. explained the onus in *Lotito Estate v. Scantlebury-MacDougall* (1996), 43 C.B.R. (3d) 23 (P.E.I. C.A.)) (at para. 14):

> .... The appellant had the burden of establishing a *prima facie* case that one of these three alternative situations [under s. 95] existed. If, on a balance of probabilities, the appellant established such a *prima facie* case, the evidentiary onus shifted to [the creditor] to rebut the *prima facie* evidence. See: *Robinson v. Countrywide Factors Ltd.* (1977), 23 C.B.R. (N.S.) 97 (S.C.C.) at pp. 135-136 ....

22 Once the trustee has established that the debtor was insolvent on the date of the impugned payment, the next question is whether the debtor had the intention to prefer one creditor over another by that payment.

23 It is not enough that a payment creates a preference in fact. The trustee must establish that the debtor had the intent to prefer one creditor over another. The cases refer to this intent as "the dominant intent." The intent of the creditor who received the payment is irrelevant. As stated by Belzil J.A. in *Norris, Re* (1996), 44 C.B.R. (3d) 218 (Alta. C.A.) (at para. 16):

> .... The state of mind of the debtor at the time of making the payment is ultimately the paramount consideration to be addressed by the court. The intent or state of mind of the preferred creditor is irrelevant, *Hudson v. Benallack* (1975), 21 C.B.R. (N.S.) 111 (S.C.C.).

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

24 The dominant intent is based on an objective assessment of the circumstances. In other words, the intention will be what the debtor's conduct objectively demonstrates when reasonably construed and not what the debtor (or others) may claim was his or her intention long after the payment was made. The point is made in the oft-cited decision in *Holt Motors Ltd., Re* (1966), 9 C.B.R. (N.S.) 92 (Man. Q.B.) (at p. 95):

> .... The test which I consider should be applied is an objective and not a subjective one; that is to say, the intention which should be attributed to the parties will always be that which their conduct bears when reasonably construed and not that which, long after the event, they claim they believe was present in their minds.

25 In *Coast Wire Rope & Supply Ltd. (Trustee of) v. Trans Pacific Hardware Inc.*, 1999 BCCA 217, 9 C.B.R. (4th) 255 (B.C. C.A.), Finch J.A. also emphasized the objective nature of the test (at para. 8):

> .... [T]his Court has held in *Ferrostaal Metals Canada Ltd. v. Olympic Steel Ltd. (Trustee of)*, [[1985] B.C.J. No. 2276 (QL)], at p. 6, that the intention of the debtor is to be determined objectively and not subjectively. Mr. Justice Carrothers for the Court said at para. 17:
>
>> The relevant intention governing determination of whether the prima facie presumption of a preference has been rebutted is that intention which the conduct of the parties bears when reasonably construed. It is an objective rather than a subjective test.
>
> In other words, the conduct of the parties may be a better measure of the debtor's intention than his expressed words.

See also *West End Furniture Co. (Trustee of) v. Sinnott's Ltd.* (1989), 75 C.B.R. (N.S.) 209 (Nfld. C.A.) and *St. Anne-Nackawic Pulp Co. (Trustee of) v. Logistec Stevedoring (Atlantic) Inc.*, 2005 NBCA 55, 13 C.B.R. (5th) 125 (N.B. C.A.).

26 Section 95(2) is crucial to the analysis. It creates the presumption of preference referred to by Finch J.A. in the above quote. Once a preference in fact has been established, this presumption of intent to prefer applies. The creditor receiving the payment must rebut the presumption. M.A. Springman, George R. Stewart & J.J. Morrison, *Frauds on Creditors: Fraudulent Conveyances and Preferences*, looseleaf (Toronto: Thomson Reuters Canada Limited, 2009), describes the presumption and the process (at p. 20-37):

> .... [T]he threshold issue for the trustee on the question of intent should be whether the transaction had the effect of conferring a preference. If it can be established that the transaction in question had that effect then, pursuant to section 95(2) of the Act, the intention to prefer will be presumed unless the creditor preferred can establish on the evidence that there was no intention to prefer. Therefore, where the presumption of section 95(2) arises, the question of intention should arise only where the presumption has been established and the creditor is called upon to rebut it. When the question of intent arises, the creditor must argue from the circumstances that the intent of the debtor was something other than to prefer the creditor. ....

The Judge's Decision

27 The judge identified the two questions that he had to address: 1) whether the bankrupt was insolvent on the date the payment was made to CIBC (September 29, 2006); and 2) if he was insolvent, whether the payment was a preference under s. 95. He answered both questions in favour of CIBC and dismissed the trustee's application.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

28 When answering the first question, the judge highlighted the lack of evidence from the trustee concerning the existence of the "three other credit cards" on September 29, 2006. As a result, he was "not satisfied that the bankrupt was 'insolvent' on the date of payment (September 29, 2006)" (at para. 13).

29 The judge addressed the second question in the event he was wrong in concluding that the bankrupt was not insolvent on September 29, 2006. He concluded that (at para. 14):

> .... CIBC has established that this is one of those "diligent creditor" scenarios referred to in the authorities. ... [T]hat the bankrupt's dominant intention at the time of the payments to CIBC and TD Visa was to obtain new financing at a lower interest rate ....

30 Just before stating this conclusion, he again focussed on the absence of evidence about the existence of the "three other credit cards" on September 29, 2006 (*ibid.*):

> .... Clearly, <u>if</u> the three credit card accounts ... were in existence on September 29, 2006, any such plan [to refinance] was improvident and unreasonable. However, I have no proper evidence before me to support that conclusion. Again, particulars of these debts could have been proven by the Trustee and may well have supported the overall positions of the Trustee. ....

Positions of the Parties

The Trustee

31 The essence of the trustee's position is that the judge erred when he focussed on the absence of evidence rather than the evidence before him. The trustee does not assert that the judge did not explain the law correctly, rather it says that he applied it incorrectly to the evidence.

32 The trustee argues that the evidence establishes that the bankrupt was insolvent on September 29, 2006, under any of the three applicable tests. However, it says that one need not go further than the first test because the evidence demonstrates that the bankrupt was "unable to meet his obligations as they generally [became] due."

33 The trustee asserts that the judge made several palpable and overriding errors, such as:

> 1) concluding that the bankrupt's monthly payment to CIBC was $320 when the account was in collection and the total amount was due and owing;
>
> 2) failing to infer that the bankrupt had not been meeting his obligations as they became due in the face of the evidence that the indebtedness to TD Visa was by way of judgment; and

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

3) failing to consider the three other creditors listed in the bankrupt's Statement of Affairs.

34 Further, the trustee argues that the judge failed to take into account that the bankrupt lied when he declared he had not paid any creditors in excess of the regular payments within 12 months of the date of bankruptcy when, in fact, he had paid out TD Visa and CIBC, and that Mr. Collins's unchallenged opinion as an officer of the court was that the bankrupt was insolvent at the material time.

35 With respect to the preference issue, the trustee asserts that the judge erred when he found that CIBC had rebutted the presumption of preference. It says that given the preference in fact to CIBC, the presumption applied and the judge erred in not applying it properly. It says that the effect of the judge's approach was to shift the onus incorrectly onto the trustee when he should have drawn an adverse inference against CIBC for not adducing evidence from the bankrupt. The trustee says that this is a palpable and overriding error, if not an error of law.

CIBC

36 CIBC responds that the judge made no errors of law and no palpable and overriding errors and therefore, this court cannot intervene and must show deference to the findings of the judge.

37 More particularly, CIBC asserts that the judge could not give credence to the bankrupt's information in the Statement of Affairs because the bankrupt was not credible for the very reason argued by the trustee. In any event, it says that the Statement of Affairs spoke from the date of bankruptcy and not as of the date of the payment to CIBC, one month earlier. Further, it says that the judge was entitled to conclude that the evidence of insolvency was "sketchy" (at para. 13) and therefore did not meet the standard to prove insolvency.

38 With respect to the preference issue, CIBC acknowledges that it had the onus to prove that the bankrupt did not make the payment to CIBC with the intention of giving it a preference. It says that Mr. Loranger's evidence demonstrates that CIBC was pressing the bankrupt for payment, which resulted in the payment to settle the indebtedness. The payment, it asserts, was part of a reasonable plan to avoid bankruptcy by refinancing and restructuring and was in response to CIBC acting as a diligent creditor.

39 CIBC acknowledges that the judge made a palpable error when he stated that the bankrupt was only required to pay $320 monthly to CIBC rather than payment in full of $18,223. However, it asserts that the error was not overriding given the evidence that, on the date of payment, the bankrupt had reached a settlement with CIBC to pay $15,000.

40 Finally, CIBC says that the judge did not err when he did not draw an adverse inference against CIBC for not adducing evidence from the bankrupt and that there was no shifting of onus, as argued by the trustee. As for the judge's comments that he had no evidence of the amounts owing by the bankrupt at the date of payment, CIBC asserts that the judge was simply pointing out that the trustee had failed to meet its initial onus of proving insolvency and a preference in fact.

Analysis and Decision

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Issues and Standard of Review

41 This appeal is not about how the judge articulated the law or the issues. Rather, it is about how he applied the legal tests to the evidence before him and the inferences that he made or failed to make. Thus, the issues raised by the trustee are either questions of fact or questions of mixed fact and law which do not entail any extricable legal principles. The standard of review is therefore palpable and overriding error. See *Canada (Director of Investigation & Research) v. Southam Inc.*, [1997] 1 S.C.R. 748 (S.C.C.) at para. 35; *Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235 (S.C.C.); *L. (H.) v. Canada (Attorney General)*, 2005 SCC 25, [2005] 1 S.C.R. 401 (S.C.C.); and *Knock v. Dumontier*, 2006 MBCA 99, 208 Man. R. (2d) 121 (Man. C.A.).

42 The two overarching issues in this appeal are:

1) Did the judge err in not finding the bankrupt insolvent on September 29, 2006?

2) If the bankrupt was insolvent on September 29, 2006, did the judge err when he did not find that the payment to CIBC was a preference under s. 95?

Did the Judge Err in Not Finding the Bankrupt Insolvent on September 29, 2006?

43 After explaining the onus on the trustee to prove insolvency, the judge commented upon the absence of evidence from the trustee (at para. 10):

> .... Here, there is proof that the bankrupt was having some financial problems in August and September 2006 in that he was not meeting some of his obligations (to CIBC and TD Visa). <u>There is no evidence as to whether he was making payments on any other debts he owed at that time. I have no evidence from the bankrupt himself, no evidence of the amounts of any other unsecured accounts that may have existed as at the date of the payment (September 29, 2006), and no evidence of the amount owed or paid to TD Visa as at that date</u> (albeit, whatever the amount was, it was subsequently recovered by the Trustee). ....
>
> [emphasis added]

44 Because of this absence of evidence, he concluded that the trustee had not met its onus to establish that the bankrupt was insolvent on September 29, 2006 (at paras. 11-13):

> Dealing firstly with the third test noted above [para. (c)], <u>I am not prepared to infer or conclude, absent evidence which was readily available and compellable</u>, that the three credit card accounts referred to in the October 27, 2006 statement of affairs existed and (or) were in arrears as at September 29, 2006. <u>Clearly, the amounts and the dates create a suspicion; however, to conclude this without specific evidence (particularly when that evidence is available) would be mere speculation</u>.
>
> As to the other two tests (paras. (a) and (b) noted above), I respectfully disagree with the conclusions urged by the Trustee. <u>Prior to the settlement with CIBC, the monthly payment on this indebtedness was $320.59. I have no evidence as to what amount was owed to TD Visa or what regular payment was required</u>, although it appears that this debt was reduced to judgment and probably required payment in full. <u>Absent proof of any other existing debts at September 29, 2006 (other than the new mortgage loan used to pay CIBC and TD Visa), the evidence falls short of establishing that the</u>

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> bankrupt was "unable" to meet his obligations as they generally became due or that he had ceased paying his current obligations as they generally came due. At best, he had decided to refinance these two loans by way of a more manageable mortgage loan. Clearly, the monthly payment owed to CIBC was a significant portion of the bankrupt's gross monthly income. However, this debt carried interest at 24% per annum and the bankrupt may well have been able to meet the monthly payment on the new mortgage. The mortgage would probably bear interest at a considerably lower rate than either CIBC or TD Visa (whatever amount was owed to TD Visa).
>
> ... [T]he Trustee's evidence on this issue is "sketchy", "less than clear and convincing", and "does not meet the standard required" (see para. 12 of the decision of Suche J. in **Krawchenko**, supra). I am not satisfied that the bankrupt was "insolvent" on the date of payment (September 29, 2006), notwithstanding that the evidence establishes his insolvency on the date of bankruptcy (October 27, 2006). ....
>
> [emphasis added]

45 The judge had every reason to note the evidence that he did not have and to be critical of the trustee for not providing it. More direct evidence about the existence of the three credit card debts on September 29, 2006, would have been helpful and preferable. Having said that, there was evidence that had to be considered and by focussing on the absence of evidence as the judge did, he failed to do so.

46 The question for the judge was whether the evidence that he did have from the trustee was sufficient to infer, on a *prima facie* basis, that the indebtedness that existed on October 27, 2006, also existed on September 29, 2006. In my view, the only reasonable inference to be drawn from that evidence is that the indebtedness that existed on October 27, 2006, or at least almost all of it, was far more likely than not in existence one month earlier.

47 A review of the evidence properly includes the declarations of the bankrupt as to his assets and liabilities. I do not accept CIBC's argument that this evidence was not credible because the bankrupt declared that he had not paid any creditors within the 12 months prior to his bankruptcy. In my view, the evidence pertaining to the bankrupt's assets and liabilities as at October 27, 2006, was properly considered because it was not challenged in any way by other evidence.

48 I review the evidence to demonstrate my conclusion. As of September 29, 2006, TD Visa had obtained judgment against the bankrupt on its credit card account and the CIBC Visa account was in collection. Both accounts were paid out of the new mortgage proceeds. Obviously, the bankrupt had not been paying these accounts as they became due. As of October 27, 2006, the bankrupt had assets, apart from his house, totalling $1,459 and he owed $22,001 on the "three other credit cards." His income was minimal and he said that he was "unable to pay my debts as they become due." His Hudson's Bay account was noted as being with the "Recovery Department."

49 Simply put, these facts speak to the bankrupt's inability to pay his credit card indebtedness as it became due. When the bankrupt declared he was unable to pay his indebtedness as it became due on the three credit cards, the only reasonable inference is that he was unable to pay them one month earlier. Therefore, the evidence establishes, at least on a *prima facie* basis, that the three credit card debts existed on September 29, 2006.

50 None of the evidence filed by CIBC rebutted this *prima facie* evidence. In fact, it supported it. It confirmed the bankrupt's inability to pay his debts as they became due as the monthly payments to CIBC Visa were not current and the account was in collection.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

51 To conclude, the only reasonable inference to be drawn from all of the evidence, when considered in totality, is that the bankrupt's accounts for the "three other credit cards" existed on September 29, 2006, and were unpaid. Given that the bankrupt did not have sufficient assets to pay these debts on September 29, 2006, the trustee did establish on the balance of probabilities that on that date, the bankrupt was unable to meet his obligations as they became due.

52 Given that conclusion, I need not address whether the trustee established insolvency under the other two tests.

53 However, I wish to comment briefly on the second test. The definition of person in the *BIA* is broad and includes "a partnership, an unincorporated association, a corporation, a cooperative society or a cooperative organization." The second test for insolvency is whether the person "ceased paying his current obligations in the ordinary course of business as they generally become due." It appears from the record and the judge's reasons that the second test was at play. I question the applicability of the second test to the circumstances here because the bankrupt was retired and not carrying on business. Given that this question was not an issue before the judge, or on appeal, I simply highlight my query and suggest that any party relying on this provision in the future address the question of whether it applies to any person or only those who were carrying on business.

Did the Judge Err When He Did Not Find that the Payment to CIBC was a Preference Under Section 95?

54 The judge addressed this question in the event that he was wrong in his conclusion that the trustee had not demonstrated that the bankrupt was insolvent on September 29, 2006, because of his indebtedness on the "three other credit cards." As will be explained, I am of the view that the judge made two palpable and overriding errors in his analysis.

55 The first was that he wrongly focussed on the absence of evidence. The judge wrote (at para. 14):

> .... <u>[I]f the three credit card accounts</u> evidenced in his statement of affairs (totalling $22,001) were in existence on September 29, 2006, any such plan was improvident and unreasonable. <u>However, I have no proper evidence before me to support this conclusion.</u> ....
>
> [emphasis added]

56 This was an error because, at this stage of the inquiry, he had to assume that the trustee had proven the bankrupt's insolvency on the basis of the very existence of the indebtedness on the "three other credit cards."

57 The second error was that the judge placed too much emphasis on the bankrupt's subjective intention, as established through Mr. Loranger. In effect, he placed the onus on the trustee and failed to give effect to the presumption under s. 95(2), as argued by the trustee.

58 There can be no question that the payment to CIBC had the effect of preferring CIBC over the three other creditors. In

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

other words, there was a preference in fact. In these circumstances, s. 95(2) comes into play and the intention of the bankrupt to prefer is presumed unless CIBC has shown that the bankrupt did not have that intention. There is no such evidence.

59 The evidence of Mr. Loranger was that he understood that the bankrupt was attempting to reorganize his affairs. However, as explained earlier, the bankrupt's intention is determined based on an objective analysis of the circumstances and not the subjective intent of the bankrupt, or the intent of the creditor.

60 A plan by an insolvent person to reorganize his or her financial affairs must be objectively reasonable to rebut the presumption. See *Coast Wire Rope & Supply*. In *Dubois-Vandale (Trustee of) v. MBNA Canada Bank*, 2006 MBQB 258, 209 Man. R. (2d) 268 (Man. Q.B.), Hanssen J. explained this well (at paras. 16-18):

> To rebut the presumption, MBNA must show on a balance of probabilities that Ms. Dubois-Vandale's dominant intention was not to prefer a creditor. The court must look at all of the circumstances and determine if there was in fact an intention on her part to give MBNA a preference. <u>Where, as here, a bankrupt asserts that it was her intention to reorganize her affairs and avoid bankruptcy, her intention must also be objectively reasonable.</u> See **Holt Motors Ltd., Re** (1966), 9 C.B.R. (N.S.) 92 (Man. Q.B.).
>
> MBNA has failed to show, on a balance of probabilities, that Ms. Dubois-Vandale's dominant intention was not to prefer it. Ms. Dubois-Vandale selected the accounts which she wanted to pay in full on January 28, 2004. She paid these accounts knowing that other debts would receive only a minimal payment or no payment whatsoever.
>
> While I am satisfied Ms. Dubois-Vandale's plan was to try to secure financing to consolidate the remainder of her debts and avoid bankruptcy, <u>her plan was not objectively reasonable. She was hopelessly insolvent.</u> Her debts greatly exceeded her [assets] and she did not have sufficient income to service a loan of the magnitude she required to consolidate her debts.
>
> [emphasis added]

61 Here, the bankrupt's conduct, viewed objectively, is that he preferred CIBC to the other three creditors that existed on September 29, 2006. His plan was "improvident and unreasonable" (at para. 14), using the judge's own words. It was not objectively reasonable.

62 Therefore, the payment to CIBC is a fraudulent preference pursuant to s. 95 and is void.

Conclusion

63 The judge erred when he failed to consider evidence of indebtedness and concluded that the evidence was insufficient to establish that the bankrupt was insolvent on the date of payment to CIBC. The judge also erred when he concluded that the evidence did not establish that the bankrupt had the intention to prefer CIBC to other creditors. Because these errors are palpable and overriding, the conclusions of the judge are not entitled to deference.

64 For the reasons set out above, I am of the view that the trustee established that the bankrupt was unable to pay his obligations as they became due on September 29, 2006, and, therefore, he was an insolvent person on that date. I am also of

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

the view that the presumed intent to prefer arising from the preference in fact in favour of CIBC was not rebutted by CIBC. Therefore, the payment to CIBC on September 29, 2006, is void as a preference under s. 95 of the *BIA*.

65 Given the foregoing, the fresh evidence motion is moot and need not be addressed.

66 I would allow the trustee's appeal, declare that CIBC received a preference in the amount of $15,000 and order that CIBC pay the trustee $15,000 plus interest calculated at five per cent per annum from the date of bankruptcy to the date of payment, as sought by the trustee in its notice of application. I would order costs in favour of the trustee in this court and the court below.

***Holly C. Beard J.A.*:**

I agree.

***Martin H. Freedman J.A.*:**

I agree.

Appeal allowed.

End of Document Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 12

1966 CarswellMan 3
Manitoba Court of Queen's Bench

Holt Motors Ltd., Re

1966 CarswellMan 3, 56 W.W.R. 182, 57 D.L.R. (2d) 180, 9 C.B.R. (N.S.) 92

Re Holt Motors Ltd.; Canadian Credit Men's Association Limited v. Stonewall Credit Union Society Limited

Bastin J. [in Chambers]

Judgment: April 13, 1966

Counsel: *J. F. R. Taylor*, for applicant.
A. H. Mackling and *H. R. Pawley*, for respondent.

Subject: Corporate and Commercial; Insolvency

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy — Avoidance of transactions prior to bankruptcy — Fraudulent preferences — Onus of proof

Fraudulent preference — Security given within three months of bankruptcy — Trustee proving essential elements to raise presumption — No rebuttal of presumption — Objective test to be applied in determining intention of parties — Concurrent intent proved on facts.

H., a director of respondent credit union, commenced business in 1962 as a car dealer and garage operator. He subsequently incorporated his business and obtained from the respondent overdraft privileges limited to $10,000. An unregistered chattel mortgage covering accounts receivable and stock-in-trade was given as security. Over a period of time, the $10,000 limit was considerably exceeded, until in July 1965, the debtor company had total loans from the respondent of some $44,000. Under pressure, H., on behalf of the company, executed a chattel mortgage and assignment of book debts in favour of the respondent. In September 1965, the company made an assignment in bankruptcy. The trustee in bankruptcy applied to set aside the chattel mortgage and assignment of book debts on the ground that they were fraudulent preferences within s. 64 of the Bankruptcy Act.

Held, the application should be granted.

1. The transaction had taken place within three months of bankruptcy.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

2. The debtor company was insolvent at the time that the security was given. At the date of the bankruptcy, there was a large deficiency and it was a reasonable assumption that little change would have occurred in the six week period between the giving of the security and the date of the bankruptcy.

3. The effect of the transaction was to give the respondent a preference over other creditors.

The trustee having proven these three requirements had established sufficient to raise the presumption that the security was fraudulent and void.

In order to meet the presumption created by s. 64, it was necessary for the respondent to show that the purpose of creating the security was not to place itself in a preferred position over other creditors. In determining the intention of the parties, the Court must apply an objective test, not a subjective one; that is, the intention which should be attributed to the parties will be that which their conduct bears when reasonably construed and not that which, long after the event, they claim they believe was present in their minds.

Knowledge of insolvency will be imputed when the creditor knows that his own debt was not being paid when due. In the circumstances, both H., the president of the debtor company, and the directors of the respondent, had information which should have made them aware that the debtor company was insolvent. There was affirmative proof of an intent on the part of the bankrupt company to give and of the respondent to receive a preference over other creditors.

There had been no *bona fide* expectation and belief that the giving of the securities would permit the debtor company to carry on business. Furthermore, the security was not given pursuant to an agreement made prior to the commencement of the three month period. The chattel mortgage and assignment of book debts were given in place of the invalid chattel mortgage and were intended to protect the position of the respondent at the expense of other creditors.

***Bastin J.*:**

1 This is an application by the trustee in bankruptcy of the estate of Holt Motors Ltd. to set aside a chattel mortgage, dated 23rd July 1965, on garage and office equipment and used cars not otherwise financed, and an assignment of all book debts, dated 22nd July 1965, given by the bankrupt company to the respondent, as being fraudulent preferences. In fact, both documents were executed in the early hours of 24th July 1965.

2 Section 64 of the Bankruptcy Act is as follows:

> 64. (1) Every conveyance or transfer of property or charge thereon made, every payment made, every obligation incurred, and every judicial proceeding taken or suffered by any insolvent person in favour of any creditor or of any person in trust for any creditor with a view to giving such creditor a preference over the other creditors shall, if the person making, incurring, taking, paying or suffering the same becomes bankrupt within three months after the date of making, incurring, taking, paying or suffering the same, be deemed fraudulent and void as against the trustee in the bankruptcy.
>
> (2) Where any such conveyance, transfer, payment, obligation or judicial proceeding has the effect of giving any creditor a preference over other creditors, or over any one or more of them, it shall be presumed *prima facie* to have been made, incurred, taken, paid or suffered with a view to giving such creditor a preference over other creditors, whether or not it was made voluntarily or under pressure and evidence of pressure shall not be receivable or avail to

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

support such transaction.

(3) For the purposes of this section, the expression 'creditor' includes a surety or guarantor for the debt due to such creditor.

3 To raise a presumption that the securities were fraudulent and void, the trustee must prove three things:

4 (1) That the transaction took place within three months of the bankruptcy. As the bankrupt company made an assignment in bankruptcy on 7th September 1965, this requirement is satisfied.

5 (2) That the debtor was insolvent at the time the securities were given. The statement of the affairs of the bankrupt company shows the amount of preference claims as $3,828.44 and of secured claims as $43,314.87. It showed the following secured creditors: Polaris Enterprises Ltd. with a claim of $8,691.42 secured by chattel mortgage on rent and equipment; Delta Acceptance Corporation with claim of $19,830 secured by chattel mortgage on stock in trade; Stonewall Credit Union with claim of $44,600 secured by accounts receivable and personal note for $15,000. The respondent also held the chattel mortgage which is being attacked in these proceedings. The book debts of the bankrupt company were valued at $7,264.42 and used cars and farm implements at $2,405. It is certain that there will be a large deficiency and it is a reasonable assumption that little change would have occurred in the period of approximately six weeks between 23rd July 1965, and the date of the bankruptcy. Mr. Thomas A. Holt, the president of the bankrupt company, confirmed that this was so. It appears from these figures that prior to the respondent acquiring its security on 23rd July 1965, the only assets available to pay the unsecured creditors of the bankrupt company, totalling $87,914.87, were these book debts which have been valued at $7,264.42 and some used cars and implements valued at $2,405, so the bankrupt company was hopelessly insolvent on 23rd July 1965.

6 (3) That the effect of the transactions which are impugned was to give the respondent a preference over other creditors. Since the chattel mortgage and assignment of book debts acquired by the respondent covered the only assets available to unsecured creditors, I hold that these securities did give the respondent a preference over other creditors.

7 On a literal reading of s. 64, the intent to give a preference would appear to be that of the insolvent person and this seems to be borne out by the concluding words of subs. (2) stating that "evidence of pressure shall not be receivable or avail to support such transaction." Prior to the enactment of this provision a creditor could prove that the intention of the debtor was not to prefer the interested creditor but to avoid threatened legal action. There are always two parties to such a transaction and it must be very seldom that their intentions do not coincide. In this case the bankrupt company and the respondent acted together to create the securities and I ascribe the same intent to both of them.

8 In order to meet the presumption created by s. 64 the respondent must show that the purpose of creating the securities was not to place the respondent in a preferred position over the other creditors. In the light of all the circumstances existing on 23rd July 1965, it is for me to determine what was the intention. This must be a matter of inference. The test which I consider should be applied is an objective and not a subjective one; that is to say, the intention which should be attributed to the parties will always be that which their conduct bears when reasonably construed and not that which, long after the event, they claim they believe was present in their minds.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

9 To decide the issue it is necessary to review the events which led up to the giving of the security. Thomas A. Holt, a resident of Stonewall for many years, commenced business as a car dealer and garage operator in Stonewall in August 1962. He was a director of the Stonewall Credit Union and on 16th April 1964, he applied for a credit of $6,000 to be in the form of overdraft privileges payable on demand and this application was approved by the credit committee. There is no evidence of his using the overdraft privilege but the respondent produced an unregistered chattel mortgage dated 23rd July 1964 given by Thomas A. Holt to the respondent to secure a loan of $5,000 covering a 1957 Fordson tractor and its equipment, to be paid when the unit was sold. There was evidence that this loan was repaid on 28th January 1965. On 30th June 1964, Thomas A. Holt incorporated Holt Motors Ltd. to take over the business in return for $7,500 in preferred shares and he put in an additional $500 as capital. The respondent produced an application, dated 8th October 1964, for a credit of $10,000 described in one place in the form as overdraft privileges and in another as a line of credit and this was signed by Thomas A. Holt and approved by the credit committee. It must be assumed that this credit was to be extended to Holt Motors Ltd. since an unregistered chattel mortgage for $10,000 dated 30th October 1964, from this company to the respondent, was executed by Thomas A. Holt and his brother, purporting to cover "Accounts Receivable — $16,000.00 to $20,000.00 — Stock in Trade — Parts $12,000.00," repayment on demand. It was argued by counsel for the respondent that the credit committee of the respondent intended that the bankrupt company should have a line of credit of the total of these two applications, namely, $16,000. I cannot accept this interpretation since the words $10,000 line of credit have only one possible meaning, which is that the borrowing is to be restricted to a maximum of $10,000. Furthermore, the evidence shows that the respondent, in its dealings, made a distinction between Holt as an individual and the company.

10 Evidence was given by the respondent as to the amount of the indebtedness of the bankrupt company to the respondent at the end of each month, commencing with 31st December 1964. The figures are as follows: 31st December 1964, $12,753.82; 31st January 1965, $11,837.21; 28th February 1965, $12,937.80; 31st March 1965, $16,687.53; 30th April 1965, $22,550.61; 31st May 1965, $28,175; 30th June 1965, $35,006.88; 22nd July 1965, $44,767.28.

11 The evidence is that none of the directors of the credit union was aware of the extent of this indebtedness which far exceeded the amount that the credit committee had approved. The manager, Robert Doubleday, was dismissed when the situation came to light and was not called to testify. What brought the situation to the attention of the directors was a report dated 28th June 1965, by the supervisor of credit unions, following an audit which began on 8th June 1965. This report made the following reference to Holt Motors Ltd. account which in the books of the respondent bore the number 440:

> *Overdrawn Deposit Accounts*: These are strictly forbidden in a Credit Union. The following are drawn to your attention: --- #440 $12,781.83
>
> The Board and Credit Committee should deal with #440 immediately. An overdrawn account of such an amount is considered an unauthorized loan.

12 If the line of credit given to the company by the credit committee was limited to $10,000, the amount of the unauthorized loan at 23rd July 1965 was $34,767.28 and this amount would be due and forthwith payable. When the members of the board looked into this account they were, as one member stated, "appalled" at the situation. They had several interviews with Thomas A. Holt and at a meeting of the board held on 23rd July 1965, passed the following resolution:

> Moved by Evancic and Seconded by Slatcher that we instruct our Solicitor to take all legal steps to execute on our mortgage and garnishee the Holt Motors Accounts receivable and have our Solicitor and Manager, Mr. Bob Doubleday contact Tom Holt to obtain required signatures on loan. Carried.

13 I assume it was about this time their solicitor informed the board that the chattel mortgage from the company, dated

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

30th October 1964, was invalid. Following the passing of this resolution, Thomas A. Holt was summoned from his bed and told that he must give security. Holt explained that his solicitor had advised him not to give security and Holt at first refused to do so, but under pressure of the members of the board, who were old friends and associates, he agreed to consult his solicitor by telephone and when he was unable to reach his solicitor he acquiesced and he and his brother signed the two documents. The explanation for inserting in the documents the figure of $39,000 as the indebtedness was that the postings to the company account were not up to date and the amount shown in the account was about this figure.

14 One factor which has been considered important in an inquiry such as this is knowledge by the creditor of the insolvency of the debtor. The Act defines insolvency as follows:

> 2. (*j*) 'insolvent person' means a person who is not bankrupt and who resides or carries on business in Canada, whose liabilities to creditors provable as claims under this Act amount to one thousand dollars, and
>
> (i) who is for any reason unable to meet his obligations as they generally become due, or
>
> (ii) who has ceased paying his current obligations in the ordinary course of business as they generally become due, or
>
> (iii) the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due; ...

15 Knowledge of insolvency will be imputed when the creditor knows his own debt was not being paid when due: *In re Shortt* (1922), 22 O.W.N. 539, 2 C.B.R. 449, 3 Can. Abr. (2nd) 2550. Where a creditor either knows of the insolvent position of the debtor, or has ample means of knowing it if he made proper inquiries, he cannot relieve the onus placed on him by s. 64: *In re Hatt & Son* (1922), 3 C.B.R. 433, 3 Can. Abr. (2nd) 2495. Knowledge of a debtor's insolvency exists in contemplation of law where the creditor, obtaining a preference, knew of circumstances from which ordinary men of business would conclude that the debtor was unable to meet his liabilities: *In re Progressive Farmers' Co.; Ex parte Brown Bros. & Burmstad Ltd.*, 3 C.B.R. 702, [1923] 1 W.W.R. 833, 3 Can. Abr. (2nd) 2501. These principles relate to the knowledge of the creditor; but since s. 64 is concerned with the intent of the debtor, his knowledge is of equal, if not of more, importance. The Court is entitled to assume that both the creditor and the debtor possessed the capacity of ordinary business men to appreciate facts which were available to them. The glaring fact known to both parties on 28th July 1965, was that since 31st January 1965, the debtor had received more than $27,000 without the approval of the directors which was morally and legally forthwith payable without demand. Inquiry would have revealed that in the same period unsecured debts of the company had increased to approximately $40,000 quite apart from the sum of $44,767.28 owing to the respondent. Inquiry would also have revealed that the stock of parts, garage equipment and new and used cars was subject to various forms of security held by Polaris Enterprises, Delta Finance Co. and Ford Motor Co., and that the only other asset consisted of book accounts, claimed to total $25,000, of which more than half were over 90 days in arrears. The directors apparently limited their inquiries to an examination of the book accounts and a financial statement showing the position of the company at 31st December 1964. This statement provided no depreciation on equipment and no reserve for losses on accounts receivable or on used cars. It also showed that the profit on new car sales was offset by the loss on the sale of used cars. The failure of the directors to examine the company accounts to ascertain its condition in July, and to trace the unauthorized borrowing from the respondent of $34,767.28, shows a wilful refusal to pursue essential investigations when put upon inquiry. I consider that both Thomas A. Holt, the president of the bankrupt company, and the directors of the respondent had information which should have made them aware on 23rd July 1965, that the bankrupt company was insolvent. I make a finding that they had this knowledge.

16 In an attempt to rebut the statutory presumption, counsel for the respondent has sought to rely on the principle that where a transaction is entered into by the debtor with the sole object and in the *bona fide* expectation and belief of being thereby enabled to successfully carry on his business, and not with the view of preferring one party to the detriment of other creditors, the transaction will not be set aside. I hold that if the directors of the respondent had not either deliberately or stupidly closed their eyes, they would have known that the bankrupt company had been operating at a loss for months and

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

had no chance of surviving. Their action in withdrawing all credits shows their lack of confidence in the company and, as they might well have known, this brought its operations to a halt. It cannot be said there was any *bona fide* expectation that the bankrupt company could be put on a paying basis.

17 Another principle to which counsel for the respondent referred was that the presumption of an intention to create a preference may be rebutted by evidence that security given within the three-month period was provided pursuant to an agreement made prior to the commencement of this period. This principle was applied in *Re Blenkarn Planer Ltd.* (1958), 37 C.B.R. 147, 26 W.W.R. 168, 14 D.L.R. (2d) 719, 3 Can. Abr. (2nd) 2600. In support of this argument counsel referred to the form of chattel mortgage dated 30th October 1964, by which the bankrupt company purported to give security for $10,000 on "Accounts Receivable — $16,000.00 to $20,000.00 — Stock in Trade — Parts $12,000.00" — as indicating an intention on the part of the company to give security. I have held that Thomas A. Holt, president of the bankrupt company, and the directors of the respondent were aware of the insolvency of the company on 23rd July 1965. I am bound to hold that the execution of proper forms of chattel mortgage and assignment of book debts in place of the invalid document was intended to protect the position of the respondent at the expense of other creditors. There is, therefore, affirmative proof of an intent on the part of the bankrupt company to give, and of the respondent to receive, a preference over other creditors.

18 I hold that the chattel mortgage and assignment of book debts which have been attacked are invalid against the trustee. The trustee will have his costs, to be taxed, with a *fiat* for discovery.

End of Document Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 13

1983 CarswellOnt 201
Ontario Supreme Court, In Bankruptcy

Thorne Riddell v. Fleishman

1983 CarswellOnt 201, 47 C.B.R. (N.S.) 233

Re TOYERAMA LIMITED; THORNE RIDDELL v. FLEISHMAN

Saunders J.

Heard: April 26-27, 1983
Judgment: September 15, 1983

Counsel: *T.R. Hawkins* , for plaintiff.
F.M. Catzman Q.C. , for defendant.

Subject: Corporate and Commercial; Insolvency

Table of Authorities

Cases considered:

Holt Motors Ltd., Re; Can. Credit Men's Assn. Ltd. v. Stonewall Credit Union Soc. Ltd. (1966), 9 C.B.R. (N.S.) 92, 56 W.W.R. 182, 57 D.L.R. (2d) 180 (Man. Q.B.) — *applied*
Mac-Wall Contr. Ltd., Re (1970), 14 C.B.R. (N.S.) 52 (Ont. S.C.) — *applied*
Van der Liek, Re (1970), 14 C.B.R. (N.S.) 229 (Ont. S.C.) — *applied*

Statutes considered:

Bankruptcy Act, R.S.C. 1970, c. B-3, ss. 2 "insolvent person", 73.

Application by trustee to declare payment and debenture fraudulent preference.

***Saunders J.* :**

1 This is a trial of an issue ordered by Hollingworth J. The issues are whether a payment of $37,862.82 by the bankrupt, Toyerama Limited ("Toyerama"), to Edith Fleishman, and the giving of a bearer debenture in the principal amount of $35,000 by Toyerama to her, are fraudulent and void as against the trustee as preferences within the provisions of s. 73 of the Bankruptcy Act, R.S.C. 1970, c. B-3.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

2 The business of Toyerama was the acquisition of toys from manufacturers. The acquisitions were usually of surplus stock which the manufacturers had not disposed of in the previous season. The toys were acquired by Toyerama under many different arrangements in the spectrum from outright cash sales to pure consignments. The toys were sold either to retailers or to consumers through leased retail outlets of Toyerama.

3 The Christmas season plays a predominant part in the toy industry. December is the largest selling month and the period from 1st October to 31st December is the largest selling quarter (61 per cent of 1978 Toyerama sales). Toyerama would often accept delivery early in the year and store the toys in its warehouse in anticipation of sale the following autumn. Manufacturers were anxious at the end of a season to deliver their surplus inventory to Toyerama, knowing that Toyerama would be unable to sell it until the next season. This, no doubt, was to make way for new products. A substantial number of manufacturers did not expect to be paid by Toyerama until the next season was over in late December or the following January.

4 The 1978 season was not good for the toy industry and, accordingly, not good for Toyerama. In January 1979 Toyerama had a large unsold inventory on hand and considerable indebtedness. Also, the manufacturers had larger than usual amounts of surplus stock available for disposal. Toyerama made an informal proposal to certain of its creditors in January 1979 whereby the creditors were asked to postpone payment for one year until the end of the 1979 season. It would appear that creditors with an aggregate indebtedness of $190,000 accepted the proposal.

5 Unfortunately, the 1979 season was worse than 1978 and on 25th January 1980 Toyerama made an assignment in bankruptcy.

6 In these proceedings the trustee attacks two transactions between Toyerama and the defendant Edith Fleishman. Edith Fleishman is the former wife of Marvin Fleishman, the president and principal shareholder of Toyerama. Their marriage took place in 1952. There were four children. The couple separated in the summer of 1977 and were divorced in 1982. Since the separation they have dealt with each other at arm's length, but, it would appear, with relatively little rancour. Their son Allan Fleishman is an officer and shareholder of Toyerama Limited and was employed by it. He appears to have been on good terms with both his mother and father.

7 Shortly after the separation in 1977, Edith Fleishman established a retail business under the name of "Toyaround" which was substantially the same business as Toyerama. Her business was not successful and closed down with considerable inventory on hand. Toyerama, in November 1978, agreed to buy the inventory from her for $37,862.82 which it was said was its retail value less 35 per cent. Toyerama agreed to pay her for the inventory one year later and to pay monthly interest in the interim. Its obligation was evidenced by a promissory note which came due on 9th November 1979.

8 Mr. and Mrs. Fleishman had made a separation agreement in September 1977, shortly after their separation, but that agreement was replaced by a second agreement dated 20th November 1978. While the second agreement does not say so, both Edith Fleishman and Marvin Fleishman testified that the purchase of the inventory by Toyerama was a condition precedent to Edith Fleishman entering it.

9 The second agreement obliged Marvin Fleishman to make certain lump sum payments to his wife. It was agreed that he would cause Toyerama to execute a second floating charge in favour of his wife whereby amounts owing by him to her and

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

certain amounts owing to her by Toyerama and others would be secured. She, in turn, agreed to provide a mortgage on the former matrimonial home as collateral security for part of the bank indebtedness of Toyerama. By debenture dated 12th January 1979, Toyerama agreed to pay Edith Fleishman the sum of $274,596.81 with interest at 10 per cent on 31st January 1980. The debenture contained a second floating charge on all its assets subject to a first charge in favour of the Royal Bank of Canada. In para. 14 of the debenture, Edith Fleishman (who did not execute the debenture in her personal capacity but only as secretary-treasurer of Toyerama) acknowledged that she was the beneficiary of the principal amount of the indebtedness to the extent of $42,191.54 and that the beneficiaries of the remainder were certain trusts bearing the name of members of the Fleishman family.

10 Shortly before 9th November 1979 Marvin Fleishman says he received an "amusing" card from his wife reminding him of the due date for payment of the inventory. Toyerama Limited made the payment by cheque dated on the due date and its bank account was debited with the amount paid on the following 13th November. The payment to Edith Fleishman for the inventory is the first transaction attacked by the trustee in these proceedings.

11 By agreement dated 20th September 1979 Toyerama purchased all the shares and shareholder loans of Yogi Yogurt Limited for an aggregate purchase price of $28,840. Marvin Fleishman testified that he considered the purchase a good investment for Toyerama because Yogi Yogurt had the benefit of certain contracts as well as some assets which would be available for disposal. He felt that the purchase was a normal business transaction even though at that time Toyerama was not doing very well. While this transaction is not attacked by the trustee in these proceedings, it is noted that both Marvin Fleishman and his son Allan Fleishman were shareholders in Yogi Yogurt Limited and received from the purchase $6,970 in the aggregate. The records of Toyerama indicate that approximately $97,000 was advanced by Toyerama to Yogi Yogurt Limited between 1st October and 31st December 1979.

12 Edith Fleishman was asked to loan $35,000 to Toyerama to assist it in the Yogi Yogurt purchase. Marvin Fleishman said that while that was the expressed reason for the request, he was more concerned that she did not deal with the inventory payment in an improvident fashion. Allan Fleishman seems to have had the same opinion and to have also felt that it was better to obtain the funds from his mother than from the bank. In what can be assumed to be a simultaneous transaction with the inventory payment, Edith Fleishman, by cheque dated 9th November 1979, advanced $35,000 to Toyerama. The cheque was credited to the Toyerama bank account on 13th November 1979, the same day as the inventory payment was debited. In return Toyerama gave Edith Fleishman a demand promissory note, dated 10th November 1979, for $35,000 bearing interest at 17 1/2 per cent per annum. Subsequently, by demand debenture, dated 29th November 1979, Toyerama agreed to pay Edith Fleishman $35,000 with interest at 15 per cent. The debenture contained a fixed and floating charge on its assets. Allan Fleishman said he discussed providing this security with his mother when she was considering making the loan. Marvin Fleishman says that the debenture was given at the insistence of her lawyers and that he was prepared to accede to their request. It is to be recalled that Edith Fleishman had received a floating charge debenture the previous January for the indebtedness to the trusts and to her under the separation agreement. The giving of the $35,000 debenture is the second transaction attacked by the trustee.

13 Section 73 of the Bankruptcy Act provides as follows:

> 73.(1) Every conveyance or transfer of property or charge thereon made, every payment made, every obligation incurred, and every judicial proceeding taken or suffered by any insolvent person in favour of any creditor or of any person in trust for any creditor with a view to giving such creditor a preference over the other creditors shall, if the person making, incurring, taking, paying or suffering the same becomes bankrupt within three months after the date of making, incurring, taking, paying or suffering the same, be deemed fraudulent and void as against the trustee in bankruptcy.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(2) Where any such conveyance, transfer, payment, obligation or judicial proceeding has the effect of giving any creditor a preference over other creditors, or over any one or more of them, it shall be presumed *prima facie* to have been made, incurred, taken, paid or suffered with a view to giving such creditor a preference over other creditors, whether or not it was made voluntarily or under pressure and evidence of pressure shall not be receivable or avail to support such transaction.

(3) For the purposes of this section, the expression "creditor" includes a surety or guarantor for the debt due to such creditor.

14 The two impugned transactions fall within those described in s. 73 and took place within three months of the bankruptcy. At the time they were made, there were unpaid creditors of the bankrupt and it is not disputed that the transaction had the effect of giving Edith Fleishman a preference over those creditors. There are, therefore, two issues to be decided:

15 (1) Was Toyerama an insolvent person at the time the transactions were entered into? The onus of establishing that Toyerama was insolvent is on the trustee and if it is unable to satisfy that onus its claim must be dismissed.

16 (2) If Toyerama was an insolvent person, were the impugned transactions entered into with a view of giving Edith Fleishman a preference over the other creditors? Because of the provisions of s. 73(2) the onus here is on Edith Fleishman to show that the transactions were not entered into with such a view.

17 On both issues it is important to consider the circumstances and general activity of Toyerama. There had been a bad season in 1978 which necessitated the informal proposal to creditors made in January 1979. The 1979 season was worse. The October sales were off by 16 per cent from the previous year. It was to get much worse. December sales dropped by 42 per cent and Marvin Fleishman described this as a disaster. The trustee is understandably concerned about the pattern of payments made by Toyerama in the months preceding its bankruptcy. There were relatively few payments to trade creditors, but Edith Fleishman received payment for her inventory in November 1979, and her loan of $35,000 and the January 1979 debenture in her favour were paid off in January 1980. The indebtedness to the bank which was guaranteed to a limited extent by both Marvin Fleishman and Allan Fleishman was reduced and available credit from that source not fully utilized. Such a pattern is consistent with an intention to reduce the potential personal loss to members of the Fleishman family at the expense of creditors in the event of a bankruptcy. On the other hand, there is an explanation for the pattern. Because of the nature of the business, a number of trade creditors had formally postponed their claims and others were not expecting payment until January 1979. Marvin Fleishman made a strenuous effort in December to persuade Edith Fleishman to postpone the payment of the 1979 debenture and to continue her agreement to guarantee a portion of the bank indebtedness. She refused to do so on the advice of her solicitors and, believing her security to be in jeopardy, issued a writ with respect to the $35,000 loan on 21st January 1979. Toyerama was legally obliged to make the payments due to her and other members of the family in January 1980. The reduction of the bank loan out of cash flow reduced interest cost. It should also be noted that in December 1979 Toyerama made a substantial investment in Yogi Yogurt and also entered into a new warehouse lease.

18 The situation of Toyerama at the beginning of 1979 was not good but had not yet reached a disastrous state. It is my conclusion on the basis of the evidence that when Edith Fleishman was paid for the inventory and given security for the $35,000 loan that Toyerama then intended to continue to carry on business for an indefinite period and was not contemplating either ceasing such business or making an assignment in bankruptcy.

19 Section 2 of the Bankruptcy Act defines "insolvent person" as follows:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

2. In this Act ...

"insolvent person" means a person who is not bankrupt and who resides or carries on business in Canada, whose liabilities to creditors provable as claims under this Act amount to one thousand dollars, and

(*a*) who is for any reason unable to meet his obligations as they generally become due, or

(*b*) who has ceased paying his current obligations in the ordinary course of business as they generally become due, or

(*c*) the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due; ...

20 Evidence was given about the books and records of Toyerama by Mr. Leyshon-Hughes, a vice-president of the trustee, and by Miss E. Bentley, one of its estates officers. In the opinion of Leyshon-Hughes, the books of Toyerama were current and had been adequately maintained. Either or both of Mr. Leyshon-Hughes and Miss Bentley had reviewed the invoices, files and other documents available to them. From these sources several tables were prepared which were put in evidence concerning the financial situation of Toyerama. In addition, there were unaudited financial statements prepared by a chartered accountant as at 30th September 1979 (the Toyerama year-end) which showed an excess of liabilities over assets and a substantial operating loss for the period covered by the statements. The evidence indicated that there were a number of unpaid creditors. Some had agreed in writing to defer payment until January 1980 or to some other date. Some had stipulated payment terms on their invoices which had not been met, while others showed no payment terms but had rendered bills prior to 9th November 1979. Marvin Fleishman testified that many of the creditors whose invoices indicated that their account was overdue did not expect payment until after the 1979 season or had verbally agreed to defer payment. Mr. Leyshon-Hughes said that the trustee did not inquire into these circumstances. No unpaid creditors were called by the trustee and the evidence of Marvin Fleishman on the arrangements he had made, although somewhat vague, stands uncontradicted.

21 The onus is on the trustee to establish on the balance of probabilities that Toyerama Limited was insolvent when it made the payment for the inventory and agreed to give the debenture for $35,000 to Edith Fleishman. To satisfy this onus, it must meet the test in one of paras. (*a*), (*b*) and (*c*) in the statutory definition of insolvency.

22 In dealing with para. (*a*), the evidence is that Toyerama in the last calendar quarter of 1979 had funds in its bank account and further bank credit available. Counsel for the trustee argued that it was a management decision not to pay the trade creditors and that Toyerama, having been prevented by its management from making the payments, was "unable" to do so. I do not agree with that submission. I agree with counsel for Mrs. Fleishman that "unable" does not mean "unwilling". If a person has ample funds to meet obligations and chooses not to do so, he, in my opinion, is not insolvent by reason of para. (*a*) of the definition. The unpaid creditors may enforce their claims if they choose to do so. In the context of the definition I see no difference between a person who has the funds and a person who has the funds available to him if he chooses. The trustee has not satisfied me on the balance of probabilities that in November 1979 Toyerama Limited was unable to meet its obligations as they generally became due.

23 The issue raised by para. (*b*) is more difficult. There were unpaid creditors in substantial amounts. Marvin Fleishman said that some amounts were disputed and that many creditors had either agreed to wait or understood that they would not be paid until the end of the 1979 season. This was because of the nature of the business where most of the sales were made in the last quarter of the year. No doubt there were some creditors who had not agreed or who had not accepted the understanding that payment would be late. No inquiry was made by the trustee as to these arrangements. Some trade creditors were paid in November and December 1979, and of these some may have been dealing with Toyerama on a C.O.D. basis. The problem is that there is no direct evidence from any of the unpaid creditors which might affirm or deny the arrangements Marvin Fleishman says were made. Leyshon-Hughes on cross-examination said he could not say either way whether the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

bankrupt was meeting its current obligations. I am unable to find, on the evidence, that in November 1979 Toyerama Limited had ceased to pay its current obligations in the ordinary course of business as they generally became due.

24 Finally, with respect to para. (*c*), the unaudited balance sheet of Toyerama as at 30th September 1979 showed an excess of liabilities over assets. It would be a fair inference that the situation did not improve in October or November 1979. The principal property of Toyerama was its accounts receivable and inventory. Its fixed assets were shown on the financial statement at a cost of approximately $57,000. There was no evidence of the fair valuation of the assets and as previously indicated the amount of obligations due and accruing due is uncertain. There is no basis for finding Toyerama insolvent because of para. (*c*) of the definition.

25 I conclude that the trustee has not satisfied the onus on it to show on the balance of probabilities that Toyerama was an insolvent person in November 1979. The claim by the trustee must therefore be dismissed.

26 The second issue should, nevertheless, be considered in the event that I am wrong in my conclusion on insolvency. On this issue, Edith Fleishman has the onus of establishing that the transactions were not entered into with a view to giving her a preference over other creditors. In several cases, it has been said that if a creditor can show on the balance of probabilities that the dominant intent of the debtor was not to prefer the creditor but was some other purpose, the onus has been satisfied: see *Re Mac-Wall Contr. Ltd.* (1970), 14 C.B.R. (N.S.) 52 (Ont. S.C.) ; and *Re Van der Liek* (1970), 14 C.B.R. (N.S.) 229 (Ont. S.C.) . The test is an objective one and in *Re Holt Motors Ltd.; Can. Credit Men's Assn. Ltd. v. Stonewall Credit Union Soc. Ltd.* (1966), 9 C.B.R. (N.S.) 92, 56 W.W.R. 182, 57 D.L.R. (2d) 180 (Man. Q.B.) , Bastin J. said at p. 95:

> In order to meet the presumption created by s. 64 [now s. 73] the respondent must show that the purpose of creating the securities was not to place the respondent in a preferred position over the other creditors. In light of all the circumstances existing on 23rd July 1965, it is for me to determine what was the intention. This must be a matter of inference. The test which I consider should be applied is an objective and not a subjective one; that is to say, the intention which should be attributed to the parties will always be that which their conduct bears when reasonably construed and not that which, long after the event, they claim they believe was present in their minds.

27 As previously stated, I have found that there was no intention on the part of the Toyerama management in November 1979 to cease carrying on business. The relationships amongst Toyerama, Edith Fleishman, Marvin Fleishman and Allan Fleishman were complex. Edith Fleishman and Marvin Fleishman dealt with each other at arm's length. Allan Fleishman worked with his father, but appeared to have a good relationship with his mother. They owned a joint bank account and he was in the habit of giving her financial advice. There was a firm obligation to pay her for the inventory and Edith Fleishman was insisting in November 1979 that it be paid for on time; likewise, in the following December she refused to extend the payment date for the debenture given the previous January. In November 1979 Allan Fleishman says there was no discussion as to whether or not to pay his mother and she was paid promptly on the due date. There were other creditors at that time, but the arrangements with them are uncertain. Marvin Fleishman says he proposed the loan of $35,000 because he was apprehensive as to what Edith Fleishman might do with the inventory payment. He says that he wanted to protect her. He had more than an altruistic interest in doing so because of his continuing support obligations to her. He agreed to give her security for the loan because she and her solicitor asked for it and this was consistent with the arrangement that had been made with respect to the indebtedness covered by the January 1979 debenture. It seems to me that the purpose of the transactions with Edith Fleishman was to preserve the delicate relationship between her and her former husband and was not to prefer her over other creditors. There was no intention that I can infer from the evidence of an intention not to pay the other creditors in due course. Mrs. Fleishman has, therefore, satisfied me on the balance of probabilities that Toyerama did not enter the impugned transactions with a view of giving Edith Fleishman a preference over other creditors.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

28 In the result, the claim is dismissed. Both the trustee and Edith Fleishman should have their costs out of the estate.

Application dismissed.

End of Document Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 14

1983 CarswellOnt 214
Ontario Supreme Court, In Bankruptcy

Touche Ross Ltd. v. Weldwood of Canada Sales Ltd.

1983 CarswellOnt 214, 48 C.B.R. (N.S.) 83

TOUCHE ROSS LIMITED v. WELDWOOD OF CANADA SALES LIMITED

Smith J.

Judgment: July 6, 1983

Counsel: *F. Highley* , for applicant.
W. Meyer, Q.C. , for respondent.

Subject: Corporate and Commercial; Insolvency; Civil Practice and Procedure

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy --- Avoidance of transactions prior to bankruptcy — Fraudulent preferences — View to prefer — Intention other than to prefer — Transaction in ordinary course of business

Bankruptcy --- Practice and procedure in courts — Costs — Award of costs — Payable by trustee personally

Avoidance of transactions prior to bankruptcy — Fraudulent preferences — Statutory presumption — Burden of proof — Debtor taking advantage of 2 per cent discount by paying within 30 days — Payment by certified cheque — Presumption rebutted.

The question arose whether certain payments made by the bankrupt company to a creditor within three months before bankruptcy constituted a fraudulent preference. The debtor took advantage of a 2 per cent discount by paying within 30 days and paid the debt of the creditor in question on 16th July and 29th July 1980. The petition in bankruptcy was issued on 6th October 1980.

Held:

The prima facie presumption contained in s. 73(2) was rebutted and the payments should stand. It should be taken as laudable that a company should meet its obligations promptly and particularly this is so when a discount is offered in consideration of prompt payment after the goods have been shipped. The court should therefore be extremely loathe to label any of such payments as fraudulent preferences even when made within the three-month period. It was not the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

intention of the framers of s. 73 that the prima facie presumption would play a significant role when the challenge was directed against the suppliers who were dealing at arm's length with the debtor company. On the other hand, the court does not confer any priority upon suppliers of goods and if a predominant intent to prefer is established by convincing and credible evidence, then the innocent supplier must suffer the same fate as all other innocent creditors. In this case, the receivables ledger disclosed that the payments did not constitute anything but a record of ordinary course of business transactions. It was not a proof of a design or a plan to prefer. Also, the fact that the cheques were certified by the payor did not lead to the conclusion that the debtor intended to prefer the creditor.

The court criticized the behaviour of the representative of the trustee on the witness stand because "he assumed an adversarial and even slightly hostile role from the witness stand which I considered to be dissonant having regard to the nature of his duties as an officer of the court".

Table of Authorities

Cases considered:

Van der Liek, Re (1969), 13 C.B.R. (N.S.) 28 , time to appeal extended 13 C.B.R. (N.S.) 200 (Ont. S.C.) — *referred to*

Statutes considered:

Bankruptcy Act, R.S.C. 1970, c. B-3, ss. 2 "insolvent person", 73(1), (2), 112.

Application by trustee to declare payment to creditor a fraudulent preference.

***Smith J.*:**

1 This is a trial of an issue directed by order of Anderson J. dated 8th September 1981 in which he defined the question as one of whether the payments made by the now bankrupt Mainland Lumber Limited to its creditor, Weldwood of Canada Sales Limited ("the creditor"), subsequent to 6th July 1980 constitute a fraudulent preference within the meaning of s. 73 of the Bankruptcy Act, R.S.C. 1970, c. B-3.

2 I will need to recite all the pertinent facts with some care since the trustee's contention is that the payments, two in number totalling $5,340.61, are but a small part of a total amount of the order of $132,000 in accounts payable to suppliers which were paid in priority to a large debt owing to the Bank of Montreal. The allegation is that an entire class of creditors was preferred although the specific concern on this issue relates to the two cheques only.

3 Section 73 reads as follows:

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> 73.(1) Every conveyance or transfer of property or charge thereon made, every payment made, every obligation incurred, and every judicial proceeding taken or suffered by any insolvent person in favour of any creditor or of any person in trust for any creditor with a view to giving such creditor a preference over the other creditors shall, if the person making, incurring, taking, paying or suffering the same becomes bankrupt within three months after the date of making, incurring, taking, paying or suffering the same, be deemed fraudulent and void as against the trustee in the bankruptcy.
>
> (2) Where any such conveyance, transfer, payment, obligation or judicial proceeding has the effect of giving any creditor a preference over other creditors, or over any one or more of them, it shall be presumed *prima facie* to have been made, incurred, taken, paid or suffered with a view to giving such creditor a preference over other creditors, whether or not it was made voluntarily or under pressure and evidence of pressure shall not be receivable or avail to support such transaction.

4 The petition in bankruptcy was issued 6th October 1980. The accounts which the cheques were meant to cover were in the respective amounts of $2,736 and $2,713.60. The debtor took advantage of a 2 per cent discount by paying within 30 days. It paid the debt in two approximately equal instalments on 16th July 1980 and 29th July 1980. The payments were then clearly made within the three-month period.

5 The second question to be addressed according to *Re Van Der Liek; Owen v. Royal Bank* (1969), 13 C.B.R. (N.S.) 28 , time to appeal extended 13 C.B.R. (N.S.) 200 (Ont. S.C.) , is that of insolvency. Reliance is placed upon the following part of the definition section [s. 2] contained in the Act:

> "insolvent person" means a person who is not bankrupt and who resides or carries on business in Canada, whose liabilities to creditors provable as claims under this Act amount to one thousand dollars, and ...
>
> (*c*) the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due; ...

6 The evidence of Robert Merkley, a chartered accountant in the employ of Touche Ross Limited, the trustee, is very convincing. His examination of the books of the company revealed an excess of liabilities over assets at book value in the amount of $52,857.50. The assets were predominantly inventory and receivables. Out of a total of $243,738.43 in receivables, only the relatively small amount of $19,000 was collected. Included in the total was a sum exceeding $113,000 owing by Midway Manufacturing Ltd., a company related to Mainland with the same principals at the helm. The latter company went bankrupt and no distribution was made. The inventory at book value was $107,693.95. The trustee realized $13,000 after taking over the company as receiver following appointment by the Bank of Montreal on 29th September 1980. I accept the opinion of Mr. Merkley that the company was insolvent as of 30th June 1980 and almost certainly for a considerable number of months prior thereto.

7 We are left with the third and in this instance, as in most others, the most crucial element to be established and perhaps the most difficult to determine, namely, that of the intent to prefer, or in other words, preference in fact.

8 There is no evidence that the Weldwood account was treated any differently than a normal supplier account in the ordinary course of business. Goods were ordered and shipped on 11th and 20th June, respectively, and were paid for within the time required to entitle the debtor to take advantage of the 2 per cent discount if paid within 30 days and seven days' grace. Another shipment of goods took place in September valued at $2,105.60. The trustee accepts that payment would

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

likely have been made about 9th October to take advantage of the discount had receivership not intervened. The area manager for Weldwood never met the principals of Mainland and has not done business with them since.

9 Leaving aside for the moment the prima facie presumption contained in s. 73(2), the trustee alleges that Mr. William Taylor, the president and general manager of Mainland, embarked upon a deliberate strategy to pay his trade suppliers in full at a time when he knew he was insolvent, to the detriment of the Bank of Montreal. The clear purpose, as implied and expressed in the course of the trustee's evidence, was to pave the way for future dealings with the same suppliers. The allegation is serious and I propose accordingly to scrutinize the evidence with care. Before doing so, I must confess to a measure of discomfort at seeing the trustee take up the cudgels for one creditor, albeit a substantial one, namely the Bank of Montreal, against others after he had served the former as a privately appointed receiver. He assumed an adversarial and even slightly hostile role from the witness stand which I considered to be dissonant having regard to the nature of his duties as an officer of the court. His avowed purpose, expressed through his counsel, was to honour the spirit of the Act as set out in s. 112, of payment pari passu to all creditors. I would have preferred a total absence of previous involvement with the Bank of Montreal in respect of this estate. I do not wish to imply that there is any impropriety on the part of the trustee. Discretion, however, might have dictated that the trustee's employee take a less militant stand.

10 Upon assuming responsibility under the private appointment on 29th September 1980, Mr. Merkley, on behalf of Touche Ross Limited, reviewed the cash disbursements to date and found them to have been significant and mainly in favour of suppliers. Indeed, all suppliers had been paid except for Weldwood's last shipment as to which the date allowed for discount purposes had not passed, excepting further an account of $10,000 in favour of Forex. Taylor is said to have expressed annoyance that this account had not been paid. There was a third account outstanding to Hornby. The evidence in this regard was to the effect that communications had broken down between Hornby and a principal in Mainland.

11 The trustee also came upon certain letters in September which he termed highly unusual. Most of them are dated 9th September 1980. They are addressed to certain debtors of Mainland and they direct them to make payment of their outstanding accounts either directly to Midway, the related company referred to above, or to creditors of Mainland.

12 Reference must equally be made to the fact that, in July and August, a practice was engaged in by Mainland of dispatching couriers to the bank with regular deposits and with a number of cheques in favour of suppliers that were presented for immediate certification. The cheques to Weldwood, however, were forwarded by mail and had not been certified.

13 The trustee's suspicions were understandably aroused. He ultimately recommended a petition for a receiving order. Prior to the petition being issued, Merkley took notes of conversations with Taylor. He commenced taking notes on 1st October, from memory, of exchanges that took place 29th and 30th September and also 1st October. In these conversations, Taylor admitted the practice of depositing funds and immediately withdrawing them by requesting certification of a number of cheques. He admitted transfers to Midway. Taylor is also reported to have said on 30th September that "he looked after his friends" and on 1st October that "he looked after his suppliers" and that "I am going to be in this business for a while yet".

14 To complete the summary of the facts, I must add that Taylor and his associate, Grenier, had both guaranteed payment of the debt to the Bank of Montreal and not to the suppliers. Taylor's guarantee was worthless. Grenier was called upon to retire a portion of the Bank of Montreal debt. Taylor and Grenier had had a falling out. The debt to the bank, incidentally, pursuant to a note signed on 28th July, which consolidated all previous notes, stands at $318,000.90.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

15 This case presents a unique problem. It must surely be taken as eminently laudable that a company should meet its obligations promptly, and particularly is this so when a discount is offered in consideration of prompt payment after the goods have been shipped. The court should therefore be extremely loathe to label any of such payments as fraudulent preferences even when made within the three-month period. It could hardly have been the intention of the framers of s. 73 that the prima facie presumption would play a significant role when the challenge was directed against the suppliers who were dealing at arm's length with the debtor company.

16 On the other hand, the Act does not confer any priority upon suppliers of goods, and if a predominant intent to prefer is established by convincing and credible evidence then the innocent supplier must suffer the same fate as all other innocent creditors.

17 In this instance, there are, in my view, only two circumstances that could give rise to a reasonable inference of an intent to prefer: the practice of certifying cheques concomittantly with the making of deposits and the absence of any outstanding accounts payable at the end of September other than those which were explained in a manner consistent with the alleged intent. I say this because I am in large measure discounting the letters dated 9th September and the conversations which took place several weeks later. These latter two additional circumstances, whatever their evidentiary weight in relation to transactions in September, can only lead to speculation as to what the intent might have been in July. Their probative value, if any, would be extremely light in any case for the July period.

18 Taking the matter one step further, the court is really left with the certification of cheques, because the payment of accounts in excess of $100,000 over a three-month period, standing alone, is neutral. It ought to be considered normal for a company to pay its accounts when due. I have reviewed Ex. 8, the receivables ledger, and it does not constitute anything but a record of ordinary course of business transactions. It is not proof of a design or of a plan to prefer.

19 As for the cheque certification practice at some time in July and August, it does not enable me to conclude that the debtor intended to prefer Weldwood in particular and very possibly no one else either. The evidence, therefore, is clearly insufficient. In the result, the payments will stand and Weldwood should have its costs out of the estate on a solicitor-and-client basis, as should also the trustee.

Presumption rebutted and application dismissed.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 15

1936 CarswellSask 15
Saskatchewan King's Bench

A.R. Colquhoun & Son Ltd., Re

1936 CarswellSask 15, [1937] 1 W.W.R. 222, 18 C.B.R. 124

In re A. R. Colquhoun & Son Limited

Canadian Credit Men's Trust Association Limited v. Campbell, Wilson & Strathdee Limited

MacDonald, J.

Judgment: November 25, 1936

Counsel: *J. L. McDougall, K.C.*, for trustee.
H. F. Thomson, K.C., for defendant.

Subject: Corporate and Commercial; Insolvency

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy — Avoidance of transactions prior to bankruptcy — Fraudulent preferences — View to prefer — Intention other than to prefer — Intention to remain in business

Fraudulent Preference — Payments Made by Retailer to Wholesaler Within Three Months of Bankruptcy — Motion to Set Aside Dismissed — Debtor Hoping to Extricate Himself — Exchange of Goods — The Bankruptcy Act, S. 64, 9 C.B.R. 141.

Payments made and goods returned by a retailer to a creditor, a wholesaler, within three months of the former's bankruptcy, the payments being for goods delivered during that period or for goods delivered previously the credit for which had expired during said period, held not to be a preference within sec. 64 of *The Bankruptcy Act*, since it was also found that during that period there was the hope on the part of the debtor that he would be able to extricate himself from his difficulties and the goods were supplied by the wholesaler with the hope of enabling him to do so; and the goods which were returned in exchange for other goods and the assets of the bankrupt available for distribution among his creditors were not affected by the exchange, because if the goods had not been returned the new goods supplied in lieu thereof would have had to be paid for in cash.

[*Tomkins v. Saffery*, 3 App. Cas. 213, at 235, 47 L.J. Bk. 11, applied].

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

A motion on behalf of the trustee in bankruptcy to set aside payments of money and transfers of property made by the debtor to Campbell, Wilson & Strathdee Ltd. on the ground that the same gave a preference to Campbell, Wilson & Strathdee Ltd. over the other creditors within the meaning of sec. 64 of *The Bankruptcy Act* [9 C.B.R. 141]. The motion was also for an accounting for certain goods which had been returned by the debtor to said company within three months prior to the filing of the petition in bankruptcy. The debtor in order to hold a sale by which he hoped to reduce his stock and accumulate some ready money had exchanged with said company said goods, then unsaleable, for other goods which were more readily saleable.

MacDonald, J. **(oral) (after stating the nature of the motion):**

1 Before any such payment or transfer of property can be set aside these conditions must be fulfilled as summarized in 2 *Halsbury*, 1st ed., p. 280:

> (1)The debtor must at the date of the transaction be unable to pay from his own money his debts as they fall due; (2) the transaction must be in favour of a creditor, or of some person in trust for a creditor; (3) the debtor must have acted with the view of giving such creditor a preference over his other creditors; (4) the debtor must be adjudged bankrupt on a bankruptcy petition presented within three months after the date of the transaction sought to be impeached.

2 Now in this case I find on the evidence the following facts: That any payment made by the debtor to Campbell, Wilson & Strathdee Ltd. within the three months in question were payments made for goods delivered during that period or for goods delivered in the month prior thereto, the ordinary time of credit for which expired during the period in question. I also find as a fact that during all that time there was the hope, however ill founded on the part of the debtor, that he would be able to extricate himself from his financial difficulties and that these goods were supplied with the hope of enabling the debtor to realize his expectations. As to the return of goods by the debtor to the creditor I am satisfied on the evidence that the same was done through an arrangement by which other goods would be supplied to the debtor in their place and the fact exchanges were made did not affect the assets of the bankrupt available for distribution among other creditors, because if these goods had not been returned to Campbell, Wilson & Strathdee Ltd. the new goods supplied in lieu thereof would have had to be paid for in cash.

3 Under this state of facts the question arises whether what the debtor did was done with a view of giving a preference to Campbell, Wilson & Strathdee Ltd. In *2 Halsbury*, 1st ed., p. 282, I find the following:

> Again, in order that a transaction may be a fraudulent preference, not only must the person who derives the advantage from the transaction be a creditor, but the act must have been done in his favour, and not in favour of anyone else. Where, therefore, although the creditor be in fact preferred in the sense of obtaining a benefit not shared by the debtor's other creditors, yet the act was done by the debtor with a view of benefiting himself, and not the creditor, then, even if all the other elements of fraudulent preference be present, the transaction cannot, on the ground that the creditor derives an advantage, be set aside.

4 For instance in *Sharp v. Jackson*, [1899] A.C. 419, 68 L.J. Q.B. 866, the facts were that a trustee who was in solvent circumstances and had committed a breach of trust, on the eve of insolvency, conveyed properties to make good his breaches of trust. It was held that as such conveyance took place with a view of protecting the trustee from the consequences of the breaches of trust, it was not a preference within the meaning of the Act. But perhaps the statement of the law which best fits

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

the facts of this case is that by Blackburn, L.J., in *Tomkins v. Saffery* (1877), 3 App. Cas. 213, at 235,[1] where he says:

> Now I think you must say it is not with a view to give an undue preference, if a man makes a payment to a creditor in the ordinary course of business. Supposing a bankrupt, although knowing that he is very likely to stop payment next week, struggles on and makes a payment without being particularly asked; supposing he pays his debts and sends his money to meet his bills on those days on which they become due, and does other things so as to keep himself alive and in good credit for the time; that would not have been undue preference I think, because those payments were not made 'in favour of' certain creditors as against others, but were made in the hope — a desperate hope perhaps — that if he were able to keep himself alive something might turn up in his favour.

5 That is a statement so applicable to the facts of the present matter that I find it unnecessary to add anything. The motion is dismissed.

Footnotes

1 Although the Law Journal reports the same case, 47 L.J. Bk. 11, the report therein does not include the statement quoted. — Ed.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 16

1994 CarswellAlta 353
Alberta Court of Queen's Bench, In Bankruptcy

Norris, Re

1994 CarswellAlta 353, [1994] A.W.L.D. 831, [1994] A.J. No. 699, [1995] 1 W.W.R. 292, 161 A.R. 77, 23 Alta. L.R. (3d) 397, 28 C.B.R. (3d) 167

Re Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, as amended; Re bankruptcy of DAVID CARL NORRIS

Agrios J.

Judgment: September 21, 1994
Docket: Doc. Edmonton BKCY 39553

Counsel: *K.A. Rowan* , for Browning, Smith Inc., trustee in bankruptcy of David Carl Norris.
S.J. Bocock , for Minister of National Revenue.

Subject: Corporate and Commercial; Insolvency

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy --- Avoidance of transactions prior to bankruptcy — Fraudulent preferences — Doctrine of pressure

Revenue Canada required to pay trustee amount received from bankrupt.

Revenue Canada was owed money by the bankrupt. It made several demands for payment. The bankrupt requested and was granted a one-month grace period, after which he paid $8,548.40 to Revenue Canada. Two months later, he made an assignment in bankruptcy. The trustee in bankruptcy applied for a declaration that the payment to Revenue Canada was a fraudulent preference within the meaning of s. 95 of the *Bankruptcy and Insolvency Act* and for an order requiring the payment to the trustee of $8,548.40.

Held:

The application was allowed.

Revenue Canada could rebut the statutory presumption under s. 95 by showing either that: (1) it was a diligent creditor, or (2) the payment was made in the ordinary course of business. Revenue Canada's forwarding of three letters to the bankrupt and the granting of a grace period could be described as steps that an ordinary creditor would take. Its actions

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

were not sufficiently aggressive as to create an imminent business or personal crisis for the bankrupt. Had they been so, Revenue Canada would have rebutted the statutory presumption. As Revenue Canada did not constitute a trade creditor of the bankrupt, it could not be said that it received the payment in the ordinary course of business.

Table of Authorities

Cases considered:

Coopers & Lybrand Ltd. v. O'Brien Electric Co. (1983), 47 C.B.R. (N.S.) 243, 48 N.B.R. (2d) 189, 126 A.P.R. 189 (Q.B.) — *referred to*
Houston v. Thornton (1973), 18 C.B.R. (N.S.) 102 (Ont. S.C.) — *referred to*

Statutes considered:

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

s. 95

s. 95(2)

Application by trustee in bankruptcy for declaration that payment to Revenue Canada was fraudulent preference.

Agrios J. :

1 In this bankruptcy I held that a payment of $8,548.40 made to Revenue Canada was a fraudulent preference within the meaning of s. 95 of the *Bankruptcy and Insolvency Act* .

2 At the time the decision was rendered, I indicated to counsel that should they require written reasons I would be happy to provide such and I now do so at the request of counsel for Revenue Canada.

Facts

3 The facts are not in issue. On November 25, 1992 Revenue Canada received a payment on taxes of $8,548.40 from David Carl Norris. On January 26, 1993 Mr. Norris made a voluntary assignment into bankruptcy.

4 Revenue Canada had made a series of demands on the bankrupt. There was a letter on September 12, 1992, a notice of October 9, 1992 amending the balance owing and again demanding payment, and a final letter on October 24, 1992 making still a further demand and stating that if arrangements were not made for payment, legal action such as garnishee of income

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

or instructions to the Sheriff to seize and sell assets might be made. On October 29, 1992 the bankrupt called Revenue Canada in response to the last letter, and requested a one-month grace period, which was granted and the aforementioned payment was received on November 25, 1992.

Issues

5 There is no serious dispute that the prima facie presumption under s. 95 as raised by the Trustee had established the three required criteria, namely:

1. that the transfer took place within three months of bankruptcy;
2. that at the date the transfer was made, it gave the creditor a preference in fact;
3. that the debtor was an insolvent person at the date of the payment.

6 Section 95(2) of the Act provides that the presumption may be rebutted on a balance of probabilities that the dominant intention of the debtor was not to prefer the creditor. There were only two issues that Revenue Canada could use to rebut the presumption:

1. they were a diligent creditor;
2. alternatively, the payment was made in the ordinary course of business.

Ordinary Course of Business

7 I have accepted the submission of counsel for the Trustee. As stated in its brief of law, all of the cases cited by Revenue Canada can fairly be characterized as payments made by the debtor in the ordinary course of its business to trade creditors for two reasons Firstly, so that the bankrupt might take advantage of favourable payment terms or, secondly, to secure a continued supply of goods and services from those trade creditors in order that it might continue in its business. There is no doubt that evidence that after payment on account, goods were supplied to the bankrupt by a trade creditor which, under normal circumstances, rebut the presumption. I accept Mr. Rowan's submission that Revenue Canada was not a trade creditor and there was no evidence that would assist Revenue Canada to be considered a trade creditor in having received a payment in the ordinary course of business.

Diligent Creditor

8 The case of *Houston v. Thornton* (1973), 18 C.B.R. (N.S.) 102 (Ont. S.C.) , followed by *Coopers & Lybrand Ltd. v. O'Brien Electric Co.* (1983), 47 C.B.R. (N.S.) 243 (N.B. Q.B.) , is cited for the following proposition [p. 103]:

> Both creditors had substantially overdue accounts and both were exerting every effort to obtain payment of their accounts. As has been so often said, our law does not penalize a diligent creditor. In order for me to set aside these transactions, I must find that there was a fraudulent scheme on the part of the debtor to prefer these creditors over other creditors.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> On the evidence, I cannot find any such scheme. Rather, I think it is a situation where diligent creditors have managed to obtain substantial payments on their accounts at a time when other creditors, who were not as diligent, did not obtain payment.
>
> ... The only reason for making the payments to the respondents was because the respondents were pressing more vigorously than other creditors for payment of their accounts.

9 I have again accepted the submissions of counsel for the Trustee that these authorities are characterized by a theme of an extremely aggressive creditor whose actions would cause an imminent business crisis unless they were dealt with. As Mr. Rowan stated: "The payments were motivated by a desire to 'get the creditor off the debtor's back', and because the continued actions of the creditor would cause an immediate business crisis."

10 Frankly, in my view, the forwarding of three letters, one of which threatened legal action and the subsequent granting of one month's grace period, could best be described as steps that any ordinary creditor would take, making demands and threatening legal proceedings. I accept the proposition that the actions of Revenue Canada, when compared with those in the cited authorities, did not amount to such aggressive action such as to create an imminent business or personal crisis for the bankrupt. Had Revenue Canada in fact taken garnishee proceedings or instructed seizure, I should have held otherwise.

11 Accordingly, as the presumed intention was not, in my view, rebutted on the balance of probabilities, I ordered that Revenue Canada pay the Trustee the sum of $8,546.40.

Application allowed.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 17

1988 CarswellBC 537
British Columbia Supreme Court

Skalbania (Trustee of) v. Wedgewood Village Estates Ltd.

1988 CarswellBC 537, [1988] B.C.W.L.D. 3101, [1988] C.L.D. 1738, [1988] B.C.J. No. 1636, 31 B.C.L.R. (2d) 184, 70 C.B.R. (N.S.) 232

HENFREY SAMSON BELAIR LTD. v. WEDGEWOOD VILLAGE ESTATES LTD. and SKALBANIA

Macdonald J.

Heard: August 8-12, 1988
Judgment: September 7, 1988
Docket: Vancouver Nos. 100456/7 and 1601/82

Counsel: *K.J. Smith* and *B. Toy*, for plaintiff trustee.
T.R. Berger and *G.A. Nelson*, for defendants.
A.D. Louie, for Attorney General for Canada.

Subject: Corporate and Commercial; Insolvency; Constitutional

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy --- Avoidance of transactions prior to bankruptcy — Fraudulent preferences

Bankruptcy --- Avoidance of transactions prior to bankruptcy — Fraudulent and illegal transactions — Reviewable transactions under Act

Constitutional Law --- Charter of Rights and Freedoms — Nature of rights and freedoms — Life, liberty and security — Economic, commercial and proprietary rights

Fraudulent conveyances — Reviewable transactions — Debtor company controlled by husband transferring half interest in hotel to defendant company controlled by wife — Defendant already owning other half interest — Transfer made within one year of debtor filing proposal — Trustee challenging adequacy of consideration — Fair market value of debtor's interest being discounted as ordinary purchaser would not obtain controlling interest — Covenant of indemnity given by wife's company included in consideration — Consideration being $1.18 million (17.5 per cent) less than fair market value of debtor's interest — Court discussing test for conspicuousness — Judgment for trustee for difference between consideration paid and fair market value.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Constitutional law — Husband's company transferring half interest in hotel to wife's company within one year of filing proposal in bankruptcy — Trustee challenging consideration paid and wife raising Charter and Canadian Bill of Rights — Sections 3, 4, and 78 of Bankruptcy Act not infringing rights under Bill of Rights or Charter — Bill of Rights not applying to corporations — Section 7 of Charter not protecting property or pure economic rights — Liberty to contract being pure economic right unless involving some activity already protected under s. 7 — Parliament justified in viewing transactions between married persons as non arm's length — All married persons treated similarly and Bankruptcy Act not being discriminatory under s. 15 of Charter.

Interest — Calculation — Judgment awarded in action concerning reviewable transaction — Prejudgment interest to run from date of appointment of trustee, not date of reviewable transaction.

On 2nd December 1981 N. and his company N.S. Ltd. entered into an agreement for the sale of the company's one-half interest in a hotel to his wife's holding company, the defendant W. Ltd., which was the owner of the other half interest in the hotel. On 4th December 1981 the wife accepted an offer to sell the entire hotel to a third party and on that same day agreed with her husband to increase the consideration payable on the transfer of his company's interest to the defendant. On 26th January 1982, being in tight financial circumstances, the husband agreed to receive two more immediate payments in lieu of the substantially larger future payments which had been agreed to on 4th December 1981. Within a year the husband and his company filed a proposal under the Bankruptcy Act. The trustee brought an action challenging the transfer of the interest to the wife's company under s. 78 of the Bankruptcy Act, claiming that the consideration paid was "conspicuously" less than the fair market value of the interest transferred. The trial judge calculated that the fair market value of the interest exceeded the consideration paid by $2,355,247. Defining "conspicuously" as meaning "striking; manifest, notable or flagrant in the sense that reasonable people would see that they were giving less than fair market value", he found in favour of the trustee. The Court of Appeal ordered a new trial on the basis that the trial judge had: applied the wrong standard with respect to the definition of "conspicuously"; erred in not discounting the fair market value of the interest as a buyer would not obtain control of the hotel; and erred in not adding to the consideration a value for the covenant of indemnity granted by the defendant to N.S. Ltd. At the new trial to determine whether the agreement affected the Bankruptcy Act, the defendants also raised the arguments that ss. 3, 4, and 78 of the Bankruptcy Act infringed their rights under the Canadian Bill of Rights and the Charter of Rights and Freedoms by, inter alia, infringing their liberty to contract, and by discriminating on the basis of marital status.

Held:

Judgment for trustee.

Since a third party purchaser of N.S. Ltd.'s interest would not have gained control of the hotel, the fair market value of the interest should be discounted by $730,000. That would be a reasonable cushion for all the uncertainties the purchaser could face in a situation where the other equal partner would have a considerably different and smaller investment in the business and would possibly hold a different view concerning the use of the assets. The covenant of indemnity was only of nominal value since the defendant, W. Ltd., as a partner was already liable for the debts and in effect was merely waiving its right to contribution from N.S. Ltd. Additionally, there was little risk of claims being made against N.S. Ltd. as the proceeds from the sale of the hotel retired two of the mortgages. Furthermore W. Ltd.'s assumption of the debt worked as an advantage by eliminating the need to raise that portion of the purchase price.

Consequently, the fair market value of N.S. Ltd.'s interest ($6.6 million) exceeded the consideration paid by W. Ltd. by $1.18 million. The ordinary meaning of the word conspicuous as being "plainly evident, attracting notice ... eminent, remarkable, [or] noteworthy" should be applied, and the proper test is whether the difference between fair market value and the consideration received is conspicuous to the court, not whether the parties involved could have seen that they were giving or getting less than fair market value. This test enables the court to consider the particular circumstances of each case, including the percentage difference between fair market value and the consideration actually paid. Here, the $1.18 million was a conspicuous difference because it was "noteworthy" and "plainly evident" being 17.5 per cent of the value of the interest sold by N.S. Ltd. The trustee should have judgment for that amount, plus pre-judgment interest from the date of its appointment.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

The Bill of Rights did not apply as this transaction was between two corporations and the Bill of Rights does not apply to corporations. The fact that the wife was a necessary party to these proceedings under s. 78(2) of the Bankruptcy Act did not change the nature of the transaction. Section 7 of the Charter does not protect property or pure economic rights. While there is a middle ground with respect to the scope of the word "liberty" in s. 7 such that interests with an economic component may be covered, liberty to contract cannot be characterized as anything other than a pure economic right unless the contract involves some activity which itself is a right protected under s. 7. Assuming a corporation is entitled to the benefit of s. 15 of the Charter, there is justification for the view that married persons do not deal at arm's length and, as all married persons are treated similarly under the Bankruptcy Act, there is no discrimination within the meaning of s. 15 of the Charter.

Table of Authorities

Cases considered:

Pac. Mobile Corp., Re; Robitaille v. Indust. l'Islet Inc. (1979), 32 C.B.R. (N.S.) 209 (Que. S.C.) — *referred to*

R. v. Cornell, [1988] 1 S.C.R. 461, 63 C.R. (3d) 50, 4 M.V.R. (2d) 153, 40 C.C.C. (3d) 385, 83 N.R. 384, 27 O.A.C. 360 — *applied*

Tremblay, Re; Re Gingras Robitaille Marcoux Ltée et Beaudry, [1980] C.S. 468, 36 C.B.R. (N.S.) 111 (Que. S.C.) — *applied*

Whitbread v. Walley, [1988] 5 W.W.R. 313, 26 B.C.L.R. (2d) 203 (C.A.) — *referred to*

Wilson v. B.C. (Med. Services Comm.), B.C.C.A., Vancouver Nos. CA007160 & CA007198, 5th August 1988 (not yet reported) — *applied*

Statutes considered:

Bankruptcy Act, R.S.C. 1970, c. B-3

s. 3

s. 4

s. 78

Canada Evidence Act, R.S.C. 1970, c. E-10

s. 4(3)

Canadian Bill of Rights

s. 1(b)

Canadian Charter of Rights and Freedoms

s. 1

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

s. 7

s. 15

Evidence Act, R.S.B.C. 1979, c. 116

s. 10 [am. 1981, c. 10, ss. 19, 20; 1985, c. 51, s. 20]

Action by trustee challenging adequacy of consideration in non arm's length sale of debtor's asset.

***Macdonald J.*:**

1 This action is an attack by the plaintiff trustee on the adequacy of the consideration paid by the defendant Wedgewood Village Estates Ltd. ("Wedgewood"), a company owned and controlled by Eleni Skalbania, to her husband's company ("N.M.S.") in return for the transfer on 2nd December 1981 of N.M.S.'s 50 per cent interest in the Georgia Hotel. The trustee contends that the transaction is governed by s. 78 of the Bankruptcy Act, R.S.C. 1970, c. B-3; that the consideration was "conspicuously less than the fair market value of the property"; and that it is entitled to judgment against Wedgewood for the difference. At the time of the transfer Wedgewood was the owner of the other 50 per cent interest in the joint venture which owned and operated the hotel.

Scope of this trial

2 This hearing was a new trial directed by the Court of Appeal (see (1987), 65 C.B.R. (N.S.) 48, 14 B.C.L.R. (2d) 1, 40 D.L.R. (4th) 216), which set aside the judgment of this court on the original trial (see 59 C.B.R. (N.S.) 38) and directed that:

3 (a) The sum of $739,000, representing costs and fees paid by Wedgewood to First City Investments to finance the purchase of N.M.S.'s 50 per cent interest in the hotel, be added to the consideration received by N.M.S. from Wedgewood.

4 (b) A sum, to be determined at the new trial, be deducted from the value of N.M.S.'s 50 per cent interest by way of a discount for lack of control.

5 (c) There be added to the consideration received by N.M.S. a sum representing the value to be assigned to the promise by Wedgewood to pay off the hotel's indebtedness and to indemnify N.M.S. against any claim arising therefrom.

6 The Court of Appeal then ordered that "subject to the foregoing, there shall be a new trial." Ordinarily, everything is at large on a new trial. The original judgment has been set aside. None of the findings of fact made by the original trial judge are binding. Issue estoppel does not apply. The only limitations on me arise from the specific directions of the Court of Appeal in respect of those matters enumerated above, each of which has the effect of narrowing the difference between the fair market value of N.M.S.'s 50 per cent interest in the hotel and the consideration received for it from Wedgewood.

WestlawNext® CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

7 However, the parties quite wisely chose to present fresh evidence directed in large part only to the "discount for lack of control" and "covenant to indemnify" issues. By agreement, all of the evidence before the court on the earlier trial is also evidence before me. Thus, for all practical purposes my consideration of the facts is limited to:

8 (a) Fixing the amount of the discount for lack of control;

9 (b) Fixing the value of the covenant to indemnify;

10 (c) Recalculating the difference between the fair market value of N.M.S.'s interest in the Georgia Hotel and the consideration which it received for that interest from Wedgewood by adjusting the calculations at the earlier trial;

11 (d) Deciding whether or not that revised difference is "conspicuous";

12 (e) If the answer to (d) is in the affirmative, determining whether or not ss. 3, 4, and 78 of the Bankruptcy Act are of no force and effect because they are inconsistent with the Charter of Rights or because they infringe the rights of the defendants under the Bill of Rights by restricting liberty to contract, by infringing the principles of natural justice in deeming a transaction between husband and wife to be one which is other than at arm's length (and thus reviewable), and by discriminating on the basis of married status.

13 While it is theoretically open to me to go completely behind the findings of fact which resulted from the first trial, even to the extent that those findings were adopted by the Court of Appeal, I have no intention of doing so. Indeed, the position of the parties is that there is no need to do so except in respect of those matters specifically directed by the Court of Appeal and two further questions of fact, namely:

14 (a) Whether Sched. "A" to the reasons of the original trial judge should be modified by deleting costs of disposition ($317,652) in arriving at the adjusted book value of the 50 per cent interest of N.M.S. in the joint venture which owned and operated the Hotel Georgia.

15 (b) Whether the bankrupt and the defendants (Mr. and Mrs. Skalbania and their respective companies) were in fact not dealing at arm's length. If so, the presumption in s. 3(3) of the Bankruptcy Act, R.S.C. 1970, c. B-3, which formed the foundation of the first trial, need not be relied upon by the trustee, and the attack on that presumption by the defendants on constitutional grounds (the Charter and the Bill of Rights) need not be considered.

16 While I propose to deal with those additional questions, I am proceeding otherwise on the basis that the facts found by Taylor J. in his reasons of 20th February 1986 following the first trial (as modified regarding inventories on 27th May 1986) still stand and are the foundation on which I must build in respect of my determination of the issues which remain.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

The background

17 Full details of the history of the involvement of Mr. and Mrs. Skalbania and their respective companies in the Georgia Hotel are set out in the reasons for judgment of Taylor J. (20th February 1986) and in the reasons for judgment of the Court of Appeal (2nd June 1987). Suffice it to say here that, through their respective companies (N.M.S. for Mr. Skalbania and Wedgewood for Mrs. Skalbania), they each owned 50 per cent of the joint venture or partnership which operated the hotel. Wedgewood actually ran the business, although there was no formal operating agreement. Wedgewood was the registered owner of the assets, in trust for the partners, either of whom could call for title at any time. However, it was understood that N.M.S. would not encumber its interest. Each partner had a right of first refusal with respect to a sale of a joint venture interest of the other. N.M.S. was obliged to provide two thirds of the working capital required for the hotel operation.

18 Taylor J. found that the value of the hotel property on 2nd December 1981 (the date of the purchase by Wedgewood of the N.M.S. 50 per cent interest) was $24,158.676. That value was derived from a sale by Wedgewood of the hotel to Mr. Hii within a week of 2nd December. No attack has been made on that finding. It is the fair market value of N.M.S.'s 50 per cent interest in those assets and in the hotel business for which they were being used which is in issue.

19 While the chronology of the sale by N.M.S. to Wedgewood is fully reviewed in the earlier judgments, there are some features thereof which are so significant as to justify repetition here.

20 (a) Wedgewood regarded its investment in the Georgia Hotel as a lifelong one. Arrangements were in place with the Royal Bank to refinance a $5 million mortgage on the hotel which came due on 30th November 1981.

21 (b) N.M.S. was desperate for funds to pay its creditors and wished to raise money on the security of its interest in the hotel (something it had agreed not to do) or to sell that interest (even in the face of Wedgewood's right of first refusal) or to influence the sale of the hotel itself so that the joint venture could be liquidated.

22 (c) N.M.S. negotiated the First City Investments loan to Wedgewood to enable it to purchase the N.M.S. interest in the joint venture. That purchase was a condition of the loan; First City would not advance funds to N.M.S.

23 (d) That loan made it inevitable that the hotel be sold. The business was incapable of carrying that extra debt load.

24 (e) The sale price set out in the 2nd December 1981 agreement between N.M.S. and Wedgewood for the sale and purchase of the 50 per cent interest bore no relationship, except by coincidence, to market value. That price was a function of the moneys which First City had agreed to make available. To that amount was added alleged "debts" of N.M.S. to Wedgewood totalling some $1.5 million plus one half of the indebtedness on the hotel, which Wedgewood assumed. Those three items (disregarding the subsequent inability of Wedgewood to justify some of the $1.5 million indebtedness) totalled $11,472,500. Thus, the price which Wedgewood agreed to pay on 2nd December 1981 for the N.M.S. interest would "suggest" a fair market value of about $23 million for the hotel assets.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

25 The Hii sale was for $30.5 million but with only $7 million due on closing, another $3 million due one year later and the $20.5 million balance due 1st November 1983 (some two years later). It is Taylor J.'s calculation of the present value on 2nd December 1981 of such future payments that results in the value of the hotel being fixed at $24,158,676 on that date. As a result of the Hii offer, Wedgewood agreed on 4th December 1981 to increase the price it was paying to N.M.S. for its 50 per cent interest. That increase was to consist of one half of all moneys received from Mr. Hii in excess of $25 million. That excess would not, of course, be received until two years had elapsed.

26 That delay proved unacceptable to Mr. Skalbania. The demands on N.M.S. for cash had a much shorter fuse. In January 1982 he pressured Wedgewood into giving him two $500,000 payments, one forthwith and the second in December 1982, in lieu of his right to receive future payments under the 4th December 1981 amendment.

27 It is not difficult to understand the reaction of the trustee and the creditors to a sale of the bankrupt's interest in the hotel where:

28 (a) The initial agreement fixed a price which bore no relationship to market value and in which market value was not even a consideration; and

29 (b) Even the subsequent adjustment of that price to more closely reflect the value of an actual sale which had occurred was bargained away by the bankrupt for less than its real value.

30 However, in determining the fair market value of the N.M.S. 50 per cent interest in the joint venture on 2nd December 1981, it is not the particular situation of Mr. Skalbania that I must consider. The experts who testified on this new trial all agreed that fair market value is the highest price available in an open and unrestricted market between informed and prudent parties acting at arm's length and under no compulsion to act. That definition assumes a notional transaction where the buyer and seller negotiate a price reflective of the highest price a prudent purchaser would be willing to pay and the lowest price a prudent vendor would be willing to accept, assuming both are fully informed of all relevant factors and neither are under any compulsion to transact. That approach rules out any consideration of the financial pressures which were on N.M.S. through Mr. Skalbania. It also rules out attributing any special value of N.M.S.'s 50 per cent interest to Wedgewood, because even though Wedgewood did achieve control by purchasing the N.M.S. interest, it was the only purchaser who could have done so. Thus, theory demands that Wedgewood need pay only $1 more than any other buyer would be prepared to spend.

31 The Court of Appeal adopted the argument of the defendants that anyone purchasing Mr. Skalbania's interest would not have acquired control of the joint venture in which Wedgewood was the other party, and would not in those circumstances be willing to pay the same price as he would for a controlling interest. There would have to be a discount for lack of control. Thus, the direction in the formal judgment of the Court of Appeal that "a sum by way of discount for lack of control shall be deducted from the fair market value of the interest" of N.M.S.

Adjusted book value

32 The defendants suggest that the starting point is $7,011,818.00, being the figure determined by Taylor J. to be the fair market value of the N.M.S. interest in the hotel venture. That calculation adjusts the N.M.S. partnership account to reflect the

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

market value of the hotel lands based on the present value of the Hii sale, and then deducts the costs of that sale such as real estate fees, legal fees and penalties on prepayment of a mortgage.

33 The Court of Appeal expressly disagreed with the approach of Taylor J. to the fair market value of the N.M.S. interest. It said [at p. 9], "The issue is not what Mr. Skalbania might have realized under some other arrangement such as a dissolution (a matter of pure speculation) but rather what was the fair market value which would be paid for his one- half interest by a third party as of 2nd December 1981." The trustee argues from that for an adjustment to Taylor J.'s fair market value calculation by putting the costs of disposition back into Sched. "A" to produce an "adjusted book value" rather than a "fair market value". I agree.

34 On a sale of the N.M.S. 50 per cent interest, the hotel assets are not being sold and no adjustment in that regard is appropriate. If N.M.S. is obliged to pay a commission on the sale of its 50 per cent interest, that is not a factor in the calculation nor of any interest or concern to the purchaser. I adopt the reasoning of Mr. M.D. Bowie in that regard on pp. 4-6 of his report, which is marked Ex. 30 on this new trial. By adding back 50 per cent of the costs of disposition, the adjusted book value of the N.M.S. 50 per cent share becomes $7,329,470. That is the starting point for my calculations.

The discount for lack of control

35 This is the issue crucial to the outcome of this litigation on the facts. I heard evidence from a number of expert witnesses on the quantum of the appropriate discount for lack of control and the considerations which would be in the minds of theoretical prudent and knowledgeable parties in respect of the same. That opinion evidence ranges all the way from a nominal discount to one of almost $2 million (about 20 per cent of the adjusted book value of the N.M.S. 50 per cent interest).

36 At p. 9 of the judgment of the Court of Appeal (see 14 B.C.L.R. (2d) 1), the court states that "the trial judge ought to have reduced the fair market value of his [N.M.S.] interest by $350,590." Counsel agree that I am not bound by that statement and that it must be read, in light of the balance of the judgment, as including the words "on the only evidence before him on the issue of a discount for lack of control ... etc. ..." The formal judgment of the Court of Appeal directs that "a sum by way of discount for lack of control shall be deducted ..." No amount is specified. I agree with counsel that the amount of the discount for lack of control is at large.

37 It must be kept in mind that the $24 million (approximately) market value of the hotel itself, which was fixed by Taylor J. on the basis of the Hii sale, bears no resemblance to the value of the hotel as a going concern on 2nd December 1981. It is common ground that the income earning capacity of the hotel on that date would produce a capitalized value of something in the range of $16 million. Thus, the Hii price, and the $24 million present value thereof, was derived not from the hotel's prospects as an ongoing business operation, but from its potential for redevelopment.

38 Any purchaser of the N.M.S. interest at that price (50 per cent of $24 million) would have had to assess the risk that redevelopment might be blocked by Wedgewood. In that event, the only alternative would be sale of the hotel property. Thus, the expenses of a sale to realize the investment would be factored in as a risk. The $317,652 which I earlier added back to Taylor J.'s dissolution value to reach an adjusted book value must be the minimum discount for lack of control.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

39 In addition to costs of disposition, there is the risk that Wedgewood would not agree to a sale, giving rise to both delay and the danger of facing losses on a forced sale. Then there are the particular characteristics of the N.M.S. interest which would call for an assessment of risk: the obligation to provide two thirds of the working capital; the potential effect on the market of the rights of first refusal; the agreement not to encumber the N.M.S. interest, etc. The N.M.S. interest was one of two equal 50 per cent interests and thus neither would have control. Because they were partnership interests, a right to a dissolution did exist. Wedgewood did not have an agreement which permitted it to manage for any specific term and, for at least the next two years, cash flow was expected to cover debt servicing requirements.

40 After reviewing the opinion of the experts and the factors outlined by each of them in support of their respective conclusions, I have decided that 10 per cent is the appropriate discount for lack of control. That amount ($732,947; say $730,000) is more than double the rateable share of a 50 per cent partner of the costs of disposition and is, in my view, a reasonable cushion against all the uncertainties which arise out of lack of control in a situation where the other equal partner has a considerably different (and a much smaller) investment in the business and perhaps a different view of the use to which the assets of the joint venture should be put.

41 There must be some difference between the amount which N.M.S. could realize on a sale of the hotel assets and what a notional purchaser would pay for N.M.S.'s 50 per cent interest. No such purchaser would pay a dollar merely to get a dollar back. On the other hand, once the amount of the discount exceeds, in the eyes of a vendor under no compulsion to act, his time, expense and delay in realizing his interest elsewhere or by other means, that vendor will refuse to sell. I have concluded that $730,000 is the appropriate discount in all the circumstances here. That leaves me with a fair market value of $6,599,470 for the N.M.S. 50 per cent interest in the Georgia Hotel joint venture, calculated as follows:

Fair market value as per Sched. "A" to reasons of Taylor J.	$7,036,818
Adjustment for inventory (supplementary reasons of Taylor J.)	-25,000

	$7,011,818
Delete costs of disposition	+317,652

	$7,329,470
Less 10 per cent discount for lack of control	-730,000

	$6,599,470

42 To make that number easier to handle, I have rounded it to $6.6 million.

The First City costs

43 The Court of Appeal directed that "the sum of $739,000 should be included in the consideration received by N.M.S. (Mr. Skalbania)." Thus, the consideration found by Taylor J. ($4,681,571) must be increased by the amount of the First City costs and fees, resulting in the consideration paid (before any determination of the value of the covenant to indemnify) increasing to $5,420,571, which I will round to $5.42 million.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

The covenant to indemnify

44 By the terms of their 2nd December 1981 agreement, Wedgewood covenanted and agreed to indemnify and save harmless N.M.S. from any and all claims arising out of the indebtedness then charging the hotel. The Court of Appeal has directed that the value of that covenant, as part of the consideration received by N.M.S. for its 50 per cent interest in the joint venture, "be added to the consideration." I consider that covenant to have a nominal value and I propose to comply with the direction of the Court of Appeal by adding $1 to the consideration received. Thus, my round figure of $5.42 million consideration paid remains unchanged.

45 The defendants approach this question by comparing the covenant (of a purchaser to assume existing encumbrances and to indemnify the vendor against them) with the guarantee of a loan by a third party or a take-out mortgage commitment. I do not consider those to be apt comparisons. Wedgewood, as one of the joint venturers, was already liable for these debts. In one sense, it was only Wedgewood's right of contribution from N.M.S. that was being waived.

46 The value of the covenant to indemnify is a direct function of the risk associated with it. Since the fourth and fifth mortgages were paid in the course of closing the Hii sale, and the second mortgage refinanced in accordance with the Royal Bank commitment after N.M.S. ceased to be a partner, there was no possibility of a claim against N.M.S. in respect of those three mortgages to which the indemnity might apply.

47 The first mortgage carried a rate of 9 3/8 per cent, substantially below the market rate at 2nd December 1981, and its current value did not likely exceed $4 million (despite an outstanding balance of some $5.2 million). Thus, the real advantage of the covenant to assume was in Wedgewood rather than N.M.S. Wedgewood, by being allowed to assume the existing indebtedness, was spared the extra cost of raising that portion of the purchase price in the current market. One need only review the terms of the First City loan negotiated by Mr. Skalbania to assess the value of that advantage.

48 Such an arrangement (the assumption of existing debt by a purchaser and the indemnification of the vendor against the same) is standard in a high percentage of real estate transactions. The market does not calculate or factor in a value to the vendor of such a covenant. Why? The vendor, if he is concerned about his covenant on the existing encumbrances, need simply bargain for cash, pay those obligations from the proceeds, and be rid of them. He may, however, by offering existing financing to the purchaser, enhance the price at little or no risk to himself, particularly if the interest rates on the existing mortgages are favourable and there is a significant spread between the debts assumed and the market value.

49 Here, the debts in respect of which N.M.S. was indemnified represented the first $5.2 million and the last $1.8 million of encumbrances totalling $12.2 million. The market value of the hotel has been established by the Hii sale at $24 million. The chances of a 50 per cent drop in market value, a drop which would have to occur before any claim for a deficiency on the $1.8 million third mortgage might arise, seems to me to be too remote to justify placing a value on the risk involved.

50 I accept the conclusion of Mr. Adler that "the promise by Wedgewood to indemnify [N.M.S.] ... had an insignificant value." I expressly reject the approach of the defendants' experts in equating this covenant to a guarantee or take-out fee which would involve a charge of 1 to 2 per cent per annum. I reject as well their application of that fee, at an unchanging rate,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

to the full balance of all three mortgages when N.M.S. had no liability on one of them (the second) and the risk in respect of the first was obviously less than that on the third.

51 Perhaps the strongest support on the evidence for placing only a nominal value on the covenant to indemnify lies in the cross-examination of Mr. Harry, an expert witness who testified for the defendants at both this and the earlier trial. In his report (Ex. 25, Tab 4) submitted in evidence on this trial pursuant to s. 10 of the Evidence Act, R.S.B.C. 1979, c. 116, Mr. Harry suggested that a value of between $315,000 (1 per cent) and $630,000 (2 per cent) be ascribed to the covenant. He preferred "the high end of the range". And yet, on cross-examination, he conceded that despite preparing an opinion for the defendant Wedgewood in respect of an income tax claim arising out of the transaction in question here and several opinions for the earlier trial, he never ascribed a value to the covenant to indemnify in any of those opinions. It never occurred to him until he read the judgment of the Court of Appeal that such a covenant might have a separate value. He has never seen that done except in MURB tax shelter transactions where the object is to load the purchase price in the direction of soft costs; those are not "normal commercial transactions". He conceded further that the difference of 100 per cent between the hotel debts not discharged on the closing of the sale to Hii and its market value based on that sale was enough to cover any market shrinkage and that it was most unlikely that N.M.S. would be called upon to pay any of those loans in light of the value of the underlying assets of the joint venture.

A conspicuous difference?

52 Having done the mathematics required of me by the Court of Appeal, I arrive at a difference of $1.18 million between the fair market value of the N.M.S. 50 per cent interest and the consideration which it received for that property from Wedgewood. Section 78 of the Bankruptcy Act now requires me to consider whether that difference is "conspicuous". It reads, in part:

> 78. (1) ...
>
> (2) Where the court ... finds that the consideration given ... was conspicuously ... less than the fair market value of the property ... the court may give judgment to the trustee against the other party to the transaction ... for the difference ...

53 On his reasoning at the earlier trial of this action, Taylor J. found a difference of $2,380,247 or (in round figures) $2.38 million. He found that difference to be conspicuous and awarded judgment to the trustee accordingly. The difference at which I have arrived is almost exactly one half of that found by Taylor J. Does that make a difference to the outcome of these proceedings?

54 Relying on *Re Pac. Mobile Corp.; Robitaille v. Indust. l'Islet Inc.* (1979), 32 C.B.R. (N.S.) 209 (Que. S.C.), where Jacques J. construed the meaning of "conspicuously" as "striking, notable or in a flagrant or gross manner", Taylor J. noted [at p. 68] that the expression was unusual and called for proof of more than the existence of a significant difference. He thought that "conspicuously" meant "'striking', 'manifest', 'notable' or 'flagrant'", the words used by Jacques J., in the sense that reasonable people would see that they were giving less than fair market value.

55 But the Court of Appeal held that was "a wrong standard" to apply. It held [at p. 17] that:

> Whether or not a reasonable person in the position of the defendants having the assistance of competent professional advice would be bound to see that the fair market value of the interest transferred ... was much greater than the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> consideration given ... was irrelevant ...

Unfortunately, the Court of Appeal failed to set out the correct standard. The only guidance which it provided was [p. 17]:

> Ultimately, the issue to be resolved, the extent of the disparity, rests on an assessment of fair market value. That requirement by s. 78 applies not only to determining the value of Mr. Skalbania's interest but also to determining the consideration he received for it.

56 I do agree with Taylor J. that there is no particular percentage difference beyond which it can be said with assurance that the difference is conspicuous. It was open to Parliament to establish such a definite criterion. It chose not to do so. Nevertheless, the percentage which the difference is of the fair market value may be a significant factor in determining whether it is or is not "conspicuous". A $50,000 difference would certainly be conspicuous in the sale of a $100,000 asset in a reviewable transaction. It would likely not be conspicuous in the sale of a $1 million asset.

57 I also agree that the particular circumstances of the case must be examined and the decision (as to whether or not the difference was conspicuous) reached in the light of that examination. Finally, I accept that the ordinary meaning of the word "conspicuous" connotes "plainly evident; attracting notice; hence, eminent, remarkable, noteworthy".

58 I have concluded that the criticism by the Court of Appeal of the standard applied by Taylor J. was based not so much on the meaning he ascribed to the word "conspicuous", but on the person to whom it must so appear. As the plaintiff submits, if the difference must be conspicuous to the parties at the time, the test would encourage camouflage and deception and frustrate the purpose of s. 78. The test must be whether or not the difference is conspicuous to the court, not whether the parties knew or ought to have known so at the time of the transaction. Such a test enables the court to consider all the relevant factors, including, in this case, the fact that the present value of the $30.5 million Hii sale was only $24 million in the light of the then current interest rates.

59 I confess to having been troubled by the fact that, had it not been for the 26th January 1982 amendment under which N.M.S. received two payments of $500,000 each (one forthwith and one on 2nd December 1982) in lieu of one half of all sales proceeds over $25 million in accordance with the 4th December 1981 amendment which had been made in contemplation of accepting the Hii offer, there would be little or no difference between fair market value and consideration. However, the manner in which the consideration becomes conspicuously less is immaterial. Whether the difference arises out of the original transaction between parties who are not dealing at arm's length or from a subsequent modification thereof which heavily discounts a future payment can make no difference to the essential question of whether the difference between the fair market value of property and the consideration paid for it was conspicuous.

60 $1.18 million is not an insignificant sum. I consider it to be "noteworthy" and "plainly evident" even in the context of a partnership interest with a fair market value of $6.6 million. The difference is 17.5 per cent of the value, not an insignificant percentage. I find $1.18 million to be a conspicuous difference within the meaning of s. 78 of the Bankruptcy Act. Subject to the arguments of the defendants under the Charter and the Bill of Rights, the trustee is entitled to judgment against the defendant Wedgewood in that amount.

Non arm's length as a fact

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

61 In an effort to finesse the Charter argument, the trustee urged that I find as a fact on all the evidence that Mr. and Mrs. Skalbania (through their respective companies) were not dealing at arm's length. Such a finding would obviate the need for the trustee to rely upon the presumption in s. 3 of the Bankruptcy Act, which deems that related persons (or corporations controlled by them) are not dealing at arm's length and renders any transaction between them reviewable, and would thus avoid the need to consider whether that presumption offends the Charter or the Bill of Rights, or both.

62 There is no question on the facts here that Wedgewood, at Mrs. Skalbania's direction, adopted a course of conduct contrary to her own wishes to accommodate the needs of her husband and N.M.S. Their married relationship clearly affected this transaction. But it would be going too far to say that she acted as he directed or was forced by him to enter into the transaction between them which is the subject of this litigation.

63 It becomes a question of the proper test to apply. If there must be "one directing mind for both parties to the transaction", then I am not prepared to find that the transaction in question here was non arm's length in fact. On the other hand, if the test is simply whether one of the parties is in a position to exercise control, influence or moral pressure on the free will of the other, the result might well be different. I prefer the standard suggested in *Re Tremblay; Re Gingras Robitaille Marcoux Ltée et Beaudry*, [1980] C.S. 468, 36 C.B.R. (N.S.) 111 at 112 (Que. S.C.), which is somewhat between those two extremes. I find that Mr. Skalbania was not in a position to pervert the ordinary rules of supply and demand in transactions with Mrs. Skalbania in the sense that he could force her to transact for a consideration in his favour which was substantially less than market value.

64 While I accept that Mrs. Skalbania did not wish to acquire her husband's 50 per cent interest in the hotel and did so only to assist him in meeting the financial crisis which he was facing, I am not prepared to find as a fact that they were not dealing at arm's length. Thus, the trustee is obliged to rely on the s. 3(3) presumption and the arguments of the defendants under the Charter and the Bill of Rights must be dealt with.

The Bill of Rights

65 The Canadian Bill of Rights, 1960, provides, inter alia, that certain human rights and fundamental freedoms, including the right to enjoyment of property, the right not to be deprived thereof except by due process of law and the right to equality before the law, exist in Canada. It goes on to state that every law of Canada is to be so construed and applied as not to abrogate or infringe such rights. The defendants say that the combination of ss. 3, 4 and 78 of the Bankruptcy Act are of no force and effect insofar as those sections infringe their liberty of contract. In contrast to the Charter, property rights are expressly mentioned in the Bill of Rights.

66 The short answer to that proposition is that the transaction in question was between two corporations and the Bill of Rights does not apply to corporations, a matter which the defendants concede. The fact that Mrs. Skalbania is a necessary party to these proceedings under s. 78(2) of the Bankruptcy Act does not convert the transaction between N.M.S. and Wedgewood into a contract to which she is a party in her personal capacity.

67 The "right to equality" argument under s. 1(*b*) of the Bill of Rights is met by the "federal objective that provides a reasonable justification for the particular inequality" and the fact that there is "some legitimate basis in the ... legislative policy" for treating related persons differently than unrelated persons insofar as reviewable transactions under the Bankruptcy Act are concerned [*Cornell*, infra, p. 473]. The notion of reviewable transactions was introduced in 1966 to capture

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

transactions disadvantageous to the bankrupt and therefore to his creditors, where the bankrupt was either related to the other contracting party (as defined) or was not in fact dealing at arm's length. Exhibit 28 contains the historical background for the "federal objective" and the "legislative policy" applicable here: see *R. v. Cornell*, S.C.C., No. 19347, 24th March 1988, at pp. 11-12 [now reported [1988] 1 S.C.R. 461, 63 C.R. (3d) 50, 4 M.V.R. (2d) 153, 40 C.C.C. (3d) 385, 83 N.R. 384, 27 O.A.C. 360].

The Charter

68 The first prong of the attack by the defendants on ss. 3, 4 and 78 of the Bankruptcy Act under the Charter relies upon the application of s. 7 thereof (security of the person) to liberty to contract. While it is clear from the recent decision of the Court of Appeal in *Wilson v. B.C. (Med. Services Comm.)*, Vancouver Nos. CA007160 and CA007198, 5th August 1988 (not yet reported) that "liberty" in s. 7 extends beyond the bare legal rights guaranteed by ss. 8 to 14 of the Charter, the court stated expressly that it did not extend to protect property or pure economic rights.

69 The defendants seek to avoid that limitation by characterizing liberty to contract as a legal rather than an economic right, as something a person has as an incident of his or her legal personality. They submit that Mrs. Skalbania's "legal personality" has been diminished by the operation of s. 3(3) of the Bankruptcy Act insofar as transactions with her husband are concerned; that she is deprived of her legal capacity to enter into a non arm's length transaction with her husband. That is analogous, the defendants argue, to the finding in *Wilson v. B.C. (Med. Services Comm.)* that the right of a licensed doctor to participate in the provincial medical plan is not merely the denial of an economic right, but actually a denial of the right to practise a profession.

70 Counsel for the Attorney General for Canada, appearing in response to notice of the attack which was to be made on ss. 3, 4 and 78 of the Bankruptcy Act, analyzed *Wilson v. B.C. (Med. Services Comm.)* and its approach to s. 7 of the Charter in this way:

71 (a) There are two extremes when considering the scope of the word "liberty" in s. 7. The first involves bodily restraint, which is clearly covered. The second involves *pure* economic rights, which are not covered.

72 (b) There is a middle ground, such as was found in *Wilson v. B.C. (Med. Services Comm.)*, where interests with an economic component may be covered. There, the right to work was equated with human dignity and self-respect which, in turn, were held to be an element of "liberty of the person". (And see *Whitbread v. Walley*, Vancouver Nos. CA008522 and CA008519, 12th May 1988 [now reported [1988] 5 W.W.R. 313, 26 B.C.L.R. (2d) 203 (C.A.)], where the opposite result was reached after a similar analysis.)

73 I accept the submission of the Attorney General for Canada that the defendants have not found the "middle ground" such as was the case in *Wilson v. B.C. (Med. Services Comm.)*. I am unable to characterize liberty to contract as anything other than a pure economic right unless the contract involves some activity which is itself a right protected under s. 7 of the Charter.

74 There is also force to the plaintiff's argument that what is really involved here is the business interests of two

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

corporations, something not protected by the Charter. In addition, the plaintiff points out that the alleged interference with the so-called liberty to contract is only to the extent that the contract becomes subject to judicial scrutiny under s. 78 of the Bankruptcy Act. Only where the contract is found to offend the legislation (i.e., where the difference between consideration and fair market value is conspicuous) are there any legal consequences. Even in that event the contract itself is not abrogated; the consequences are that a liability to the creditors of the bankrupt arises by the operation of the Bankruptcy Act. There is no absolute denial of the defendants' "right" to contract.

Discrimination — s. 15 of the Charter

75 The second string in the defendants' Charter bow relies on s. 15, which prohibits discrimination. It now seems settled (see *Whitbread v. Walley*, supra, at p. 22 [pp. 330-31, W.W.R.]) that s. 15(1) is not limited to the enumerated grounds. Here, the defendants submit, the impugned provisions of the Bankruptcy Act discriminate on the basis of marital status. Mrs. Skalbania (and Wedgewood) is denied equality under the law on account of her marital status.

76 Even assuming for the moment that the argument of the defendants based on *R. v. Big M Drug Mart Ltd.*, [1985] 1 S.C.R. 295, [1985] 3 W.W.R. 481, 37 Alta. L.R. (2d) 97, 18 C.C.C. (3d) 385, 18 D.L.R. (4th) 321, 13 C.R.R. 64, 85 C.L.L.C. 14,023, 60 A.R. 161, 58 N.R. 81, successfully overcomes the statement in *Milk Bd. v. Clearview Dairy Farm Inc.*, [1987] 4 W.W.R. 279, 12 B.C.L.R. (2d) 116 at 125 (C.A.), that a corporation is not entitled to the benefit of s. 15, it is nevertheless my conclusion that it is not unfair or unreasonable for Parliament to deem that married persons do not deal at arm's length. This is one of those rare cases where a restricted class is justified. By treating all married persons equally (albeit differently from all unmarried persons) the impugned provisions of the Bankruptcy Act do not offend s. 15 of the Charter. Similarly situated people (married persons) are treated similarly.

77 That restricted view of the appropriate class is justified by these considerations:

78 (a) It is probable, as occurred in this case, that married persons will be influenced by factors other than the rules of supply and demand and other pure economic considerations in their dealings with each other.

79 (b) If obliged to prove that a bargain between spouses was not at arm's length, a trustee is in a difficult position because neither can be compelled to disclose inter-spousal communications (Canada Evidence Act, s. 4(3)).

Charter — s. 1

80 The plaintiff submitted that, if the impugned provisions of the Bankruptcy Act were found to offend either s. 7 or s. 15 of the Charter, they would be saved by s. 1 thereof as a reasonable limit demonstrably justified in a free and democratic society. Were it necessary for me to do so to preserve ss. 3, 4 and 78 of the Bankruptcy Act, I would accept that argument in reliance upon the material contained in Ex. 28. The objectives which the impugned provisions are designed to serve are of sufficient importance to warrant a partial limitation on even a constitutionally protected right.

Judgment

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

81 The plaintiff trustee is entitled to judgment against the defendant Wedgewood Village Estates Ltd. in the sum of $1.18 million. There will be prejudgment interest on that amount calculated at the district registrar's rate from time to time applicable from the date of the appointment of the trustee to this date. I adopt the supplementary reasons of Taylor J., filed 27th May 1986, in that regard.

82 The plaintiff is entitled to its costs of this new trial.

Judgment for trustee.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 18

2002 CarswellOnt 4507
Ontario Superior Court of Justice

Conte Estate v. Alessandro

2002 CarswellOnt 4507, [2002] O.J. No. 5080

Elisa Conte, Executrix and Trustee for Cesidio Conte and Elisa Conte, Plaintiffs and Joe Alessandro Also Known as Giuseppe Alessandro, a Bankrupt, Gregorina Alessandro, Alba Alessandro and A. Farber & Partners Inc., Trustee in Bankruptcy of the Estate of the Said Giuseppe (aka) Joe Alessandro, Defendants

Rouleau J.

Heard: September 17-23, 2002
Judgment: December 10, 2002
Docket: 96-CU-114234

Counsel: *Joseph J. Colangelo*, for Plaintiffs
William G. Dingwall, Q.C., for Defendants

Subject: Contracts; Corporate and Commercial; Torts; Property

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Fraud and misrepresentation — Fraudulent conveyances — Fraudulent intent — "Badges of fraud"

Shortly after plaintiff had commenced debt action against defendant JA for $350,000, JA transferred property to wife, defendant GA, for $2 — Plaintiff was awarded $413,768.33 in debt action — Following judgment against JA, GA executed $225,000 charge on transferred property in favour of daughter — Plaintiff brought action to set aside transfer and mortgage as fraudulent conveyances — Defendants brought counterclaim for declaration that property was beneficially owned by GA and mortgage to daughter was valid — Action allowed; transactions set aside — Counterclaim dismissed — Transfer and mortgage were conveyed with fraudulent intent, as evidenced by numerous badges of fraud surrounding both transactions.

Table of Authorities

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Cases considered by *Rouleau J.*:

Bank of Montreal v. Jory, 39 C.B.R. (N.S.) 30, 1981 CarswellBC 497 (B.C. S.C.) — considered

Koop v. Smith, 51 S.C.R. 554, 8 W.W.R. 1203, 25 D.L.R. 355, 1915 CarswellBC 151 (S.C.C.) — considered

Petrone v. Jones, 33 C.B.R. (3d) 17, 1995 CarswellOnt 312 (Ont. Gen. Div.) — considered

Prodigy Graphics Group Inc. v. Fitz-Andrews, 2000 CarswellOnt 1178 (Ont. S.C.J.) — referred to

Twyne's Case (1601), 76 E.R. 809, 3 Co. Rep. 80b, [1558-1774] All E.R. Rep. 303 (Eng. K.B.) — referred to

Statutes considered:

Assignments and Preferences Act, R.S.O. 1990, c. A.33
Generally — considered

s. 4(1) — referred to

s. 4(2) — referred to

s. 4(3) — referred to

s. 5(1) — referred to

Fraudulent Conveyances Act, R.S.O. 1990, c. F.29
Generally — considered

s. 2 — referred to

s. 3 — referred to

Statute of Uses, R.S.O. 1897, c. 331
Generally — referred to

ACTION by plaintiff to set aside property transfer and mortgage as fraudulent conveyances; COUNTERCLAIM by defendants for declaration of beneficial ownership of property and validity of mortgage.

***Rouleau J.*:**

I. Introduction

1 This action was brought by Cesidio and Elisa Conte ("Cesidio" and "Elisa" respectively) to set aside two non arm's length transactions and to declare them fraudulent and void. The first non arm's length transaction was a conveyance of 1629 James Street, Tiny, Ontario ("the property") from the defendant Giuseppe Alessandro ("Joe") to his wife, the defendant Gregorina Alessandro ("Gregorina"). The second non arm's length transaction was a $225,000 mortgage placed on the property by Gregorina in favour of her daughter, the defendant Alba Alessandro ("Alba"). The plaintiffs also sought other

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

ancillary relief, and the defendants counterclaimed seeking declarations that the property is in fact beneficially owned by Gregorina and that Alba's mortgage is valid.

2 The issue in this action is whether the two transfers of property were fraudulent conveyances: the transfer of property from an insolvent husband to his wife and the subsequent mortgage of the property by the wife to their daughter. I have concluded that both transactions are fraudulent conveyances.

II. The Facts

3 The plaintiff Cesidio died before trial, and the action was continued by his estate. As his death was anticipated, the parties videotaped his testimony which was admitted at trial.

4 The defendant Joe declared bankruptcy in February 2002 and, by order of Wilson J., the plaintiffs were allowed to continue the present action. The trustee in bankruptcy decided not to continue to defend the action and consented to judgment against the bankrupt. For purposes of the trial, therefore, only the defendants Gregorina and Alba defended.

A) The Debt

5 Cesidio and Joe were former partners with two others in a lumber business. In the late 1980s, Joe bought out Cesidio for $400,000 made up of $50,000 cash and a $350,000 promissory note due February 1, 1993. When the note became due in February 1993, the plaintiffs demanded payment but the debt was not paid. Cesidio brought an action for recovery of the $350,000 which resulted in the judgment of Cameron J. dated April 3, 1996. This judgment awarded Cesidio and Elisa Conte $413,768.33 and solicitor and client costs. The judgment bears interest at 10% annually.

6 Despite repeated attempts at collection including a judgment debtor examination, nothing has been paid on this debt. As at the 17th day of September 2002, I was advised that the value of the judgment, with interest, was $642,831.74.

B) The Property

7 In 1972, a numbered company purchased the property that was, at the time, a vacant cottage lot near Georgian Bay. Shortly thereafter the defendant Joe took title of the property in his name "to uses." Although there is conflicting evidence on the point, it appears that the property was purchased as part of an arrangement among several partners to acquire a series of properties, divide these into building lots and resell them at a profit. Because the partners were purchasing several adjoining lots, they purchased these in a sort of "checker board" arrangement putting properties in their names, in the names of their spouses or in joint ownership.

8 According to the testimony of one of the partners, Giuseppe Marchese, the property was one of five properties acquired by him and three other partners, the defendant Joe, Raffaele Morano and Domenic Scroll. Four of the properties (the "Block D properties") were adjoining, and these were registered in each of the names of the defendants, Gregorina and Joe, and in the names of Raffaele "to uses" and Mariaella Morano. The property which was not adjoining to the others was, as set out above, registered in the name of the defendant Joe "to uses." The sale of the Block D properties generated sufficient monies

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

to cover the full purchase price of the five properties. Therefore the remaining property held by Joe for the four partners was the "profit" of the four partners.

9 According to Giuseppe Marchese, sometime later Joe bought out the interest in the property owned by the three other partners paying $3,000 to each of them. No transfer was necessary since the property was already in Joe's name.

10 In August 1994 the property was transferred from Joe "to uses" to Gregorina for nominal consideration. The land transfer tax affidavit stated that the consideration was $2.00 and that Gregorina "has been the sole beneficial owner during the entire period the lands had been registered in the name of Joe."

C) The Mortgage

11 In October 1996, Alba registered a mortgage in the amount of $225,000 against the property. Alba testified that the consideration for the mortgage was a series of payments made by her to Gregorina during the period December 1993 to April 3, 1995. This series of advances had been made under an agreement entered into among the three defendants in December 1993 (the "loan agreement"). According to Alba the advances were made because her mother needed the money.

12 There was a series of thirteen cheques totalling $258,500 entered into evidence. The defendants claimed the cheques were advances made pursuant to the loan agreement. Although the cheques were all drawn on Alba's account, Joe signed every cheque but one. The three payees of the cheques were Alessandro Holding Ltd., Joe Alessandro, and Joe and Gregorina Alessandro jointly. Little is known of the source and use of these funds as the bank statements were not entered into evidence. Alba testified that by the time she reached her early twenties, she had made hundreds of thousands of dollars trading in penny stocks. Again, no documentation was provided in support of this. It also appeared from Joe's testimony that he was a member of the Board or may have played some role in one or more of the companies, the stock of which Alba traded and profited from.

13 Pursuant to the terms of the loan agreement, the advances of $258,500 would have become due in April 1997. It appears that there was no repayment of these sums.

14 The mortgage was registered in October 1996, and full payment was due one year later. During the first year of the mortgage, Gregorina paid interest. However, on October 1, 1997, when the balance became due, payments stopped, and the mortgage went into default.

D) Chronology

15 The plaintiffs suggest that much can be inferred from the timing of various events. They have put forward a chronology setting out the dates of various key events. I agree that the timing is important and therefore will set out some of the key dates and events in this judgment. They are as follows:

September 26, 1972	Purchase of the subject property by Joe "to uses"
February 1, 1988	Joe purchases the lumber business from Cesidio and Elisa for $400,000; $50,000 payable in cash and the balance of $350,000 by promissory note
February 11, 1993	Demand for payment by the plaintiffs of the $350,000 note

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

December 3, 1993	Loan agreement among Alba, Joe and Gregorina pursuant to which Alba agrees to advance sums to Joe and Gregorina in the future. The agreement includes a recital that Joe holds the property in trust for Gregorina
December 6, 1993	First advance made under the loan agreement. It is a $5,000 cheque to Alessandro Holdings Ltd.
June 7, 1994	Statement of Claim issued by Cesidio and Elisa to obtain repayment of the $350,000 debt
August 30, 1994	Transfer of the property from Joe to Gregorina for $2
April 3, 1996	Judgment of Justice Cameron in the debt action granting judgment in the amount of $413,768.33, plus post-judgment interest at 10%. Included in the reasons for Justice Cameron is the statement that alleged oral agreements put forward by Joe did not occur and that Justice Cameron did not believe Joe.
July 3, 1996	Examination in aid of execution of Joe
October 4, 1996	Execution of charge on the property by Gregorina and Joe in favour of their daughter Alba
November 14, 1996	Statement of claim in the present action is issued.

III. Issues

16 The issues in this case are as follows:

(a) was the transfer from Joe to Gregorio a fraudulent conveyance?

(b) was the mortgage from Gregorina to Alba a fraudulent conveyance?

(c) Did the plaintiffs and defendants settle the claim before the trial?

IV. The Law

A) Statutory Framework

17 The plaintiffs rely principally on two statutes, the *Fraudulent Conveyances Act* R.S.O. 1990, c.F-29 and the *Assignments and Preferences Act*, R.S.O. 1990, c.A-33.

18 The relevant portions of the *Fraudulent Conveyances Act* are as follows:

> **2.** Every conveyance of real property or personal property and every bond, suit, judgment and execution heretofore or hereafter made with intent to defeat, hinder, delay or defraud creditors or others of their just and lawful actions, suits, debts, accounts, damages, penalties or forfeitures are void as against such persons and their assigns. R.S.O. 1990, c. F.29, s. 2.
>
> **3.** Section 2 does not apply to an estate or interest in real property or personal property conveyed upon good consideration and in good faith to a person not having at the time of the conveyance to the person notice or knowledge of the intent set forth in that section. R.S.O. 1990, c. F.29, s. 3.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

19 The relevant portions of the *Assignments and Preferences Act* are as follows:

Nullity of gifts, transfers, etc., made with intent to defeat or prejudice creditors

4.-(1) Subject to section 5, every gift, conveyance, assignment or transfer, delivery over or payment of goods, chattels or effects, or of bills, bonds, notes or securities, or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made by a person when insolvent or unable to pay the personal, debts in full or when the person knows that he, she or it is on the eve of insolvency, with intent to defeat, hinder, delay or prejudice creditors, or any one or more of them, is void as against the creditor or creditors injured, delayed or prejudiced. R.S.O. 1990, c. A.33, s. 4(1).

(2) Subject to section 5, every such gift, conveyance, assignment or transfer, delivery over or payment made by a person being at the time in insolvent circumstances, or unable to pay his, her or its debts in full, or knowing himself, herself or itself to be on the eve of insolvency, to or for a creditor with the intent to give such creditor an unjust preference over other creditors or over any one or more of them is void as against the creditor or creditors injured, delayed, prejudiced or postponed.

(3) Subject to section 5, if such a transaction with or for a creditor has the effect of giving that creditor a preference over the other creditors of the debtor or over any one or more of them, it shall, in and with respect to any action or proceeding that, within sixty days thereafter, is brought, had or taken to impeach or set aside such transaction, be presumed, in the absence of evidence to the contrary, to have been made with the intent mentioned in subsection (2), and to be an unjust preference within the meaning of this Act whether it be made voluntarily or under pressure.

Assignments for benefit of creditors and good faith sales, etc., protected.

5.(1) Nothing in section 4 applies to an assignment made to the sheriff for the area in which the debtor resides or carries on business or, with the consent of a majority of the creditors having claims of $100 and upwards computed according to section 24, to another assignee resident in Ontario, for the purpose of paying rateably and proportionately and without preference or priority all the creditors of the debtor their just debts, nor to any sale or payment made in good faith in the ordinary course of trade or calling to an innocent purchaser or person, nor to any payment of money to a creditor, nor to any conveyance, assignment, transfer or delivery over of any goods or property of any kind, that is made in good faith in consideration of a present actual payment in money, or by way of security for a present actual advance of money, or that is made in consideration of a present actual sale or delivery of goods or other property where the money paid or the goods or other property sold or delivered bear a fair and reasonable relative value to the consideration therefor. R.S.O. 1990, c. A.33, s. 5(1).

B) Presumption of Fraud

20 In this type of case it is unusual to find direct proof of intent to defeat, hinder or delay creditors. It is more common to find evidence of suspicious facts or circumstances from which the court infers a fraudulent intent.

21 These suspicious facts or circumstances are sometimes referred to as the "badges of fraud." These badges of fraud are evidentiary indicators of fraudulent intent and their presence can form the *prima facie* case needed to raise a presumption of fraud. These badges of fraud can be traced back to *Twyne's Case* (1601), 3 Co. Rep. 80b (Eng. K.B.) and are elaborated upon in *Prodigy Graphics Group Inc. v. Fitz-Andrews*, [2000] O.J. No. 1203 (Ont. S.C.J.).

22 The presence of one or more of the badges of fraud raises the presumption of fraud. Once there is a presumption, the burden of explaining the circumstantial evidence of fraudulent intent falls on the parties to the conveyance. The persuasive

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

burden of proof stays with the plaintiff; it is only the evidentiary burden that shifts to the defendants.

23 In cases of non arm's length transactions, independent corroborative evidence is strongly recommended but not required if the defendants' evidence is found to be credible. In *Koop v. Smith* (1915), 51 S.C.R. 554 (S.C.C.), Duff J. discussed the need for corroborative evidence in a case involving a transaction between two near relatives for no consideration. Duff J., at p.559 stated as follows:

> I think the true rule is that suspicious circumstances coupled with relationship make a case of *res ipsa loquitur* which the tribunal of fact may and will generally treat as a sufficient *prima facie* case, but that it is not strictly in law bound to do so; and that the question of the necessity of corroboration is strictly a question of fact. Having examined the evidence carefully I am satisfied that the learned trial judge was entitled to take the course he did take and not only that the evidence, as I read it in the record, casts the burden of explanation upon the respondent, but that the testimony given by her brother ought not in the circumstances to be accepted as establishing either the actual existence of the debt or of the *bona fides* of the transaction.

24 Another useful case is *Petrone v. Jones* (1995), 33 C.B.R. (3d) 17 (Ont. Gen. Div.). That case supports the proposition that where, as in the present case, the transferor is transferring the only asset he has remaining with which to pay his debts, there is a presumption of an intent to defeat creditors. Wright J., at p.20, stated the proposition as follows:

> In the absence of any direct proof of intention, if a person owing a debt makes a settlement which subtracts from the property which is the proper fund for the payment of those debts, an amount without which the debts cannot be paid then, since it is the necessary consequence of the settlement that some creditors must remain unpaid, it is the duty of the judge to direct a jury that they must infer the intent of the settlor to have been to defeat or delay his creditors. (*Sun Life Assurance Co. v. Elliott* (1900), 31 S.C.R. 91.)
>
> Even if we consider the direct evidence that the defendant had no intention of defeating, hindering, *et cetera* the claims of the plaintiff, can this evidence remain standing in the face of the undoubted evidence that for the past year the defendant has in fact acted in every way to defeat, hinder or delay the plaintiff's claim?
>
> Even if the defendant had no intention, at the time of the conveyance, of defeating, hindering or delaying the plaintiff's claim, surely his actions since that date, the defence of the claim on the promissory note, the defence of this action, prevent him from raising that lack of specific intent as a defence.
>
> Further: even if the plaintiff did not intend to defeat, hinder or delay this creditor but effected the transfer with a view to defeating, hindering or delaying potential future creditors his defence would still fail.

V. Analysis

25 The plaintiffs' position is that the many suspicious circumstances and badges of fraud surrounding the transfer of the property by Joe to Gregorina and the mortgage by Gregorina to Alba raise the presumption of fraud which has not been rebutted. This leads to the inevitable conclusion that the mortgage and the transfer of the property should both be set aside pursuant to the *Fraudulent Conveyances Act*.

A) Assignments and Preferences Act

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

26 The plaintiffs have also relied on the *Assignments and Preferences Act* as a basis to set aside the mortgage. For the Act to apply, the transferor (or mortgagor) must be insolvent. It may well be that Joe was insolvent at the time that the mortgage was placed on the property, but the mortgage was granted by Gregorina. No evidence was led suggesting that Gregorina was insolvent. Even though Joe, as spouse, consented to the transaction, I do not believe that this would bring the *Assignment and Preferences Act* into play.

B) Requirements to Prove Fraudulent Conveyance

27 The plaintiffs need to show that both the transfer to Gregorina and the subsequent mortgage to Alba were both part of a scheme to defeat, hinder, delay or defraud the plaintiffs contrary to the *Fraudulent Conveyances Act.*

28 If I find that the conveyances were made with intent to defeat, hinder, delay or defraud creditors it would still not be void if the defendants could establish that the transactions were made for good consideration, were *bona fide* and the transferee or mortgagee was a person not having, at the time of the transaction, notice or knowledge of the intent to defraud. The onus to show this, however, is on the defendants. (*Bank of Montreal v. Jory*, [1981] B.C.J. No. 1014 (B.C. S.C.)).

C) Taking Title "To Uses"

29 The taking of title "to uses" was the subject of much argument. The defendants maintain this has the same effect as taking title "in trust." The plaintiffs maintain that it is simply a form of title that was used at that time to avoid the obligations flowing from dower. While both positions may be sustainable, the real determinant is the intention of the parties. Therefore, I see no need to deal with the *Statute of Uses* R.S.O. 1897, c.331 and its application to the present case.

D) The Defendant's Case

30 The defendants admit that the transfer from Joe to Gregorina was not made for consideration. They take the position that the transfer was simply putting the property into Gregorina's name on the basis that, since the mid-70s, it had been held by Joe on behalf of Gregorina. They point to the fact that title had been taken by Joe "to uses" as evidence of this. If accepted, this is a complete answer to the plaintiffs' claim.

31 If the court sets aside the transfer to Gregorina as a fraudulent conveyance, the defendants take the position that the mortgage on the property is valid and enforceable. It would remain as a charge on the property and take priority over the plaintiffs' claims.

32 Finally, the defendants take the position that the action has been settled and that, as a result, the claim should be dismissed.

E) The Evidence

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

33 The events surrounding this action date back, in some cases thirty years. As a result, some allowance must be made for faulty memories and for the difficulty in proving certain facts. Similarly, the real estate transactions carried out in the 1970s, including the acquisition of the property by Joe "to uses," involved many different lots contributing to confusion in the testimony and recollection of the parties.

34 Even accounting for this, the evidence put forward by the defendants is far from satisfactory. I noted a number of significant inconsistencies. Some of the more significant inconsistencies surrounding key events were as follows:

1. Gregorina testified that the property had always been in her name. However, there was also evidence that:

    • according to land registry records the property was put into the name of Joe "to uses" in 1972 and not transferred to Gregorina till August 1994

    • Joe's discovery evidence was that the 1994 transfer of the property was made at Gregorina's request

    • Gregorina's discovery evidence was that the property was transferred to her because Joe had problems at the bank and did not want to lose the cottage.

2. Alba testified that she gave her mother a mortgage because her mother needed the money. However, there was also evidence to the effect that:

    • the mortgage was placed on the property after all of the funds said to support the mortgage were advanced;

    • the advances purportedly supporting the mortgage were not made to Gregorina, they were made principally to Alessandro Holdings Ltd., a company apparently controlled by Joe, and to a lesser degree to Joe and Gregorina jointly.

    • Joe's discovery evidence was that some of the money was to pay his debts at the Royal Bank for which Gregorina was co-signer.

    • all but one of the cheques drawn on Alba's account were signed and likely initiated by Joe.

    • although Alba's testimony on this point is somewhat evasive, it is likely that Gregorina was giving Alba significant gifts, including cash gifts, in the same period that the alleged advances were made and remained outstanding;

    • Alba testified that it was her mother that gave the necessary instructions to the lawyer regarding the mortgage, but Gregorina's discovery evidence was that all of the paper work regarding the property was prepared or arranged by Alba;

3. Joe testified that he was never a partner in the venture that acquired the property and the Block D properties. He also testified that there were four partners: Gregorina, Giuseppe Marchese, Domenic Sgro and Raffaele Morano. Other evidence on the point, however, was as follows:

    • evidence of Gregorina that there were three partners: her, Morano and Marchese.

    • the evidence of Giuseppe Marchese was that there were four partners and that one of those four was Joe and not Gregorina;

    • Joe gave previous evidence that there were five partners and that he had never held any property in trust. At trial he changed his testimony and said that these prior sworn statements were made in error.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

35 When I review the whole of the evidence and consider the reliability of the various witnesses I find Joe's testimony that he took the property in trust for four partners, including his wife, and that it was Gregorina who, as one of the four beneficiaries, paid out the other three partners thereby becoming the sole beneficial owner of the property to be self-serving and improbable. The evidence is more consistent with Joe being the partner who acquired the complete interest in the property sometime in the mid 70s, and I so find.

36 The 1994 transfer to Gregorina was a non arm's length transaction for no consideration at a time when Joe was insolvent. It was an attempt to put the property out of the reach of his creditors.

37 Support for this conclusion includes the following:

1. The clear and cogent evidence of Giuseppe Marchese. He testified that there were four partners, one of whom was Joe, and that after the Block D properties were sold, Joe bought out his partners by paying each of them $3,000. As a result, Joe became the sole owner of the property.

2. When one reviews all of the transactions shown in the various property registers for the area, it is clear that Joe and his partners bought and sold many properties. It does not seem reasonable that Joe would put this particular property into his name when he had no interest in it. Some properties were put in his name, in Gregorina's name and in their joint names and there seems little logic in his name appearing on title of this particular property if he had no interest in it.

3. The way Joe acted and parts of his testimony suggest that he was directly and intimately involved in these transactions and are more consistent with Joe being a partner than not.

4. Gregorina's discovery evidence read in at trial was that Joe transferred the property into her name because he had problems with the bank and did not want to lose the cottage.

5. The evidence of Cesidio and Sylvio Conte, Cesidio's son, was that Joe had advised them both that the property was "his cottage," that is, Joe's cottage.

38 I turn now to Gregorina's evidence on the question of ownership. As set out previously, her testimony at trial was that the property had always been hers and in her name. She was visibly emotional about it, and it may well be that at the time of trial this was her honest belief. This belief, even if sincere, does not make it so. There were many transactions and payments made in the early 70s. From her testimony, it was clear that Gregorina did not know which specific property would have been put into her name nor which property was put into the name of her husband.

39 She testified repeatedly that the cottage lot she bought was on Ronald Avenue and, after being told that the property was located on James Street, said she must have forgotten that the lots she purchased were scattered on different streets. In fact she and Joe did buy a lot on Ronald Avenue as part of the many transactions in the area, and it is on this lot that they built their first cottage. The Ronald Avenue lot is not, however, the lot that is the subject of the present litigation. The Ronald Avenue cottage was later sold and a second cottage was built on the property located on James Street which, as stated earlier, was also acquired as part of these transactions but is in the name of Joe "to uses".

40 In my view, the property on which the current cottage is situated, the property that is the subject of this litigation, was

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

not a property that Gregorina bought in the 1970s. Her testimony concerning her alleged purchase of the property is confused, inconsistent and changing. The evidence is more consistent with Joe having acquired that property.

41 I now turn to the transactions themselves — the transfer and subsequent mortgaging of the property.

F) Badges of Fraud

42 From the chronology and facts we can identify a series of "badges of fraud" for both the transfer and mortgaging of the property.

1. Transfer from Joe to Gregorina

43 Based on my earlier finding that Joe did not hold the property in trust and had in fact become the owner of the property in the 70s, the 1994 transaction should be viewed as a simple transfer rather than a transfer to the beneficiary under a trust arrangement. I will therefore turn to a review of some of the badges of fraud and how they relate to the transfer to Gregorina. They are as follows:

a) The transferor has few remaining assets after the transfer:

- the property transferred was the only asset owned by Joe and was done at a time when Joe was insolvent.

b) Transfer to a non arm's length person:

- the transfer was non arm's length from Joe to his wife.

c) There are actual or potential liabilities facing the transferor or he is about to enter upon a risky undertaking:

- the transfer was made very shortly after the plaintiffs issued the statement of claim to recover the $350,000 debt owed by Joe.

d) Grossly inadequate consideration:

- the consideration for the transfer from Joe to Gregorina was nominal.

e) The transferor remains in possession or occupation of the property for his own use after the transfer:

- Joe continued to use and benefit from the property after the transfer to Gregorina.

f) The deed contains a self-serving and unusual provision:

- the land transfer tax affidavit contained a self-serving statement being that the transferee had been the sole beneficial owner during the entire period the lands were registered in the name of Joe.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

g) The transfer was effected with unusual haste:

• after holding for over 20 years the transfer is effected shortly after the plaintiffs issued the statement of claim.

44 The presence of one or more of these badges of fraud raises a presumption of fraud. As set out earlier, while the persuasive burden of proof remains with the plaintiffs, the burden of explaining the circumstantial evidence of fraudulent intent now shifts to the defendants.

45 In addition to these badges of fraud there is the evidence of Gregorina which was read in from the discovery transcript. Her evidence was that the transfer was done to take the property out of reach of the bank, one of Joe's creditors. Considering this evidence, not only was there little or no evidence to explain the circumstantial evidence of fraudulent intent and rebut the presumption of fraud, there was direct evidence supporting the fraudulent intent.

2. Mortgage Between Gregorina and Alba

46 When we look for badges of fraud in a mortgage transaction that is alleged to be the second part of a two part scheme to defeat or delay creditors we need to adapt the principles somewhat to take into account the unique circumstances. Some of the badges of fraud and how they relate to the mortgage of the property are as follows:

a) Transfer to a non arm's length person:

• the transaction was non-arm's length, being between Gregorina and her daughter Alba.

b) The effect of the transaction is to delay and defeat creditors:

• there was a risk that the transfer would be set aside and the property seized by creditors, therefore, the mortgage served to protect against that.

c) Payment to a person not a party to the disposition:

• the consideration for the mortgage and the making of the mortgage were not contemporary. The consideration did not go to Gregorina but rather went principally to a company apparently controlled by Joe, and to Joe and Gregorina jointly.

d) The transfer was effected with unusual haste:

• the timing of the loan agreement which underlies the mortgage was shortly after the plaintiffs demanded payment from Joe; and:

• Gregorina and/or Alba registered the mortgage on the property shortly after the date of the judgment debtor examination of Joe.

e) The absence of a sound business or tax reason for the transaction:

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

- Alba and Gregorina were mother and daughter. Alba had received numerous gifts of money and goods from her mother. There was no business or tax reason for the mortgage and no reason why the mortgage should be placed on the cottage lot rather than Gregorina's home in Toronto.

f) The deed contains a self-serving and unusual provision:

- The loan agreement which deals with the purported loan from Alba to Gregorina and Joe contains a recital describing Joe as the holder in trust of the property, and Gregorina is the beneficial owner.

47 The existence of one or more of these various badges of fraud serves to shift the burden of explaining the circumstantial evidence of fraudulent intent to the defendants.

48 The defendants allege that the mortgage flowed from the loan agreement and that the mortgage was placed on the property as consideration for the advances made pursuant to the loan agreement.

49 When one reviews the mortgage transaction in the context of all of the other facts and events surrounding the property it is, in my view, improbable that the mortgage was a regular financial arrangement between Alba and Gregorina. The mortgage and the loan agreement were part of the scheme to keep the property out of the reach of Joe's creditors.

50 The advances under the loan agreement were to or for the benefit of Joe, and Gregorina did not have much involvement in it. The loan agreement was likely triggered by the plaintiffs' demand for payment from Joe or other creditors' demands. The mortgage was intended to protect the cottage from being seized by creditors and sold to provide money to repay Joe's debts.

51 While Joe, Gregorina and Alba each tried to characterize these transactions as regular and proper, I found the evidence of each of them to be self-serving and unreliable. On the balance of probabilities, I am satisfied that the dominant purpose of both of the transactions was to prevent creditors from having access to the property for payment of Joe's debts. Gregorina and Alba were both well aware of Joe's financial situation. While Gregorina did not appear to me to be sophisticated enough to structure the various transactions, I find that she willingly cooperated with Alba and Joe who undertook to put the property out of the reach of Joe's creditors.

G) Was There Consideration for the Mortgage?

52 If the defendants can establish that either of the transactions was made for good consideration and was a *bona fide* transaction to a person not having notice or knowledge of the intent to defraud, then the grantee may keep the property free of the taint of fraud.

53 With respect to the transfer of the property from Joe to Gregorina, there was no valuable consideration, and I need go no further.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

54 With respect to the mortgage, the defendants tried to show that the mortgage was given for good and valuable consideration. The burden was on the defendants to establish consideration. The evidence presented by the defendants is not sufficient to discharge the burden of proof in this case. The production of various cheques, most of which were payable to one of the companies controlled by Joe was unconvincing as it was clear on the whole of the evidence that Joe was controlling the flow of funds. In the absence of the various bank accounts showing the source of the monies and the ultimate disposition of the funds, I am not satisfied that the advances were *bona fide* payments made by Alba to Gregorina in support of the mortgage. In addition, as stated earlier, I find that Alba was well aware of the reason for these various transactions, and it was no coincidence that she sought to place a mortgage on the property rather than on other assets in the name of Gregorina.

55 I find, on a balance of probabilities, that the transfer to Gregorina and the mortgage were done with an intent to defeat, hinder, delay or defraud the creditors. The transfer and the mortgage were not made for consideration nor was the mortgage made in good faith to a person who, at the time of the placing of the mortgage, had no notice or knowledge of the intent to defeat, hinder, delay or defraud the creditor.

H) Alleged Settlement

56 A full and final release, a consent and an agreement to settle the claim, all executed October 7, 1999, were entered into evidence.

57 The defendants allege that the action was settled and that, as a result, the claim ought to be dismissed.

58 In his videotaped evidence, Cesidio confirmed that he did in fact execute the documents but that this had been done on the understanding that the executed documents would be exchanged through intermediaries against payment in full of the debt. He testified that no payment was ever made. As a result, he never authorised the release of the settlement documents, and no settlement was effected.

59 Joe testified that the settlement negotiations were conducted through an intermediary and that he had paid the settlement funds.

60 It is not clear from Joe's evidence what amount was to be paid in settlement of the claim. Other than Joe's testimony, the only evidence of payment of any settlement funds was a certified cheque for $72,000 dated July 13, 1999, payable to J. Sansone, a friend of the families. There was no evidence provided regarding who cashed the cheque in October 1999 nor how the funds were used.

61 The burden is on the defendants to establish that a settlement has been concluded. Given the evidence of Cesidio denying any payment, the proof that the settlement funds were actually paid is essential. Mr. Sansone was never called to testify concerning what the $72,000 payment to him was for nor has any other document been tendered showing that this, or any other sum, was ever paid to the plaintiffs.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

62 The defendants have not satisfied me on a balance of probabilities that a settlement was entered into which resolved all of the issues in this action. They offered no satisfactory explanation for the failure to call the payee of the cheque, J. Sansone. By reason of that failure I draw an inference adverse to the defendants that the testimony of that witness would not have assisted the defendants' case.

63 In any event, the amount paid to Mr. Sansone was less than the amount allegedly agreed upon, and other than Joe's testimony, there is no evidence that these sums were paid. The defendants have not satisfied me that any consideration was paid for the alleged settlement. I therefore conclude that this defence must fail.

VI. Conclusion

64 In the result, I grant judgment setting aside the transfer of the property described municipally as 1629 James Street, Tiny, Ontario, from Giuseppe Alessandro to Gregorina Alessandro, Instrument 01263935 dated August 31, 1994. I also grant judgment setting aside the charge granted on that same property by Gregorina Alessandro to Alba Alessandro, instrument 01325897 dated October 11, 1996.

65 In view of my conclusions in respect of the plaintiffs' claims, I dismiss the defendants' counterclaim.

66 If the parties are unable to agree on the issue of costs, the plaintiffs are to provide me with written submissions within 15 days of the release of these reasons, and the defendants are to respond in writing to these within 10 days thereafter.

Action allowed; counterclaim dismissed.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 19

1984 CarswellOnt 137
Ontario Supreme Court, In Bankruptcy

Fancy, Re

1984 CarswellOnt 137, 46 O.R. (2d) 153, 51 C.B.R. (N.S.) 29, 8 D.L.R. (4th) 418

Re FANCY

Anderson J.

Heard: February 20, 1984
Judgment: May 14, 1984
Docket: Toronto No. 32433

Counsel: *G. Morawetz* , for plaintiff trustee.
R. Dexter , for defendants.

Subject: Corporate and Commercial; Insolvency; Contracts; Torts

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy --- Avoidance of transactions prior to bankruptcy — Settlements of property — Transfer of matrimonial home

Fraud and Misrepresentation --- Fraudulent conveyances — Practice and procedure — Burden of proof — Transactions between near relatives — Corroboration

Conveyance set aside.

Conveyance set aside.

Affidavits without pleadings not satisfactory.

The bankrupt conveyed his interest in the matrimonial home to his wife within one year before his bankruptcy and continued to live there. His explanation was that when the property was acquired it was intended that it belong to his wife for her purposes and those of the children, but that it was initially registered in their joint names on advice that that was the practice in Canada and that to do so would enhance his credit position. The trustee applied to have the conveyance set aside either as a settlement under s. 69(1) of the Bankruptcy Act or as a fraudulent conveyance under s. 2 of the Fraudulent Conveyances Act. An order was made directing trial of the issue with the affidavits of the parties to

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

constitute the pleadings.

Held:

Application granted.

The word "settlement" in s. 69 should not be given a restricted meaning. A settlement will be created if a man transfers the family residence to his wife, their intention being that he will maintain it as the family home and continue to reside therein. The saving provision of s. 69(3) did not apply because the payment of nominal consideration by the wife did not make her "a purchaser ... for valuable consideration". The conveyance was a disposition of property to be held for the enjoyment of some other person and was in such a form that it could be traced.

On an application pursuant to s. 2 of the Fraudulent Conveyances Act the plaintiff must prove that the conveyance was made with the intent defined in that section. Whether the intent exists is a question of fact to be determined from all of the circumstances as they existed at the time of the conveyance. Although the primary burden of proving his case on a reasonable balance of probabilities remains with the plaintiff, the existence of one or more of the traditional "badges of fraud" may give rise to an inference of intent to defraud in the absence of an explanation from the defendant. In such circumstances, there is an onus on the defendant to adduce evidence showing an absence of fraudulent intent. Where the impugned transaction was between close relatives under suspicious circumstances, it is prudent for the court to require that the debtor's evidence on bona fides be corroborated by reliable independent evidence. The explanation offered by the husband was not sufficient explanation and did not constitute corroboration.

It is often unsatisfactory to try an issue without the benefit of pleadings. It would be better practice if all orders for the trial of an issue called for pleadings; even pleadings may fail to define the issue with great precision. Affidavits alone fail to define the issues at all and a trial of an issue based on affidavits alone is not satisfactory.

Table of Authorities

Cases considered:

Bozanich, Re; A.H. Boulton Co. Ltd. v. Trusts & Guar. Co. Ltd., [1942] S.C.R. 130, 23 C.B.R. 234, [1942] 2 D.L.R. 145 — *applied*
Coopers & Lybrand Ltd. v. Murphy (1978), 27 C.B.R. (N.S.) 54, (sub nom. *Murphy v. Murphy)* 27 N.S.R. (2d) 391, 41 A.P.R. 391 (C.A.) — *referred to*
Geraci, Re, [1970] 3 O.R. 49, 14 C.B.R. (N.S.) 253 , I.L.R. 1-343, 12 D.L.R. (3d) 314 (C.A.) — *applied*
Grant, Re, 7 C.B.R. 254, [1926] 1 D.L.R. 681 (N.S.T.D.) — *referred to*
Holdenreid v. Holdenreid (1978), 29 C.B.R. (N.S.) 138 (Ont. H.C.) — *applied*
Vasey v. Kreutzweiser (1965), 8 C.B.R. (N.S.) 225 (Ont. H.C.) — *applied*

Statutes considered:

Bankruptcy Act, R.S.C. 1927, c. 11, s. 62(3).

Bankruptcy Act, R.S.C. 1952, c. 14, s. 60(1).

Bankruptcy Act, R.S.C. 1970, c. B-3, s. 69(1), (3).

Fraudulent Conveyances Act, R.S.O. 1980, c. 176, ss. 2-4.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Land Titles Act, R.S.O. 1980, c. 230.

Authorities considered:

Waters, Law of Trusts in Canada, (1974), pp. 255-56.

Application to have conveyance from bankrupt to wife set aside.

Anderson J. :

1 This is the trial of an issue arising out of a motion made by the trustee for an order setting aside a conveyance from the bankrupt to his wife.

2 The issue, as argued before me, ultimately proved to consist of two separate questions raised in the notice of motion as follows:

3 (1) Was the transaction in dispute void as being a "settlement" within the meaning of s. 69(1) of the Bankruptcy Act, R.S.C. 1970, c. B-3 ("the Act")?

4 (2) Alternatively, was the transaction a fraudulent and void conveyance within the terms of s. 2 of the Fraudulent Conveyances Act, R.S.O. 1980, c. 176.

5 Before turning to the disposition of these questions, I wish to say a word about the form of the proceedings. The order directing the trial of the issue was made at a time when no material had been filed on behalf of either of the defendants. The order dispensed with the usual requirements for pleadings and instead provided that the affidavits of the parties should constitute pleadings. Due to a combination of circumstances which need not be reviewed, when the matter came before me there was still no material filed on behalf of the defendants. In other words, I was faced with the trial of an issue which had not been defined and, indeed, could scarcely be said to exist. I allowed a short adjournment for the purpose of permitting the defendants to prepare and file a statement of defence. Having regard to the manner in which the trial eventually proceeded, however, I have great difficulty understanding why it was necessary. In my view, the course of these proceedings shows how unsatisfactory it is when parties apply for the trial of an issue before material is filed by both the parties establishing that there is an issue to be tried. Secondly, I am left convinced that it is unsatisfactory to try an issue without the benefit of pleadings. It would be much better if all orders for the trial of an issue called for pleadings. Even pleadings may fail to define the issue with great precision. Affidavits alone, however, simply fail to define the issues at all.

6 A short review of the facts is appropriate. They are not complicated and are not greatly in dispute.

7 The impugned conveyance was a transfer made pursuant to the usual practice under the Land Titles Act, R.S.O. 1980, c.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

230, without limiting condition insofar as the transferee was concerned. Consideration was nominal. The property was the matrimonial residence of the parties. The defendant husband continues to live there. His evidence was to the effect that the conveyance was intended to assure that the property would be available as a home for his wife and children. The transfer was dated 6th March 1980 and was registered on 14th March 1980. The defendants are immigrants from Bangladesh, that part of the Indian subcontinent formerly known as Pakistan, where the bankrupt was apparently a businessman of some consequence. His business interests and life generally were disrupted by political and economic changes that resulted in his decision to leave the land of his birth, first for England and subsequently for Canada. Here he acquired business interests, including a company known as Textile Industries Limited. At about the time of the conveyance in question the defendant was contemplating embarking upon a further business venture involving the manufacture of shoes. The business of Textile Industries declined and in consequence the financial fortunes of the bankrupt declined with it.

8 On 19th July 1977 a writ of summons was issued against a numbered company and the bankrupt, claiming recovery of the sum of $105,592 and interest. This action took a more leisurely course than usual and was ripe for trial in the spring of 1980. The plaintiffs in that action were the petitioning creditors, Severino J. Peloso and Nelson H. Pickard.

9 On 11th September 1980 a writ of summons was issued by the Canadian Commercial and Industrial Bank against the bankrupt. The claim was on a guarantee by the bankrupt of the indebtedness of Textile Industries Limited. The claim was for $400,000 and interest.

10 On 2nd May 1980 judgment was given in the action brought by the petitioning creditors for the aggregate sum of $144,972.62 together with interest.

11 On 13th June 1980 a writ was issued by the petitioning creditors against the bankrupt and his wife to set aside the impugned coveyance as being fraudulent and void as against the plaintiffs. This action was never pursued to a conclusion. On 8th September 1981 the receiving order was made.

12 The first question to be decided is whether the impugned conveyance is a "settlement" within the meaning of s. 69(1) of the Act. That subsection reads as follows:

> 69.(1) Any settlement of property, if the settlor becomes bankrupt within one year after the date of the settlement, is void against the trustee.

The Act in its present form contains no definition of "settlement". However, the Canadian courts have often been called upon to decide the meaning of that term so that its meaning in the context of s. 69(1) is now relatively clear.

13 *Re Bozanich; A.H. Boulton Co. Ltd. v. Trusts & Guar. Co. Ltd.*, [1942] S.C.R. 130, 23 C.B.R. 234, [1942] 2 D.L.R. 145 , was a decision of the Supreme Court of Canada handed down at a time when the Bankruptcy Act, R.S.C. 1927, c. 11, did contain a provision "defining" the term "settlement". That provision, which appeared as s. 62(3) in the 1927 consolidation of the statute, was in the following terms:

> 3. For the purpose of this section and sections sixty and sixty-one "settlement" shall include any conveyance or transfer of property.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

The question to be decided in *Re Bozanich* was whether a certain chattel mortgage was valid and effectual as against the trustee or whether it constituted a settlement. In determining that the transaction in question was not in fact a "settlement", despite the broad language of s. 62(3), the court discussed the meaning of that term at some length. The primary majority judgment was written by Duff C.J.C. At p. 237 the learned Chief Justice, after noting that the relevant sections of the Canadian Bankruptcy Act were in substance re-enactments of the provisions of the English statute, had this to say:

> Broadly speaking, the settled principle in England is that this clause [s. 62(3)] has not the effect of bringing within the scope of the term "settlement", as used in the sections corresponding to secs. 60, 61 and 62 of our Act, transactions which have none of the essential elements of a "settlement", as that term is commonly understood.
>
> In the treatise on Bankruptcy and Insolvency in the 2nd ed. of Halsbury by Lord Justice Luxmoore it is stated (para. 487) that *the term "settlement" "implies an intention that the property shall be retained or preserved for the benefit of the donee in such a form that it can be traced"* . This construction was well settled in the year 1919 when the relative (sic) provisions of the English statute were enacted as part of the bankruptcy law of this country. It is proper to assume that it was the statute as it had been construed by the English Courts and applied in the administration of bankruptcy law in England that Parliament intended to adopt. (The italics are mine.)

14 A recent decision of the Ontario Court of Appeal confirms that the interpretation of "settlement" accepted by Duff C.J.C. in *Re Bozanich* remains applicable under the present Act. In *Re Geraci*, [1970] 3 O.R. 49, 14 C.B.R. (N.S.) 253 , I.L.R. 1-343, 12 D.L.R. (3d) 314 (C.A.) , the court was required to determine whether a bankrupt's designation of his wife as beneficiary of a certain life insurance policy owned by the bankrupt was void against the trustee. The provision of the Bankruptcy Act invoked by the trustee was identical in its terms to s. 69(1) of the present Act. In ruling that the transaction was indeed void, as being a "settlement" within the meaning of the Bankruptcy Act, R.S.C. 1952, c. 14, Jessup J.A., writing for the court, stated as follows (at pp. 255-56):

> The learned trial Judge held that the designation of the bankrupt's wife as the beneficiary of his policy of life insurance was a "settlement of property" within the meaning of s. 60(1) of the Bankruptcy Act, and I agree with him. *I think there emerges from the authorities a definition of the ordinary meaning of "settlement" that it is a disposition of property to be held, either in original form or in such form that it can be traced, for the enjoyment of some other person;* and that the designation of a beneficiary of an insurance policy is such a disposition: *Re Player; Ex parte Harvey* (1885), 15 Q.B.D. 682 ; *Re Bozanich; A.H. Boulton Co. v. Trusts & Guar. Co.* , [supra]; *Gunner v. Gunner & Stirling*, [1949] P. 77, [1948] 2 All E.R. 771 ; *Lort-Williams v. Lort-Williams* , [1951] P.395, [1951] 2 All E.R. 241 ; *Re Roddick* (1896), 27 O.R. 537 ; *Re Benjamin* (1926), 59 O.L.R. 392 . (The italics are mine.)

In *Re Geraci* it was argued on behalf of the bankrupt that the bankrupt's designation of his wife as beneficiary could not constitute a "settlement" because the designation was not irrevocable. In rejecting this argument and affirming that the granting to the wife of even a contingent interest under the policy was a disposition of property and, in the circumstances, a settlement, Jessup J.A. referred to "the wide ranging affairs" to which the Bankruptcy Act applies, and concluded (at p. 256) that the word "settlement" as used therein should not be given a restricted meaning.

15 *Vasey v. Kreutzweiser* (1965), 8 C.B.R. (N.S.) 225 (Ont. H.C.) , is a case whose facts were somewhat similar to those of the instant case. In that case the defendant bankrupt had transferred his house to his wife a little more than one year before he went into bankruptcy. The consideration given by the wife amounted to one dollar and "natural love and affection" (p. 231). Bennett J., sitting as local master, agreed with the trustee that the transfer was a void settlement within the meaning of s. 60 of the 1952 Bankruptcy Act. In *Vasey* , it appeared that the donee, the bankrupt's wife, intended to sell the house in question and to retain the proceeds for herself or for herself and her husband. Nevertheless, the court had no difficulty concluding that in the circumstances the property could be traced and that the transfer was a "settlement".

WestlawNext® CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

16 In my view, the result is no less straightforward where, as in the instant case, the evidence is that the parties' intention at the time of the transfer was to continue to reside in the house as a family home. In Waters, Law of Trusts in Canada (1974), pp. 255-56, the learned author says:

> ... a settlement would be created if a man transfers the family residence to his wife, the joint intention being that she will maintain it as the family home.

Authority for this proposition is *Re Grant*, 7 C.B.R. 254, [1926] 1 D.L.R. 681 (N.S.T.D.) , where it would appear that such a conveyance would have been set aside as a settlement but for the fact that the transferee gave good consideration by way of a bar of dower.

17 It is apparent that the impugned conveyance in the instant case was, to use the language of Jessup J.A. in *Re Geraci* , supra, "a disposition of property to be held ... for the enjoyment of some other person", and that the husband's conveyance to his wife was made in such a form that it can be traced. I am satisfied that the conveyance was a "settlement" within the meaning of that term in s. 69(1) of the Act. The saving provisions of s. 69(3) of the Act do not apply. In particular I find that the payment of nominal consideration by the bankrupt's wife in the circumstances does not make her "a purchaser ... for valuable consideration": see *Vasey v. Kreutzweiser* , supra, p. 231; *Re Grant* , supra, p. 257; and *Coopers & Lybrand Ltd. v. Murphy* (1978), 27 C.B.R. (N.S.) 54, (sub nom. *Murphy v. Murphy)* 27 N.S.R. (2d) 391, 41 A.P.R. 391 (C.A.) . The transaction occurred within one year of the date of the settlor's bankruptcy and is therefore void against the trustee.

18 Lest it be held elsewhere that I am in error in that regard, I should consider the alternative question of whether the impugned transaction should be set aside as a fraudulent conveyance.

19 The relevant provisions of the Fraudulent Conveyances Act are ss. 2, 3 and 4, which read as follows:

> 2. Every conveyance of real property or personal property and every bond, suit, judgment and execution heretofore or hereafter made with intent to defeat, hinder, delay or defraud creditors or others of their just and lawful actions, suits, debts, accounts, damages, penalties or forfeitures are void as against such persons and their assigns.
>
> 3. Section 2 does not apply to an estate or interest in real property or personal property conveyed upon good consideration and *bona fide* to a person not having at the time of the conveyance to him notice or knowledge of the intent set forth in that section.
>
> 4. Section 2 applies to every conveyance executed with the intent set forth in that section notwithstanding that it was executed upon a valuable consideration and with the intention, as between the parties to it, of actually transferring to and for the benefit of the transferee the interest expressed to be thereby transferred, unless it is protected under section 3 by reason of *bona fides* and want of notice or knowledge on the part of the purchaser.

In the instant case, the provisions of ss. 3 and 4 have no application. The plaintiff plainly is a creditor within the meaning of s. 2. The plaintiff must prove that the conveyance was made with the intent defined in that section. Whether the intent exists is a question of fact to be determined from all of the circumstances as they existed at the time of the conveyance. Although the primary burden of proving his case on a reasonable balance of probabilities remains with the plaintiff, the existence of one or more of the traditional "badges of fraud" may give rise to an inference of intent to defraud in the absence of an explanation from the defendant. In such circumstances there is an onus on the defendant to adduce evidence showing an absence of fraudulent intent. Where the impugned transaction was, as here, between close relatives under suspicious circumstances, it is prudent for the court to require that the debtor's evidence on bona fides be corroborated by reliable independent evidence.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

20 The explanation offered by the defendants for the making of the conveyance was that when the property was acquired it was intended that it should belong to the wife for her purposes and those of the children. The explanation further went that the property was initially taken in their names jointly on advice that that was the practice in Canada and that it would enhance the position of the defendant husband in respect of credit. I do not think this can be taken as a sufficient explanation and there is clearly no corroboration. The circumstances under which the conveyance was made are such as to arouse suspicion.

21 In *Holdenreid v. Holdenreid* (1978), 29 C.B.R. (N.S.) 138 at 144 (Ont. H.C.) , the question of onus was put by Osborne J. in the following terms:

> While the primary burden of proving her case in the reasonable balance of probabilities remains upon the plaintiff, I find under the circumstances that the combination of somewhat suspicious circumstances surrounding the transfers and the relationship between the defendants gives rise to an inference of fraud in the absence of an explanation from or on behalf of the defendants.

In my view, no sufficient explanation has been offered by these defendants.

22 In the result, an order will go setting aside the conveyance.

Application granted.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 20

2004 CarswellOnt 1502
Ontario Court of Appeal

Boudreau v. Marler

2004 CarswellOnt 1502, [2004] O.J. No. 1543, 185 O.A.C. 261, 18 R.P.R. (4th) 165, 48 C.B.R. (4th) 188

ANDRE BOUDREAU (Plaintiff / Respondent) and JONATHAN H. MARLER, MURRAYFIELD CORP. and JOHN WIEBE (Defendants / Appellants)

Abella, Cronk JJ.A., Juriansz J. (ad hoc)

Heard: January 21, 2004
Judgment: April 19, 2004
Docket: CA C38201

Proceedings: affirming *Boudreau v. Marler* (2002), 2002 CarswellOnt 5844 (Ont. S.C.J.)

Counsel: Eric R. Murray, Chris Morrison for Appellant
Guy A. Wainwright for Respondent

Subject: Contracts; Corporate and Commercial; Torts; Civil Practice and Procedure; Property; Insolvency

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Fraud and misrepresentation — Fraudulent conveyances — Fraudulent intent — Presumption of fraudulent intent — General

Defendant corporation advanced funds to individual, P, secured by means of mortgage on P's residence — After P commenced proceedings against corporation in relation to mortgage, corporation retained defendant lawyer — Lawyer accepted cash retainer as well as assignment of mortgage on P's residence as collateral security for future legal services — Few years prior to assignment, plaintiff, business associate of P, had successfully obtained judgment against corporation in relation to debt owed to plaintiff by P that was guaranteed by corporation — One day before sheriff attempted to seize corporation's interest in mortgaged property, assignment of mortgage from corporation to lawyer was registered — Plaintiff successfully brought action against lawyer and corporation and obtained declaration that assignment of mortgage was void as fraudulent conveyance — Lawyer and corporation appealed — Appeal dismissed — Trial judge was entitled to conclude that lack of meaningful consideration for assignment, corporation's insolvency at time of assignment, lawyer's secrecy, and outstanding judgment in plaintiff's favour created rebuttable presumption that lawyer had requisite intent to defeat plaintiff — Most significantly, lawyer failed to register assignment for one and a half years, an act of secrecy that supported trial judge's inference of fraud — Trial judge's credibility findings along with his findings that lawyer knew that corporation was insolvent at time of assignment supported his conclusion that presumption of fraud had not been rebutted.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Barristers and solicitors --- Relationship with client — Conflict of interest — Duty to former client — General

Plaintiff brought action against lawyer, corporate client of lawyer, and directing mind of corporate client seeking to establish that particular transaction between lawyer and corporation constituted fraudulent conveyance — Lawyer's firm had been solicitors of record throughout proceedings for all of defendants, including lawyer himself — One week prior to trial, lawyer wrote to plaintiff's counsel indicating that lawyer intended to be represented separately by counsel, KP, or, in alternative, he proposed to act for himself — When trial started, plaintiff objected to KP acting as lawyer's solicitor because KP was junior associate at law firm plaintiff had retained to defend himself in earlier litigation involving corporation — KP acknowledged that she had met with plaintiff many times in preparing defence pleadings in earlier litigation — Trial judge held that KP could not act for lawyer and denied lawyer's motion for self-representation — Lawyer appealed — Appeal dismissed — Trial judge did not err in his exercise of discretion by not permitting KP to represent lawyer — Evidence of KP's former relationship with plaintiff created reasonable likelihood of possible conflict — Fact that KP's law firm drafted mortgage that formed subject matter of transaction at issue in trial and that lawyer only notified opposing counsel of his intention to retain KP one week before start of trial suggested that trial judge's discretion ought not to be interfered with — No interference was warranted with respect to trial judge's decision to refuse to allow lawyer to represent himself while lawyer's firm represented other defendants.

Table of Authorities

Cases considered by *Abella J.A.*:

Chapters Inc. v. Davies, Ward & Beck LLP (2001), 2001 CarswellOnt 178, 10 B.L.R. (3d) 104, 52 O.R. (3d) 566, 141 O.A.C. 380 (Ont. C.A.) — followed

Everingham v. Ontario (1992), 88 D.L.R. (4th) 755, 8 O.R. (3d) 121, 5 C.P.C. (3d) 118, 54 O.A.C. 224, 1992 CarswellOnt 421 (Ont. Div. Ct.) — considered

Heck v. Royal Bank (1993), (sub nom. *Essa (Township) v. Guergis)* 15 O.R. (3d) 573, (sub nom. *Essa (Township) v. Guergis)* 52 C.P.R. (3d) 372, (sub nom. *Membery v. Hill)* 22 C.P.C. (3d) 63, 1993 CarswellOnt 473 (Ont. Div. Ct.) — referred to

MacDonald Estate v. Martin (1990), [1991] 1 W.W.R. 705, 77 D.L.R. (4th) 249, 121 N.R. 1, (sub nom. *Martin v. Gray)* [1990] 3 S.C.R. 1235, 48 C.P.C. (2d) 113, 70 Man. R. (2d) 241, 1990 CarswellMan 384, 1990 CarswellMan 233 (S.C.C.) — followed

Platt, Re (2004), 2004 CarswellOnt 1500 (Ont. C.A.) — referred to

Statutes considered:

Assignments and Preferences Act, R.S.O. 1990, c. A.33
Generally — referred to

s. 4(1) — referred to

Fraudulent Conveyances Act, R.S.O. 1990, c. F.29
Generally — referred to

Rules considered:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Rules of Civil Procedure, R.R.O. 1990, Reg. 194
Generally — referred to

APPEAL by defendants from judgment reported at *Boudreau v. Marler* (2002), 2002 CarswellOnt 5844, 18 R.P.R. (4th) 182, 48 C.B.R. (4th) 178 (Ont. S.C.J.), concerning fraudulent conveyance.

Abella J.A.:

1 This is an appeal from a finding that a residential mortgage assigned by a corporate client to its lawyer was a fraudulent conveyance and an unlawful preference. The appeal also involves the trial judge's decision to disqualify a proposed lawyer from acting.

2 This appeal was heard together with the appeal in *Platt, Re* [2004 CarswellOnt 1500 (Ont. C.A.)] Both decisions are being released concurrently.

BACKGROUND

3 The background to this appeal is complex, marked by years of litigation between the parties and associated persons. Accordingly, it is useful to set out the background facts in some detail.

The China Wars Litigation

4 In the late 1980s, Mr. Platt owned mining claims for kaolin, an industrial mineral (the Kaolin Claims). He and Jacobus Hanemaayer were partners in a controlling interest in Great Lakes Nickel Ltd., a public company incorporated to own and develop the Kaolin Claims.

5 Mr. Hanemaayer and his lawyer, Eric Kraushaar, incorporated 798839 Ontario Ltd. (39 Ltd.), which obtained an option from Mr. Platt to purchase the Kaolin Claims subject to a right of reversion.

6 In the spring of 1989, a kaolin deposit was confirmed. However, on December 8, 1989, 39 Ltd. informed Mr. Platt that it was terminating work on the Kaolin Claims. This event, according to Mr. Platt, triggered his reversionary right.

7 In March 1990, Mr. Hanemaayer and 39 Ltd. sued Mr. Platt, the respondent Andre Boudreau (an associate of Mr. Platt), James Bay Kaolin Corp. (JBK), and others for $14 million on the basis that funds advanced to Mr. Platt and JBK had not been spent on exploration and development of the Kaolin Claims as they should have been (the 1990 Hanemaayer Action).

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

8 In June 1993, Mr. Platt and others sued, among others, Mr. Hanemaayer, Mr. Kraushaar, 39 Ltd., and Great Lakes Nickel Ltd., to obtain the return of the Kaolin Claims (the 1993 Platt Action).

9 Since 1994, Farley J. has case managed both the 1990 Hanemaayer Action and the 1993 Platt Action, litigation he refers to as the "China Wars". This litigation is ongoing.

The Platt Mortgage and Bankruptcy Proceedings

10 On October 7, 1996, Mr. Boudreau obtained a judgment against 964433 Ontario Inc., now called Murrayfield Corp. (Murrayfield), for approximately $29,000. Murrayfield was controlled by John Wiebe. On September 25, 1997, Mr. Boudreau obtained an order for costs against Murrayfield in the amount of $2,500 plus disbursements. The judgment was based on a debt owed to Mr. Boudreau by Mr. Platt. The debt was guaranteed by Murrayfield. Mr. Boudreau chose to enforce the judgment against Murrayfield.

11 Murrayfield's only asset was a mortgage on Mr. Platt's home in Cochrane, Ontario registered on January 27, 1993. In 1993, Mr. Platt had mortgaged the property for $80,000 but, according to Mr. Wiebe, only $45,000 had been advanced.

12 The mortgage had been transferred from Murrayfield to Betty Jane Wheeler on February 4, 1993, then transferred back to Murrayfield on December 15, 1998.

13 In October 1998, Murrayfield attempted to enforce the mortgage by way of power of sale. Mr. Platt, in turn, commenced proceedings against 964433 Ontario Inc., Murrayfield, and Ms. Wheeler concerning the mortgage transfers. He also moved successfully before Boissonneault J. on March 10, 1999 to have the mortgage discharged from title on the basis that there was no money owing under it. No one appeared on the motion on Murrayfield's behalf.

14 Murrayfield then retained Jonathan Marler to act for it in the Platt mortgage proceedings. On March 26, 1999, Mr. Marler accepted a cash retainer of $4,000 as well as an assignment of the Cochrane mortgage as collateral security for future legal services. At the time, Murrayfield was insolvent, with debts approximating $500,000. Its only asset was the mortgage.

15 The assignment of the mortgage from Murrayfield to Mr. Marler was not registered until November 6, 2000, approximately one and a half years later.

16 On April 1, 1999, one week after Murrayfield had assigned the mortgage to him, Mr. Marler moved before Boissonneault J. on behalf of both Murrayfield's predecessor company and Ms. Wheeler, to have the mortgage reinstated on title. Boissonneault J. set aside his previous order and directed that a trial take place in the proceedings commenced by Mr. Platt, once cross-examinations on the parties' affidavits had been completed.

17 Subsequently, on June 9, 1999, Murrayfield, 39 Ltd., and Ersen Cogulu filed a petition for a receiving order against

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Mr. Platt. This put on hold the trial ordered by Boissonneault J. in the Platt mortgage proceedings.

18 When Mr. Platt sought security for costs against Mr. Cogulu, he withdrew from the bankruptcy litigation. Mr. Cogulu was replaced as a petitioning creditor by Kaarina Malmstrom, a former employee of 39 Ltd. On December 17, 1999, the date set for Mr. Platt's bankruptcy trial, the proceeding was adjourned when Murrayfield, upon being told that its mortgage debt was being disputed by Mr. Platt, withdrew as a petitioning creditor in order to avoid a lengthy hearing.

19 On February 7, 2000, Farley J. found Mr. Platt to be bankrupt and made a receiving order.

The Boudreau Mortgage Action

20 In November 2000, in an attempt to collect on some 1996 and 1997 judgments against Murrayfield, Mr. Boudreau instructed the sheriff to seize Murrayfield's interest in the mortgaged property and have it sold under writ of seizure and sale. Mr. Boudreau learned that the assignment of the mortgage to Mr. Marler had been registered on title the day before the attempted seizure.

21 On March 5, 2001, Mr. Boudreau commenced an action against Mr. Marler, Mr. Wiebe, and Murrayfield (the Boudreau Mortgage Action). He sought a declaration that Murrayfield's assignment of the mortgage to Mr. Marler was void as a fraudulent conveyance under the *Fraudulent Conveyances Act*, R.S.O. 1990, c. F.29 and/or an unlawful preference under the *Assignments and Preferences Act*, R.S.O. 1990, c. A.33, and an order setting aside the assignment.

THE TRIAL JUDGE'S RULINGS

Mr. Marler's Motion to Change Solicitors

22 Mr. Marler's firm had been the solicitors of record throughout the Boudreau Mortgage Action for all the defendants, including Mr. Marler. However, during the week prior to the trial, scheduled to be heard by Nadeau J., Mr. Marler wrote to Guy Wainwright, counsel for Mr. Boudreau, indicating that he intended to be represented separately by Kathryn Pirie. In the alternative, he proposed to act for himself.

23 Mr. Marler did not file a notice of change of solicitor or notice of intention to act in person, as required by the *Rules of Civil Procedure*, R.R.O. 1990, Reg. 194.

24 When the trial started, Mr. Wainwright objected to Ms. Pirie acting as Mr. Marler's solicitor because she was a junior associate at the law firm Mr. Boudreau had retained to defend him in the China Wars litigation. Mr. Wainwright also objected to Mr. Marler having separate counsel while Mr. Marler's law firm continued to act for the other defendants.

25 A letter from Owen Smith to Mr. Boudreau, dated January 20, 1995 and written on the old letterhead of Smith, Byck &

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Grant, Litigation Division (now Smith, Wowk), was produced to the court as proof that the firm had acted for Mr. Boudreau in the 1993 Platt Action. At the time of that action, there had been an association between Mr. Platt, Mr. Wiebe, and Mr. Boudreau. Mr. Smith had received instructions from Mr. Boudreau, and Mr. Boudreau had paid legal fees to Mr. Smith directly. At the same time, Mr. Smith had been acting for Mr. Wiebe and his company, Murrayfield.

26 Mr. Wainwright also filed a letter from Mr. Smith dated January 18, 2002 to reinforce his argument that Mr. Smith's prior relationship with Mr. Boudreau disqualified his firm from acting for Mr. Marler in the Boudreau Mortgage Action. This letter stated that the very mortgage which was the subject of the action had been prepared by Theodore Byck of Smith, Byck & Grant.

27 In this letter, however, Mr. Smith maintained that when the mortgage was drafted, he was a sole practitioner and had entered into an arrangement with Ted Byck and Richard Grant, whereby he practised litigation exclusively while the other two lawyers practised only commercial law. Accordingly, the mortgage had been prepared in a separate office by a law firm that shared nothing with Mr. Smith's law practice but the name.

28 Mr. Smith also stated in his January 18, 2002 letter that he knew of nothing arising out of the earlier retainer that had any bearing on the Boudreau Mortgage Action. He pointed out that his partner, John Wowk, had cross-examined Mr. Boudreau on an affidavit in connection with the Platt bankruptcy without objection. In his view, therefore, the only reason for Mr. Boudreau's objection to Ms. Pirie's involvement was to delay the proceedings.

29 In response to the challenge to her representation of Mr. Marler, Ms. Pirie acknowledged that she had met with Mr. Boudreau many times in preparing the defence pleadings in the China Wars litigation. She said, however, that the litigation office of Smith, Byck & Grant had taken no part in the registration or preparation of the Platt mortgage and that she did not recall knowing about it. She stated that the mortgage files were still in Mr. Smith's office in storage, and that she had not reviewed them. She also said that if there was any confidential information that was relevant to the Boudreau Mortgage Action, she did not know what it was.

30 The trial judge asked Ms. Pirie if she intended to cross-examine Mr. Boudreau:

> The Court: It's more whether there's any kind of advantage being given by knowledge by a previous engagement with the law firm and that's the real issue, I think, that I have to address . . . Before Mr. Wainwright raises it, and I think he has, if that's going to be contemplated, that's my most serious concern so far.
>
> Ms. Pirie: Well certainly the appearance is there, Your Honour.
>
> The Court: Uh-hum.
>
> Ms. Pirie: I do have to acknowledge that. That's admitted. That problem, I think, could be solved by having Mr. Andrew [counsel for the other defendants] cross-examine Mr. Boudreau and certainly, Your Honour, I do have to say that if I'm removed, Mr. Marler intends to continue on representing himself.
>
> The Court: Uh-hum.
>
> Ms. Pirie: The defendants very much want to have these proceedings completed in the next two days, Your Honour.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

31 Mr. Wainwright summarized his position to the trial judge as follows:

> I'm not bringing a motion here today to remove Ms. Pirie. Ms. Pirie is not the solicitor of record now. The only people that are entitled to attend before you are the solicitors of record and they're requesting someone assist them. So it's not quite the same as me bringing a motion to remove anybody. They're really seeking leave.
>
> Now in terms of Mr. Marler acting for himself, I'll just alert you to the fact that he has notified me that if Ms. Pirie is not acting for him he'll be acting for himself. I'll be objecting to that too . . . His counsel is Mr. Andrew. The firm of Marler and Kyle [are] the solicitors of record. Mr. Marler has not defended this by himself. He has retained counsel which happens to be his own firm and whether that was wise or it was not, it was done. I've never objected. So that's the way it is. But he is not entitled at this stage, without leave from Your Honour, to discharge his solicitors and then appear personally. And of course, we'll then get into problems of assuming he's a witness, he's going to have counsel from his firm cross-examine him as a witness. We get into lots of problems.

32 Mr. Wainwright argued, based on Sopinka J.'s decision in *MacDonald Estate v. Martin,* [1990] 3 S.C.R. 1235 (S.C.C.), that once Mr. Boudreau established that Mr. Smith's firm had a previous relationship with him that was sufficiently related to its current retainer with Mr. Marler, the court should infer that confidential information was imparted unless Ms. Pirie satisfied the court otherwise.

33 Before ruling on the challenge to Ms. Pirie's involvement, the trial judge gave her an opportunity to demonstrate that no confidential information had been imparted that could be relevant. The transcript describes the exchange as follows:

> The Court: So dealing with that first question in this case, we have Ms. Pirie who has indicated that she has been with the Smith firm from the period of 1989 to 1998, and now is back with that firm. And I note from Exhibit number one, the letter from Owen Smith of her firm, where at page two he indicates that the Smith firm defended the 1990 action against Platt and the plaintiff here, Andre Boudreau. And that Ms. Pirie, to her credit, indicates that she assisted in this defence and in fact met with Andre Boudreau many times. All of this at the same time as this mortgage was prepared by the Smith firm, which mortgage is the subject matter of this action.
>
> Therefore on the first question, I am satisfied, on what has been presented here, that there existed a previous relationship which is sufficiently related to the retainer from which it is sought to remove Ms. Pirie.
>
> And therefore, on that question, on the first question, I am . . . Ms. Pirie, giving you the . . . having regard to making the initial determination, . . . the option as to whether you wish to satisfy the court . . . that no information was imparted which could be relevant . . . with the difficulties, as he [Sopinka J.] indicates, the dilemma that he indicates exist for any counsel attempting to discharge that heavy burden.
>
> So I think in the circumstances, as I have mentioned, I am satisfied that there is a previous relationship which is sufficiently related and I will infer that there is confidential information imparted, unless you decide to discharge the burden.
>
> . . .
>
> Ms. Pirie: As I've said before, I haven't reviewed the file. I agree with Mr. Justice Sopinka that it's almost impossible to do that. As I say, I have no idea what the information would be, nor do I feel at liberty to discuss it any further. I've indicated to the court, I frankly have no recollection of having represented Mr. Boudreau specifically. Mr. Smith confirms though that we did. I have no recollection of being involved in those pleadings. I stand to be corrected, should I look at the file, but I have to be quite frank, Your Honour. I just have no recollection.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

34 The trial judge concluded that Ms. Pirie could not act for Mr. Marler.

Mr. Marler's Motion to Represent Himself

35 Mr. Marler then brought a motion requesting permission to represent himself, with Mr. Andrew of his firm continuing to represent the other defendants.

36 Mr. Wainwright argued that Mr. Marler's motion, if granted, would place Mr. Marler in the position of testifying as a witness, acting as an advocate, and, potentially, directing the defence of the other parties, contrary to the *Rules of Professional Conduct*.[1] Moreover, he argued that the arrangement Mr. Marler proposed would confer an unfair advantage on Mr. Marler. Mr. Marler's firm, in effect, could end up with the opportunity to cross-examine Mr. Boudreau twice, make two sets of submissions, and have Mr. Andrew cross-examine Mr. Marler to correct any problems with his evidence-in-chief.

37 Mr. Wainwright submitted:

> And at this late stage I'm not sure what the intent of this is. I'm not sure why they're doing it. If there's a dispute . . . The logical reason would be there's now a dispute between Mr. Marler and his co-defendants. That would be the logical reason as to why they now want separate counsel and that may be their very reason. If that's the case then I question whether the law firm of Marler and Kyle can continue to act for the other defendants because they're going to be in conflict when they're examining Mr. Marler.
>
> The other reason I can think of is . . . Do they want to conduct two cross-examinations of my client, make two sets of submissions to Your Honour? Does Mr. Marler want to give his evidence and then have his own firm cross-examine him in case there's things that need to be fixed up?

38 Mr. Andrew responded by informing the court that Mr. Wainwright had been notified of Mr. Marler's position by letter dated January 10, 2004, ten days before the trial. He informed the trial judge that he had no intention of cross-examining Mr. Marler, as it was a "very straightforward case" and, significantly, that there were no issues between the defendants.

39 The trial judge denied Mr. Marler's motion to represent himself, ruling:

> This is a very unusual request by Mr. Jonathan Marler requesting that his own firm be removed from the record for his interest at this very late stage of the proceedings. As Mr. Andrew indicated, it is a straightforward case and there's no issues between the defendants. I am not allowing the firm of Marler, Kyle, Andrew to be removed from the record for the defendant Jonathan Marler at this late stage of the proceedings.

40 After his motion was denied, Mr. Marler did not seek an adjournment of the trial. As previously indicated, Ms. Pirie had earlier informed the trial judge that all of the defendants were anxious to proceed that day. The trial proceeded with all the defendants represented by counsel of record, namely, Mr. Andrew of Mr. Marler's law firm.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

The Fraudulent Conveyance and the Unlawful Preference

41 Mr. Boudreau, Mr. Marler, and Mr. Wiebe each testified at the trial. Mr. Marler testified that the reason he had requested the assignment of the mortgage from Murrayfield was that Murrayfield "did not have much in the way of liquid assets" and that the assignment was as "security for the payment of legal fees and disbursements" to be assessed. The stated consideration for the assignment from Murrayfield to Mr. Marler was $2, but the assignment document noted that the transfer was for the purpose of securing future legal fees and disbursements that were to be incurred on behalf of Murrayfield. As previously noted, Murrayfield also gave Mr. Marler a $4,000 cash retainer.

42 The trial judge did not accept this explanation from Mr. Marler, concluding that there were no outstanding legal fees and disbursements. Moreover, Murrayfield was insolvent, being approximately $500,000 in debt. Its only asset was the mortgage from Mr. Platt. The trial judge found:

> In this matter, the Transfer of Charge from Murrayfield to Marler states that the consideration is for $2.00, although there is also a reference to "security for the payment of legal fees and disbursements" to be assessed. The testimony of Marler was that he had also received a $4,000.00 retainer from Murrayfield on or about March 26, 1999, although he could not produce a statement of account for this retainer.
>
> *It is clear on this evidence that there were no legal fees and disbursements by Marler to be assessed at that time* [emphasis added]. This Court therefore concludes that Jonathan Marler was not "a creditor" of Murrayfield at the time of apparent execution on March 26, 1999 of the Transfer of Charge to Marler.
>
> . . . [T]he unsatisfactory testimony of both Marler and Wiebe with respect to subsequent billings by Marler for questionable legal services apparently rendered, which billings were the subject of a very calculated and suspect Consent to the Assessment of Bills of Costs by Wiebe (as principal of Murrayfield), certainly cannot make this conveyance one of adequate valuable consideration. In these circumstances on the evidence presented, this Court finds that the Transfer of Charge from Murrayfield to Marler is a voluntary conveyance for inadequate or no valuable consideration.

43 In determining that the assignment was made contrary to s. 4(1) of the *Assignments and Preferences Act*, the trial judge stated:

> This legislation only operates to invalidate transactions made when the person making the conveyance is in insolvent circumstances, is unable to pay its debts in full, or knows that it is on the eve of insolvency. As indicated previously, there is no difficulty in this matter making such a finding regarding Murrayfield.
>
> This Court must also determine from the particular facts of this case whether Murrayfield made the conveyance with the intent to defeat, hinder, delay or prejudice Boudreau. If otherwise there is good consideration and *bona fides* in the Murrayfield conveyance to Marler, the mere fact that the execution of the conveyance may have the effect of defeating Boudreau is not enough. If Marler has no fraudulent intent, he cannot be affected by the fact that there was such an intent, unknown to him, in the mind of Murrayfield. Furthermore, a transaction entered into by Murrayfield in insolvent circumstances is not impeachable as being given with intent to give a preference if Marler had no knowledge of the insolvency and was not a party to such intent. Knowledge by Marler of the insolvency of Murrayfield is not sufficient in itself to cause the Transfer of Charge to be set aside as an unlawful preference. There is nothing improper in Marler obtaining security to protect himself in the event of a possible insolvency. It is quite another thing however for Marler, knowing that Murrayfield has many unpaid creditors, to remain silent or make no reasonable inquiry and then take the only remaining security from Murrayfield; particularly when the effect is to leave creditors such as Boudreau with no recourse.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

This Court is clearly not at liberty to set aside this Transfer of Charge upon the mere suspicion that it is an unlawful preference. There must be either direct affirmative evidence of fraudulent intent or controlling circumstantial evidence leading to that conclusion. However as exists here, where the natural consequence of the conveyance is to delay, hinder or defraud the creditor (Boudreau) and where the circumstances of the conveyance demonstrate badges of fraud, the question of upholding this conveyance made by the Defendants as legitimate becomes extremely strained.

In reviewing all of the evidence in this trial, it is clear that the provisions of section 4(1) of the *Assignments and Preferences Act* are satisfied. In determining whether the saving section 5(1) rescues the Defendants in these circumstances, this Court must consider whether the Transfer of Charge was made in good faith in consideration "of a present actual payment in money, or by way of security for a present actual advance of money".

44 The trial judge described Mr. Marler as follows:

[W]hen I consider his intelligence and obvious experience in dealing with matters of this nature, I am not at all satisfied with the credibility of his testimony presented to this Court. In reviewing the internal and external consistency of his testimony, his rationalization of the outrageous billing practices, his obvious self interest by many of his statements, as well as his controlling and argumentative nature demonstrated to this Court, I find that Jonathan Marler was a direct participant and a party to the intent of John Wiebe to defeat and prejudice the judgment and order of Andre Boudreau. In fact, this Court is convinced that Jonathan Marler was a central figure in the very calculated plan to defeat the enforcement by Boudreau.

45 His censorious conclusion was equally forceful:

This Court finds that all of the Defendants were depleting the only asset of Murrayfield to pursue legal proceedings without reasonable basis nor benefit to Murrayfield in its circumstances. This Court agrees that the Transfer of Charge is surrounded by "badges of fraud". There was an element of secrecy to this conveyance, compounded by the late registration of the Instrument one day prior to attempted seizure of the mortgage by Boudreau through the Sheriff. The fact that John Wiebe was not advised by Marler to obtain independent legal advice adds a further element to this secrecy. The Court is also concerned that the mortgage was the only asset of the corporation in insolvent circumstances. Add to this that the judgment and order in favour of Boudreau had existed for some time prior to the conveyance, and the inadequate valuable consideration for the Transfer of Charge. All these factors assist the Court in concluding on all of the evidence that the three Defendants were acting in concert, and not in good faith, with the intent and effect to prejudice Boudreau.

46 The trial judge summarized his findings as follows:

a) Was the Transfer of Charge made by Murrayfield "with intent to defeat, hinder, delay or defraud (or prejudice) Boudreau? Yes.

b) Was the Transfer of Charge to Marler made "upon good consideration and in good faith"? No.

c) Was the Transfer of Charge by Murrayfield to Marler made "in good faith in consideration of a present actual payment in money, or by way of security for a present actual advance of money"? No.

d) Was Marler a party and a participant to the "intent to defeat, hinder, delay or defraud (or prejudice)" Boudreau? Yes.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

47 Therefore he held that the assignment from Murrayfield to Mr. Marler was a fraudulent conveyance under the *Fraudulent Conveyances Act* and an unlawful preference under the *Assignments and Preferences Act*. The assignment was declared void and set aside.

48 Mr. Marler appealed.

ANALYSIS

49 During oral argument before this court, counsel for Mr. Marler argued that the trial judge made two errors. First, he erred in not allowing Ms. Pirie to act as solicitor for Mr. Marler and, having disqualified Ms. Pirie, in not allowing Mr. Marler to represent himself while his law firm continued to represent the co-defendants. As a result, Mr. Marler and his co-defendants were represented by the same lawyer, Mr. Andrew. Mr. Marler now claims that Mr. Andrew was too young and inexperienced to act for him.

50 Second, Mr. Marler maintains that the trial judge erred in finding that he had the requisite knowledge of Murrayfield's insolvency and of Mr. Wiebe's intent to defraud, to support the conclusion that the mortgage assignment was a fraudulent conveyance and an unlawful preference.

51 In his factum, Mr. Marler also submitted that Mr. Boudreau's claim was barred by virtue of issue estoppel or *res judicata*. He did not pursue this submission during oral argument.

a) Mr. Marler's Legal Representation and the Fresh Evidence

52 This court allowed both parties to submit fresh evidence. Mr. Marler introduced the two court orders of Boissonneault J. in the Platt mortgage proceedings and an endorsement of Riopelle J. dated October 16, 2001 regarding the pre-trial in the Boudreau Mortgage Action. The endorsement states in part: "The defendants are likely to retain trial counsel other than Mr. Marler to conduct the trial." Riopelle J.'s endorsement does not specifically refer to Ms. Pirie.

53 Mr. Marler also introduced the letter dated January 15, 2002 he had written to Mr. Wainwright indicating that Ms. Pirie would be representing him at the trial the following week. In this letter, he had indicated that, in his opinion, Ms. Pirie had not been privy to any confidential information and, should Ms. Pirie be disqualified, he intended to represent himself. Mr. Marler argued that this letter demonstrated that his application to represent himself was not untimely and that, in any event, counsel for Mr. Boudreau had notice of the possible change despite Mr. Marler's failure to follow strictly the notice requirements of the *Rules of Civil Procedure*.

54 As evidence that Ms. Pirie's involvement did not present a conflict, Mr. Marler also relied on the January 18, 2002 letter to Mr. Wainwright from Mr. Smith that had been filed as an exhibit before the trial judge, which explained Mr. Boudreau's previous involvement with the firm of Smith, Byck & Grant.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

55 Mr. Boudreau filed an affidavit, sworn by him on May 14, 2003, outlining his factual response to the appellant's fresh evidence. In it, he stated that he had instructed his counsel to object to Ms. Pirie as counsel because her firm had not only previously acted for him, but had also drafted the mortgage in issue in the proceedings. Mr. Boudreau stated that Mr. Andrews, who was described by Mr. Marler in his factum on this appeal as young and inexperienced, was born in 1942. As to Mr. Marler's concerns, expressed for the first time on this appeal, about the competence of his partner to act for him, counsel for Mr. Boudreau also questioned why, if Mr. Andrew's inexperience was a serious issue, Mr. Marler had said nothing about this at trial and was content to have him continue to act for his co-defendants, who were also his former clients.

56 The leading case on the disqualification of a lawyer based on a conflict of interest is *MacDonald Estate v. Martin, supra.* In that case, a former junior solicitor for the appellant transferred her employment to the law firm acting for the respondent. Sopinka J. held that the relevant questions were: (1) Did the lawyer receive confidential information attributable to a solicitor and client relationship relevant to the matter at hand? (2) Is there a risk that the confidential information will be used to the prejudice of the client?

57 In explaining the test, Sopinka J. wrote at p. 1260:

> In my opinion, once it is shown by the client that there existed a previous relationship which is sufficiently related to the retainer from which it is sought to remove the solicitor, the court should infer that confidential information was imparted unless the solicitor satisfies the court that no information was imparted which could be relevant. This will be a difficult burden to discharge. Not only must the court's degree of satisfaction be such that it would withstand the scrutiny of the reasonably informed member of the public that no such information passed, but the burden must be discharged without revealing the specifics of the privileged communication. Nonetheless, I am of the opinion that the door should not be shut completely on a solicitor who wishes to discharge this heavy burden.

58 At p. 1243, Sopinka J. explained that there are three competing values to be considered when resolving an alleged conflict of interest issue:

> There is first of all the concern to maintain the high standards of the legal profession and the integrity of our system of justice. Furthermore, there is the countervailing value that a litigant should not be deprived of his or her choice of counsel without good cause. Finally, there is the desirability of permitting reasonable mobility in the legal profession.

59 Finally, Sopinka J. anticipated the concerns expressed by Nadeau J. regarding the potential for Ms. Pirie to have an advantage during her cross-examination of Mr. Boudreau due to her past relationship with him, when he said at p. 1261:

> Furthermore, there would be a danger that the lawyer would avoid use of information acquired legitimately because it might be perceived to have come from the [former] client. This would prevent the lawyer from adequately representing the new client. Moreover, the former client would feel at a disadvantage. Questions put in cross-examination about per-sonal matters, for example, would create the uneasy feeling that they had their genesis in the previous relationship.

60 In *Everingham v. Ontario* (1992), 8 O.R. (3d) 121 (Ont. Div. Ct.), the Divisional Court observed: "The issue is whether a fair-minded reasonably informed member of the public would conclude that the proper administration of justice required the removal of the solicitor."

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

61 The applicable standard of appellate review was articulated by Goudge J.A. in *Chapters Inc. v. Davies, Ward & Beck LLP* (2001), 52 O.R. (3d) 566 (Ont. C.A.), at 574 and 576:

> [T]he conclusions . . . that the two retainers are sufficiently related to cast the onus on [the law firm] . . . and that [the law firm] could not discharge that onus are matters of judicial discretion. They are the product of applying a legal standard to the facts. As such, these conclusions would be subject to reversal on appeal only if . . . [the trial judge] applied the wrong legal standard or based his conclusion on irrelevant factors or on factors to which he attached inappropriate weight.
>
> . . .
>
> For the court to find that the retainers are sufficiently related, it must conclude that in all the circumstances it is *reasonably possible* that the lawyer acquired confidential information pursuant to the first retainer that could be relevant to the current matter [emphasis added].

62 I see no error in the exercise of discretion by the trial judge in not permitting Ms. Pirie to represent Mr. Marler. The evidence of her former relationship with Mr. Boudreau and Mr. Platt created the reasonable likelihood of a possible conflict, particularly given the protracted intensity and the conspiratorial claims involved in the China Wars litigation.

63 The following facts suggest that the trial judge's discretion ought not to be interfered with: Ms. Pirie met directly with Mr. Boudreau concerning his defence in the China Wars litigation; Ms. Pirie's law firm drafted the mortgage that formed the subject matter of the assignment at issue in the trial; Mr. Marler, an experienced litigator, only notified Mr. Wainwright of his intention to retain Ms. Pirie one week before the trial was scheduled to start; and Mr. Marler, despite being immediately advised that Mr. Boudreau objected to Ms. Pirie's retainer based on his former relationship with her, persisted in raising the issue at the outset of the trial without having followed the *Rules of Civil Procedure* and filing the necessary notices.

64 Of these factors, Ms. Pirie's and her law firm's prior relationships with Mr. Boudreau are the most significant justifications for the trial judge's decision, but the other factors are relevant to whether Mr. Marler can now complain that Ms. Pirie, who was never his solicitor of record, ought to have been permitted to represent him at trial.

65 The second asserted error involves the trial judge's decision, having disqualified Ms. Pirie, to prevent Mr. Marler from representing himself. Mr. Wainwright had no problem with Mr. Marler acting for himself if Mr. Andrew was also removed from the record for the other defendants. However, he argued that it was inappropriate for both Mr. Marler and his law firm to be on the record as equally participating counsel.

66 The issue is whether a reasonably informed member of the public would consider it fair for Mr. Marler to be permitted at a late stage to represent himself, leaving his co-defendants and former clients in the hands of his law partner who he suddenly decided, one week before the trial, should not represent him, notwithstanding that he had been acting for him in this lawsuit for one and a half years.

67 Mr. Marler's firm were the solicitors of record until - and including - the beginning of the trial. As previously indicated, Mr. Marler's letter to Mr. Wainwright telling him that if Ms. Pirie was disqualified, he intended to represent himself, was dated January 15, 2002. The trial was scheduled to begin the following week. Mr. Marler made no attempt to follow the *Rules of Civil Procedure*. It was clear that he was going to be a witness and that his evidence would be crucial, yet

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

he chose not to seek an adjournment to retain other counsel: see *Heck v. Royal Bank* (1993), 15 O.R. (3d) 573 (Ont. Div. Ct.).

68 In these circumstances, I would not interfere with the trial judge's discretionary decision to refuse to allow Mr. Marler to represent himself while his law firm represented the other defendants. Mr. Marler offered no evidence to this court by way of affidavit to justify his suggestion that Mr. Andrews could not - and did not - adequately represent him at the trial, or any explanation for why, if he was so concerned about his law partner's experience and ability to act, he permitted him to represent the co-defendants, who were his former clients and whose interests, as Mr. Andrews explained at trial, were the same as his.

b) The Fraudulent Conveyance and the Unlawful Preference

69 Nor do I see any basis for interfering with the trial judge's factual findings or his application of the relevant law in connection with the assignment of the mortgage from Murrayfield to Mr. Marler.

70 The trial judge was entitled to conclude that the following factors created a rebuttable presumption that Mr. Marler had the requisite intent to defeat Mr. Boudreau in accordance with s. 4(1) of the *Assignments and Preferences Act*:

a) the lack of meaningful consideration for the assign-ment of the mortgage;

b) Murrayfield's insolvency at the time of the purported assignment;

c) Mr. Marler's secrecy, evidenced by his late registration of the assignment of the mortgage only one day before Mr. Boudreau attempted to seize Murrayfield's inter-est in the mortgaged property; and

d) the outstanding judgment in Mr. Boudreau's favour.

71 Murrayfield's only asset at the time that it made the assignment was the mortgage, which was worth anywhere from nothing to $45,000. Its debts, however, totalled $500,000. Mr. Marler took a $4,000 retainer and the mortgage for *future* legal fees, since none were immediately anticipated beyond the $4,000 retainer. As previously indicated, the trial judge had found: "It is clear on this evidence that there were no legal fees and disbursements by Marler to be assessed at that time."

72 Most significantly, Mr. Marler failed to register the assignment for one and a half years, an act of secrecy that supports the trial judge's inference of fraud in these circumstances.

73 Mr. Marler billed Murrayfield $70,270 and Ms. Malmstrom $51,700, totalling $121,970, to collect debts worth dramatically less. There was no money owing on the Murrayfield mortgage and the debt to Ms. Malmstrom totalled $1,500. Mr. Marler attempted to authenticate these bills by way of a consent assessment with his co-defendant, Mr. Wiebe. These were the billings Mr. Marler relied on to justify the assignment and they represented, according to the trial judge, "outrageous" billing practices. Moreover, they were billed in connection with Murrayfield, which had debts in excess of $500,000 when it commenced legal proceedings against Mr. Platt.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

74 It is clear that the trial judge believed neither Mr. Marler nor Mr. Wiebe, to whom the onus to disprove fraud shifted once badges of fraud were demonstrated. The trial judge's credibility findings, along with his findings that Mr. Marler double and triple billed his clients, that the assignment of the mortgage was not for an initial deposit on account of fees or for outstanding legal fees, and that Mr. Marler knew that Murrayfield was insolvent at the time of the assignment, all support his conclusions that the presumption of fraud had not been rebutted, and that the assignment of the mortgage was a fraudulent conveyance and an unlawful preference.

CONCLUSION

75 I would dismiss the appeal with costs fixed in the total amount of $15,000.

***Cronk J.A.*:**

I agree.

***Juriansz J. (ad hoc)*:**

I agree.

Appeal dismissed.

Footnotes

1 Two rules of the *Rules of Professional Conduct* are relevant. Rule 2.04, Avoidance of Conflicts of Interest, states:

> (1) In this rule a "conflict of interest" or a "conflicting interest" means an interest (a) that would be likely to affect adversely a lawyer's judgment on behalf of, or loyalty to, a client or prospective client, or (b) that a lawyer might be prompted to prefer the interests of a client or prospective client.

. . .

> (3) A lawyer shall not act or continue to act in a matter where there is or is likely to be a conflicting interest unless, after disclosure adequate to make an informed decision, the client or prospective client consents.

The Commentary reads in part: "A client or the client's affairs may be seriously prejudiced unless the lawyer's judgment and freedom of action on the client's behalf are as free as possible from conflict of interest."

Rule 4.02, The Lawyer as Witness, states:

> (1) Subject to any contrary provisions of the law or the discretion of the tribunal before which a lawyer is appearing, a lawyer who appears as advocate shall not submit his or her own affidavit to the tribunal.

> (2) Subject to any contrary provisions of the law or the discretion of the tribunal before which a lawyer is appearing, a lawyer who appears as advocate shall not testify before the tribunal unless permitted to do so by the rules of court or the rules of procedure of the tribunal, or unless the matter is purely formal or uncontroverted.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

IN THE MATTER OF THE *COMPANIES CREDITORS' ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED AND IN THE MATTER OF A PLAN OR COMPROMISE OR ARRANGEMENT OF CASH STORE FINANCIAL SERVICES INC. et al

Court File No. CV-14-10518-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

Proceedings commenced in Toronto

BOOK OF AUTHORITIES OF 0678786 B.C. LTD.

VOLUME 1 OF 2

BENNETT JONES LLP
One First Canadian Place
Suite 3400, P.O. Box 130
Toronto, Ontario
M5X 1A4

Robert W. Staley (LSUC #27115J)
Raj Sahni (LSUC #42942U)
Gannon Beaulne (LSUC #63948V)

Tel: 416-777-4856
Fax: 416-863-1716

Lawyers for 0678786 B.C. Ltd.

Court File No. CV-14-10518-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE - COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF THE CASH STORE FINANCIAL SERVICES INC., THE CASH STORE INC., TCS CASH STORE INC., INTSALOANS INC., 7252331 CANADA INC., 5515433 MANITOBA INC., 1693926 ALBERTA LTD. DOING BUSINESS AS "THE TITLE STORE"

APPLICANTS

BOOK OF AUTHORITIES OF THE MOVING PARTY, 0678786 B.C. LTD. (FORMERLY THE MCCANN FAMILY HOLDING CORPORATION)
(returnable June 11, 2014)

VOLUME 2 OF 2

Dated: May 30, 2014

BENNETT JONES LLP
One First Canadian Place
Suite 3400, P.O. Box 130
Toronto, Ontario
M5X 1A4

Robert W. Staley (LSUC #27115J)
Raj Sahni (LSUC #42942U)
Gannon Beaulne (LSUC #63948V)

Tel: 416-777-4856
Fax: 416-863-1716

Lawyers for the 0678786 B.C. Ltd.

TO: THE SERVICE LIST

Party/Counsel	Telephone	Facsimile	Party Represented
Lax O'Sullivan Scott Lisus LLP Suite 2750, 145 King Street West Toronto, ON M5H 1J8 Canada Eric R. Hoaken Email: ehoaken@counsel-toronto.com **JJS Barristers** Suite 800, The Lancaster Building 304 - 8 Avenue SW Calgary, Alberta T2P 1C2 Canada Robert Hawkes, Q.C. Email: hawkesr@jssbarristers.ca	416.598.1744 416.645.5075 403.571.1544	416.598.3730 403.571.1528	Counsel for DirectCash Bank, DirectCash ATM Processing Partnership, DirectCash ATM Management Partnership, DirectCash Payments Inc., DirectCash Management Inc. and DirectCash Canada Limited Partnership ("DirectCash") who are co-defendants with The Cash Store Financial Services Inc. and The Cash Store Inc. (the "Cash Store") in class action (Court File No. 7908/12CP)
Osler Hoskin & Harcourt LLP P. O. Box 50, 1 First Canadian Place Toronto ON M5X 1B8 Marc Wasserman Email: mwasserman@osler.com Jeremy Dacks Email: jdacks@osler.com Patrick Riesterer Email: priesterer@osler.com Karin Sachar Email: ksachar@osler.com	416.362.2111 416.862.4908 416.862.4923 416.862.5947 416.862.5949	416.862.6666	Counsel to the Chief Restructuring Officer ("CRO")
Rothschild Neil Augustine Email: nycprojectoilers@rothschild.com Bernard Douton Email: nycprojectoilers@rothschild.com	212.403.3500 212.403.5411 212.403.5254	212.403.3501	Financial Advisors to the CRO

Party/Counsel	Telephone	Facsimile	Party Represented
Cassels Brock & Blackwell LLP 2100 Scotia Plaza, 40 King Street West Toronto, Ontario M5H 3C2 Wendy Berman Email: wberman@casselsbrock.com Ryan C. Jacobs Email: rjacobs@casselsbrock.com	416.869.5300 416.860.2926 416.860.6465	416.640.3107 416.640.3189	Counsel to the Applicants
FTI Consulting Canada Inc. TD Waterhouse Tower 79 Wellington Street West Suite 2010, P.O. Box 104 Toronto ON M4K 1G8 Greg Watson Email: greg.watson@fticonsulting.com Jeff Rosenberg Email: jeffrey.rosenberg@fticonsulting.com	416.649.8077	416.649.8101	Monitor
McCarthy Tétrault Suite 5300, TD Bank Tower Box 48, 66 Wellington Street West Toronto ON M5K 1E6 James Gage Email: jgage@mccarthy.ca Heather Meredith Email: hmeredith@mccarthy.ca	416.362.1812 416.601.7539 416.601.8342	416. 868.0673	Counsel to the Monitor
Goodmans LLP Bay Adelaide Centre 333 Bay Street, Suite 3400 Toronto ON M5H 2S7 Robert J. Chadwick Email: rchadwick@goodmans.ca Brendan O'Neill Email: boneill@goodmans.ca	416. 979.2211 416.597.4285 416.849.6017	416. 979.1234	Counsel to Ad Hoc Noteholders
Norton Rose Fulbright Canada LLP Suite 3800, Royal Bank Plaza, South Tower 200 Bay Street, P.O. Box 84 Toronto, ON M5J 2Z4 Orestes Pasparakis Email: orestes.pasparakis@nortonrosefulbright.com	416.216.4000 416.216.4815 416.216.4805 416.216.4853 416.216.2419	416.216.3930	Counsel to Coliseum Capital Management

Party/Counsel	Telephone	Facsimile	Party Represented
Alan Merskey Email: Alan.Merskey@nortonrosefulbright.com Virginie Gauthier Email: virginie.gauthier@nortonrosefulbright.com Alex Schmitt Email: alexander.schmitt@nortonrosefulbright.com			
McMillan LLP Brookfield Place, 181 Bay Street, Suite 4400 Toronto, ON M5J 2T3 Adam C. Maerov Email: adam.maerov@mcmillan.ca Brett Harrison Email: brett.harrison@mcmillan.ca	403.531.4700 403.215.2752 416.865.7932	416.865.7048	Counsel to Trimor Annuity Focus LP #5
Computershare Trust Company of Canada and Computershare Trust Company, NA 100 University Avenue, 11th Floor, North Tower Toronto, ON M5J 2Y1 Patricia Wakelin, Corporate Trust Officer Email: patricia.wakelin@computershare.com Shelley Bloomberg, Manager, Corporate Trust Email: Shelley.Bloomberg@computershare.com Mohanie Shivprasad, Associate Trust Officer Email: mohanie.shivprasad@computershare.com Tina Vitale, Senior VP, Corporate Trust Email: tina.vitale@computershare.com John Wahl, Corporate Trust Officer Email: john.wahl@computershare.com	416.263.9317 416.263.9322 212.805.7345 646.334.3350 (C) 303.262.0707	416.981.9777 514.981.7677	Collateral Trustee under the Collateral Trust and Intercreditor Agreement
Dickinson Wright LLP 199 Bay Street, Suite 2200 Commerce Court West Toronto, ON M5L 1G4 Michael A. Weinczok Email: mweinczok@dickinsonwright.com David P. Preger Email: Dpreger@dickinsonwright.com	416.777.4026 416.301.4883 (C) 416-646-4606	416-865-1398	Canadian Counsel to Computershare
Perkins Coie LLP 30 Rockefeller Plaza 22nd Floor New York, New York 10112-0085 United States of America Tina N. Moss Email: TMoss@perkinscoie.com Ronald T. Sarubbi	212.262.6910 212.262.6914	212.977.1648 212.977.1644	US Counsel to Computershare

Party/Counsel	Telephone	Facsimile	Party Represented
Email: RSarubbi@perkinscoie.com			
Borden Ladner Gervais Centennial Place, East Tower 1900 520 – 3rd Ave SW Calgary, AB, T2P 0R3 Josef G.A. Kruger Email: jkruger@blg.com Patrick T. McCarthy Email: PMcCarthy@blg.com	403.232.9500 403.232.9563 403.232.9441	403.266.1395	Counsel to the Trustee in Bankruptcy for Assistive Financial Corp.
Duncan Craig LLP 2800 Scotia Place 10060 Jasper Avenue Edmonton, Alberta T5J 3V9 Darren R. Bieganek, Q.C. Email: dbieganek@dcllp.com	780.428.6036 780.441.4386	780.428.9683 780.969.6381	Counsel to Mr. Cameron Schiffner
Harrison Pensa LLP 450 Talbot Street London, ON N6A 5J6 Jonathan Foreman Email: jforeman@harrisonpensa.com **Koskie Minsky LLP** Barristers & Solicitors 20 Queen Street West, Suite 900 Toronto, ON M5H 3R3 Andrew J. Hatnay Email: ahatnay@kmlaw.ca	519. 679.9660 519.661.6775 416.595.2083	519.667.3362 416.204.2872	Counsel to the Plaintiff in the class action of Timothy Yeoman v. The Cash Store Financial Services Inc. et al. (Court File No. 7908/12CP) Agent to Plaintiff's Counsel in class action (Court File No. 7908/12CP)
Siskinds LLP 100 Lombard Street, Suite 302 Toronto, ON M5C 1M3 Canada Charles M. Wright Email: charles.wright@siskinds.com Serge Kalloghlian Email: serge.kalloghlian@siskinds.com Alex Dimson Email: alex.dimson@siskinds.com	416.362.8334	416.362.2610	Lawyers for an Ad Hoc Committee of Purchasers of the Applicant's Securities, including the Representative Plaintiff in the Ontario Class Action against the Applicant

Index

Court File No. CV-14-1051800CL

ONTARIO
SUPERIOR COURT OF JUSTICE - COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF THE CASH STORE FINANCIAL SERVICES INC., THE CASH STORE INC., TCS CASH STORE INC., INTSALOANS INC., 7252331 CANADA INC., 5515433 MANITOBA INC., 1693926 ALBERTA LTD. DOING BUSINESS AS "THE TITLE STORE"

INDEX

VOLUME 1

1. *Clarke v Baillie,* [1911] 45 SCR 50, 1911 CarswellOnt 733 (SCC).
2. *Metropolitan Toronto Police Widows and Orphans Fund v Telus Communications Inc* (2003), 30 BLR (3d) 288, 2003 CarswellOnt 168 (Sup Ct), rev'd on other grounds (2005), 75 OR (3d) 784, 5 BLR (4th) 251 (CA), leave to appeal to SCC ref'd [2005] SCCA No 379, 216 OAC 399 (note).
3. *Access Cash International Inc v Elliot Lake & North Shore Corp for Business Development* (2000), 1 PPSAC (3d) 209, 2000 CarswellOnt 2824 (Sup Ct).
4. *Cliffs Over Maple Bay Investments Ltd v Fisgard Capital Corp*, 2008 BCCA 327, 296 DLR (4th) 577.
5. *Romspen Investment Corporation v 6711162 Canada Inc*, 2014 ONSC 2781, 2014 CarswellOnt 5836.
6. *Re Dondeb Inc*, 2012 ONSC 6087, 2012 CarswellOnt 15528.
7. *Romspen Investment Corp v Edgeworth Properties*, 2012 ONSC 4693, 222 ACWS (3d) 854.
8. *Tucker v Aero Inventory (UK) Ltd*, 2011 ONSC 4223, 338 DLR (4th) 577 (Sup Ct).

9. *Verdellen v Monaghan Mushrooms Ltd*, 2011 ONSC 5820, 207 ACWS (3d) 553 (Sup Ct).

10. *Re Dilollo*, 2013 ONSC 578, 97 CBR (5th) 182 (Sup Ct), aff'd 2013 ONCA 550, 117 OR (3d) 81.

11. *Keith G Collins Ltd v Canadian Imperial Bank of Commerce*, 2011 MBCA 41, 268 Man R (2d) 30.

12. *Re Holt Motors Ltd* (1966), 57 DLR (2d) 180, 56 WWR 182 (Man QB).

13. *Thorne Riddell v Fleishman,* 47 CBR (NS) 233, 1983 CarswellOnt 201 (Sup Ct).

14. *Touche Ross Ltd v Weldwood of Canada Sales Ltd*, 48 CBR (NS) 83, 1983 CarswellOnt 214 (SC).

15. *Re AR Colquhoun & Son Ltd*, [1937] WWR 222, 18 CBR 124 (Sask KB).

16. *Re Norris* (1994), 23 Alta LR (3d) 397, 28 CBR (3d) 167 (QB), rev'd on other grounds (1996), 45 Alta LR (3d) 1, 193 AR 15 (CA).

17. *Skalbania (Trustee of) v Wedgewood Village Estates Ltd* (1988), 31 BCLR (2d) 184, 70 CBR (NS) 232 (SC), aff'd (1989), 37 BCLR (2d) 88, 60 DLR (4th) 43 (CA), leave to appeal to SCC ref'd (1989), 40 BCLR (2d) xxxiii (note), 62 DLR (4th) viii (note) (SCC).

18. *Conte Estate v Alessandro*, 2002 CarswellOnt 4507, [2002] OJ No 5080 (Sup Ct).

19. *Re Fancy* (1984), 46 OR (2d) 153, 8 DLR (4th) 418 (SC).

20. *Boudreau v Marler*, 18 RPR (4th) 165, 48 CBR (4th) 188 (CA).

VOLUME 2

21. *Montor Business Corp (Trustee of) v Goldfinger*, 2013 ONSC, 237 ACWS (3d) 296.

22. *Robinson v Countrywide Factors Ltd* (1977), [1978] 1 SCR 753, 72 DLR (3d) 500.

23. *Re Garrett*, 30 CBR (NS) 150, 1979 CarswellOnt 195 (SC).

24. *Indcondo Building Corp v Sloan*, 2010 ONCA 890, 103 OR (3d) 445.

25. *Oliver v McLaughlin*, 24 OR 41, [1893] OJ No 11 (CA).

26. *Bank of Montreal v Peninsula Broilers Ltd*, 177 ACWS (3d) 405, 2009 CarswellOnt 2906 (Sup Ct).

27. *Dapper Apper Holdings Ltd v 895453 Ontario Ltd* (1996), 38 CBR (3d) 284, 11 PPSAC (2d) 284 (Gen Div).

28. *Burton v R & M Insurance Ltd* (1977), 5 Alta LR (2d) 14, 9 AR 589 (SC TD).

29. *Alberta (Director of Employment Standards) v Sanche*, 134 AR 149, 5 Alta LR (3d) 243 (QB).

30. *Dwyer v Fox*, 190 AR 114, 43 Alta LR (3d) 63 (QB).

31. *Taylor & Associates Ltd v Louis Bull Tribe No 439*, 2011 ABQB 213, 46 Alta LR (5th) 182.

32. *Maki Megbiz, KFT v Osprey Energy Ltd*, 2006 ABQB 630, 405 AR 165 (Master).

33. *Re Canwest Publishing Inc/Publications Canwest Inc*, 2010 ONSC 222, 184 ACWS (3d) 684.

Tab 21

2013 ONSC 6635
Ontario Superior Court of Justice [Commercial List]

Montor Business Corp. (Trustee of) v. Goldfinger

2013 CarswellOnt 14983, 2013 ONSC 6635, [2014] W.D.F.L. 940, [2014] W.D.F.L. 941, 237 A.C.W.S. (3d) 296, 8 C.B.R. (6th) 200

A. Farber & Partners Inc., the trustee of the bankruptcy estates of Montor Business Corporation, Annopol Holdings Limited and Summit Glen Brantford Holdings Inc. Applicant and Morris Goldfinger, Goldfinger Jazrawy Diagnostic Services Ltd., Summit Glen Bridge Street Inc., Mahvash Lechcier-Kimel, Annopol Holdings Limited and Summit Glen Brantford Inc. Respondents

In the Matter of the Bankruptcy of Summit Glen Waterloo/2000 Developments Inc.

D.M. Brown J.

Heard: October 10, 11, 2012; December 3-5, 2012; February 12-13, 2013; June 20, 2013
Judgment: October 28, 2013
Docket: 10-8629-00CL, 31-OR-207640-T

Proceedings: additional reasons at *Montor Business Corp. (Trustee of) v. Goldfinger* (2014), 2014 CarswellOnt 1169, 2014 ONSC 756 (Ont. S.C.J. [Commercial List])

Counsel: P. Shea, F. Lamie for A. Farber & Partners Inc., Trustee of the bankruptcy estates of Montor Business Corporation, Annopol Holdings Limited, Summit Glen Brantford Holdings Inc. and Summit Glen Waterloo/2000 Developments Inc.
M. Davis, B. Hughes for Morris Goldfinger, 1830994 Ontario Limited and Goldfinger Jazrawy Diagnostic Services Ltd.
F. Tayar for Mahvash Lechcier-Kimel
M. McQuade for Morris Goldfinger, 1830994 Ontario Limited and Goldfinger Jazrawy Diagnostic Services Ltd. on the charging order motion

Subject: Insolvency; Estates and Trusts; Family; Property; Corporate and Commercial; Public; Torts; Civil Practice and Procedure; Contracts; Restitution

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy and insolvency — Proving claim — Provable debts — Miscellaneous

MG invested money with JK, real estate developer who owned SG group of companies — Relationship soured, resulting in two settlement agreements — MG brought action alleging breach of first settlement agreement — Several of SG group companies were placed into bankruptcy — In bankruptcy of SGW Ltd., MG moved for determination of priority

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

of several claims advanced against proceeds realized from sale of property — Motion really involved examination and determination of proofs of claim in SGW Ltd. bankruptcy under s. 135 of Bankruptcy and Insolvency Act, exercise which trustee in bankruptcy had not performed ("claims motion") — Second proceeding consisted of application by trustee asserting preference-like claims against MG in capacity as trustee in bankruptcy of companies MB Corp., A Ltd., and SGBH Inc. ("preferences application") — MG's trial lawyers moved for order granting them charging order over any proceeds MG obtained from these proceedings — Determination was made as to claims motion — Trustee provided sufficient evidence in support of claim that SGW Ltd., at time of its bankruptcy, was indebted to MB Corp. in amount of $500,000, such indebtedness being secured by MB Corp. $500,000 charge — SGW Ltd. was indebted to MB Corp. for further sum of $25,000, but as unsecured claim, as security was never given for that amount — Evidence supported finding that at date of SGW Ltd.'s bankruptcy it owed A Ltd. at least $100,000 and that indebtedness was secured by A Ltd. $100,000 charge — Claim of trustee for secured claim in respect of $750,000 charge was disallowed, as A Ltd. did not advance any funds to SGW Ltd. when latter granted charge — Determination was also made as to claim by MG's company, 183 Ltd., based on assignment of Community Trust Company (CTC) mortgages — Claim in respect of CTC $50,000 and $500,000 charges was allowed.

Bankruptcy and insolvency --- Property of bankrupt — Trust property — Miscellaneous

MG invested money with JK, real estate developer who owned SG group of companies — Relationship soured, resulting in two settlement agreements — MG brought action alleging breach of first settlement agreement — Several of SG group companies were placed into bankruptcy — In bankruptcy of SGW Ltd., MG moved for determination of priority of several claims advanced against proceeds realized from sale of property — Motion really involved examination and determination of proofs of claim in SGW Ltd. bankruptcy under s. 135 of Bankruptcy and Insolvency Act (BIA), exercise which trustee in bankruptcy had not performed ("claims motion") — Second proceeding consisted of application by trustee asserting preference-like claims against MG in capacity as trustee in bankruptcy of companies MB Corp., A Ltd., and SGBH Inc. ("preferences application") — MG's trial lawyers moved for order granting them charging order over any proceeds MG obtained from these proceedings — MG argued that since he made all of cash payments for acquisition of property by SGW Ltd., as well as payment against VTB mortgage, he was entitled to constructive trust claim against estate of SGW Ltd. for those amounts — Claim for constructive trust dismissed — MG did not comply with claims mechanisms specified in BIA, having failed to file proof of claim in respect of trust property claim or proof of claim in respect of related debt or liability claim — Claim also failed for substantive reasons — Evidence did not support claim for constructive trust in respect of monies MG advanced to SGW Ltd. to finance part of purchase price for property and to make payment against VTB — Second release precluded MG from asserting such claim at this point in time — There was no injustice requiring remedy by way of constructive trust.

Bankruptcy and insolvency --- Administration of estate — Trustees — Duty to act fairly

MG invested money with JK, real estate developer who owned SG group of companies — Relationship soured, resulting in two settlement agreements — MG brought action alleging breach of first settlement agreement — Several of SG group companies were placed into bankruptcy — In bankruptcy of SGW Ltd., MG moved for determination of priority of several claims advanced against proceeds realized from sale of property — Motion really involved examination and determination of proofs of claim in SGW Ltd. bankruptcy under s. 135 of Bankruptcy and Insolvency Act, exercise which trustee in bankruptcy had not performed ("claims motion") — Second proceeding consisted of application by trustee asserting preference-like claims against MG in capacity as trustee in bankruptcy of companies MB Corp., A Ltd., and SGBH Inc. ("preferences application") — MG's trial lawyers moved for order granting them charging order over any proceeds MG obtained from these proceedings — MG made allegations of conflict of interest against trustee — Court expressed concern that trustee, by acting as trustee for both bankrupt and claimants, did not afford court full benefit of independent arguments in respect of claims on behalf of estate, on one hand, and claimants, on other — That said, trustee provided sufficiently fulsome record relating to claims advanced — Court was not persuaded that trustee's obvious conflict of interest in claims procedure caused inadequate record to be placed before court, although court required trustee to provide more sufficient information regard particular claim.

Bankruptcy and insolvency --- Avoidance of transactions prior to bankruptcy — Fraudulent preferences — Miscellaneous

MG invested money with JK, real estate developer who owned SG group of companies — Relationship soured, resulting in two settlement agreements — MG brought action alleging breach of first settlement agreement — Several of SG group companies were placed into bankruptcy — In bankruptcy of SGW Ltd., MG moved for determination of priority

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

of several claims advanced against proceeds realized from sale of property — Motion really involved examination and determination of proofs of claim in SGW Ltd. bankruptcy under s. 135 of Bankruptcy and Insolvency Act, exercise which trustee in bankruptcy had not performed ("claims motion") — Second proceeding consisted of application by trustee asserting preference-like claims against MG in capacity as trustee in bankruptcy of companies MB Corp., A Ltd., and SGBH Inc. ("preferences application") — MG's trial lawyers moved for order granting them charging order over any proceeds MG obtained from these proceedings — Determination was made as to preference application — Trustee's claim for declaration under s. 96(1) of Act to set aside payment of $2.5 million to MG was dismissed — Payment was not made by debtor with intent to defraud, defeat or delay creditor — Finding was same with respect to Assignments and Preferences Act and Fraudulent Conveyances Act claims.

Business associations --- Specific matters of corporate organization — Shareholders — Shareholders' remedies — Relief from oppression — Oppressive conduct — Improper payment by corporation

MG invested money with JK, real estate developer who owned SG group of companies — Relationship soured, resulting in two settlement agreements — MG brought action alleging breach of first settlement agreement — Several of SG group companies were placed into bankruptcy — In bankruptcy of SGW Ltd., MG moved for determination of priority of several claims advanced against proceeds realized from sale of property — Motion really involved examination and determination of proofs of claim in SGW Ltd. bankruptcy under s. 135 of Bankruptcy and Insolvency Act (BIA), exercise which trustee in bankruptcy had not performed ("claims motion") — Second proceeding consisted of application by trustee asserting preference-like claims against MG in capacity as trustee in bankruptcy of companies MB Corp., A Ltd., and SGBH Inc. ("preferences application") — MG's trial lawyers moved for order granting them charging order over any proceeds MG obtained from these proceedings — Trustee challenged payment of $2.5 million to MG under oppression provisions in s. 248 of Business Corporations Act (BCA) — Claims under ss. 130(4) and 248 of BCA were dismissed; claims by trustee for return of $2.5 million paid by A Ltd. to MG were dismissed — It was found that at time of payments there was no intent to defeat, hinder, delay or defraud creditors — Same findings were relied upon to conclude that A Ltd.'s payment to MB did not violate reasonable expectations of its creditors — Claim against director of A Ltd. also failed — Payments to MB were not payments under ss. 30 or 38 of BCA — Trustee's claim under s. 96(1) of BIA was dismissed, and it followed that claim against director of A Ltd. under that section as privy was also dismissed.

Bankruptcy and insolvency --- Avoidance of transactions prior to bankruptcy — Settlements of property — Miscellaneous

MG invested money with JK, real estate developer who owned SG group of companies — Relationship soured, resulting in two settlement agreements — MG brought action alleging breach of first settlement agreement — Several of SG group companies were placed into bankruptcy — In bankruptcy of SGW Ltd., MG moved for determination of priority of several claims advanced against proceeds realized from sale of property — Motion really involved examination and determination of proofs of claim in SGW Ltd. bankruptcy under s. 135 of Bankruptcy and Insolvency Act (BIA), exercise which trustee in bankruptcy had not performed ("claims motion") — Second proceeding consisted of application by trustee asserting preference-like claims against MG in capacity as trustee in bankruptcy of companies MB Corp., A Ltd., and SGBH Inc. ("preferences application") — MG's trial lawyers moved for order granting them charging order over any proceeds MG obtained from these proceedings — Trustee sought to set aside certain charges — Trustee also sought to set aside payment of $471,000 to MG — Trustee's claim under s. 96(1) of BIA dismissed; relief in respect of $471,000 granted — At time of closing of first settlement, JK and his signatory companies did not intend to defraud, defeat or delay creditors — Payment of $471,000 to MG was to be declared void, and MG had to repay that amount to trustee — MG knew that payment of $471,000 to him would prefer his interests over those of MB Corp. — MG sought and obtained payment with intent to defeat, hinder, delay or defraud another creditor, MB Corp.

Professions and occupations --- Barristers and solicitors — Solicitor's lien — Statutory charging order — Entitlement

MG invested money with JK, real estate developer who owned SG group of companies — Relationship soured, resulting in two settlement agreements — MG brought action alleging breach of first settlement agreement — Several of SG group companies were placed into bankruptcy — In bankruptcy of SGW Ltd., MG moved for determination of priority of several claims advanced against proceeds realized from sale of property — Motion really involved examination and determination of proofs of claim in SGW Ltd. bankruptcy under s. 135 of Bankruptcy and Insolvency Act, exercise which trustee in bankruptcy had not performed ("claims motion") — Second proceeding consisted of application by

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

trustee asserting preference-like claims against MG in capacity as trustee in bankruptcy of companies MB Corp., A Ltd., and SGBH Inc. ("preferences application") — MG's trial lawyers moved for order granting them charging order over any proceeds MG obtained from these proceedings — Motion for charging order granted, on terms — Fairness required that solicitor's lien be lifted to extent of requiring firm to deliver to MG those portions of its files dealing with documentation relating to certain issues — Requiring MG to pay $40,000 against unpaid amount, without prejudice to any right to assess firm's accounts, constituted reasonable and proportionate condition for lifting lien to extent to enable MG to deal with remaining issues — Normal course was to prevail, and any net funds attached by charging order were to be paid to firm.

Table of Authorities

Cases considered by *D.M. Brown J.*:

Abou-Rached, Re (2002), 2002 BCSC 1022, 2002 CarswellBC 1642, 35 C.B.R. (4th) 165 (B.C. S.C.) — considered

Bank of Montreal v. Bonner (1988), 1988 CarswellBC 500, 38 B.L.R. 45 (B.C. S.C.) — referred to

BCE Inc., Re (2008), (sub nom. *Aegon Capital Management Inc. v. BCE Inc.)* 383 N.R. 119, 71 C.P.R. (4th) 303, 52 B.L.R. (4th) 1, (sub nom. *Aegon Capital Management Inc. v. BCE Inc.)* 301 D.L.R. (4th) 80, 2008 SCC 69, (sub nom. *BCE Inc. v. 1976 Debentureholders)* [2008] 3 S.C.R. 560, 2008 CarswellQue 12595, 2008 CarswellQue 12596 (S.C.C.) — referred to

Boudreau v. Marler (2004), 2004 CarswellOnt 1502, 48 C.B.R. (4th) 188, 185 O.A.C. 261, 18 R.P.R. (4th) 165 (Ont. C.A.) — referred to

Canrock Ventures LLC v. Ambercore Software Inc. (2011), 2011 ONSC 1138, 2011 CarswellOnt 1069, 76 C.B.R. (5th) 298 (Ont. S.C.J. [Commercial List]) — referred to

Chisos Investment Co. v. Firm Capital Equities Corp. (1998), 1998 CarswellOnt 3861 (Ont. Gen. Div. [Commercial List]) — referred to

City Peel Taxi v. Hanna (2012), 91 C.B.R. (5th) 1, 2012 CarswellOnt 5416, 2012 ONSC 2450 (Ont. S.C.J.) — referred to

Coast Operations of Canada Ltd. (Trustee of) v. Ottawa Credit Exchange Ltd. (2001), 2001 CarswellOnt 568 (Ont. S.C.J.) — considered

Coast Operations of Canada Ltd. (Trustee of) v. Ottawa Credit Exchange Ltd. (2002), 2002 CarswellOnt 424 (Ont. C.A.) — referred to

Conte Estate v. Alessandro (2002), 2002 CarswellOnt 4507 (Ont. S.C.J.) — considered

Credifinance Securities Ltd., Re (2011), 74 C.B.R. (5th) 161, 2011 ONCA 160, (sub nom. *DSLC Capital Corp. v. Credifinance Securities Ltd.)* 277 O.A.C. 377, 2011 CarswellOnt 1218 (Ont. C.A.) — considered

Dapper Apper Holdings Ltd. v. 895453 Ontario Ltd. (1996), 1996 CarswellOnt 440, 38 C.B.R. (3d) 284, 11

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

P.P.S.A.C. (2d) 57 (Ont. Gen. Div.) — considered

Elias Markets Ltd., Re (2006), 2006 CarswellOnt 5597, (sub nom. *Elias Markets Ltd. (Bankrupt), Re)* 216 O.A.C. 49, 274 D.L.R. (4th) 166, 47 R.P.R. (4th) 32, 25 C.B.R. (5th) 50, 10 P.P.S.A.C. (3d) 255 (Ont. C.A.) — referred to

Fancy, Re (1984), 46 O.R. (2d) 153, 51 C.B.R. (N.S.) 29, 8 D.L.R. (4th) 418, 1984 CarswellOnt 137 (Ont. Bktcy.) — considered

Garland v. Consumers' Gas Co. (2004), 2004 CarswellOnt 1558, 2004 CarswellOnt 1559, 2004 SCC 25, 72 O.R. (3d) 80 (note), 237 D.L.R. (4th) 385, 319 N.R. 38, 43 B.L.R. (3d) 163, 9 E.T.R. (3d) 163, 42 Alta. L. Rev. 399, 186 O.A.C. 128, [2004] 1 S.C.R. 629 (S.C.C.) — followed

General Electric Canada Real Estate Financing Holding Co. v. Liberty Assisted Living Inc. (2013), 2013 ONCA 119, 2013 CarswellOnt 1919 (Ont. C.A.) — referred to

Gingras, Robitaille, Marcoux Ltée v. Beaudry (1980), (sub nom. *Tremblay, Re)* 36 C.B.R. (N.S.) 111, 1980 CarswellQue 59, [1980] C.S. 468 (Que. S.C.) — considered

Kisluk v. B.L. Armstrong Co. (1982), 40 O.R. (2d) 167, (sub nom. *Pontiac Forest Products Ltd., Re)* 44 C.B.R. (N.S.) 251, 143 D.L.R. (3d) 66, 1982 CarswellOnt 232 (Ont. S.C.) — referred to

Mamczasz Electrical Ltd. v. South Beach Homes Ltd. (2010), (sub nom. *South Beach Homes Ltd. (Bankrupt), Re)* 357 Sask. R. 82, 69 C.B.R. (5th) 1, 93 C.L.R. (3d) 209, 2010 CarswellSask 339, 2010 SKQB 182 (Sask. Q.B.) — followed

McLarty v. R. (2008), [2008] 4 C.T.C. 221, (sub nom. *McLarty v. Minister of National Revenue)* 374 N.R. 311, (sub nom. *Canada v. McLarty)* [2008] 2 S.C.R. 79, 46 B.L.R. (4th) 1, (sub nom. *McLarty v. Canada)* 293 D.L.R. (4th) 659, 2008 CarswellNat 1380, 2008 CarswellNat 1381, 2008 SCC 26, (sub nom. *R. v. McLarty)* 2008 D.T.C. 6366 (Fr.), (sub nom. *R. v. McLarty)* 2008 D.T.C. 6354 (Eng.) (S.C.C.) — followed

McLennan v. McLennan (2003), 6 R.P.R. (4th) 139, 169 O.A.C. 249, 2003 CarswellOnt 401 (Ont. C.A.) — distinguished

Nuove Ceramiche Ricchetti S.p.A. v. Mastrogiovanni (1988), 76 C.B.R. (N.S.) 310, 1988 CarswellOnt 184 (Ont. H.C.) — considered

Olympia & York Developments Ltd. (Trustee of) v. Olympia & York Realty Corp. (2003), 2003 CarswellOnt 5210, 42 B.L.R. (3d) 14, 68 O.R. (3d) 544, 46 C.B.R. (4th) 313, (sub nom. *Olympia & York Developments Ltd. (Bankrupt) v. Olympia & York Realty Corp.)* 180 O.A.C. 158 (Ont. C.A.) — considered

Piikani Nation v. Piikani Energy Corp. (2012), 58 Alta. L.R. (5th) 219, 88 C.B.R. (5th) 1, 2012 ABQB 187, 2012 CarswellAlta 459, (sub nom. *Piikani Energy Corp. (Bankrupt), Re)* 537 A.R. 211 (Alta. Q.B.) — considered

Piikani Nation v. Piikani Energy Corp. (2013), 2013 CarswellAlta 1567, 2013 ABCA 293 (Alta. C.A.) — considered

Quick Credit v. 1575463 Ontario Inc. (2010), 78 B.L.R. (4th) 234, 2010 ONSC 7227, 2010 CarswellOnt 9980 (Ont. S.C.J.) — referred to

Quick Credit v. 1575463 Ontario Inc. (2012), 2012 ONCA 221, 2012 CarswellOnt 3981, 3 B.L.R. (5th) 204 (Ont.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

C.A.) — referred to

Royal City Chrysler Plymouth Ltd., Re (1998), 1998 CarswellOnt 1041, 38 O.R. (3d) 380, 3 C.B.R. (4th) 167 (Ont. C.A.) — referred to

SimEx Inc. v. IMAX Corp. (2005), 2005 CarswellOnt 7297, 206 O.A.C. 3, 11 B.L.R. (4th) 214 (Ont. C.A.) — referred to

Soulos v. Korkontzilas (1997), [1997] 2 S.C.R. 217, 212 N.R. 1, 1997 CarswellOnt 1490, 1997 CarswellOnt 1489, 9 R.P.R. (3d) 1, 46 C.B.R. (3d) 1, 17 E.T.R. (2d) 89, 32 O.R. (3d) 716 (headnote only), 146 D.L.R. (4th) 214, 100 O.A.C. 241 (S.C.C.) — referred to

Thomas Gold Pettinghill LLP v. Ani-Wall Concrete Forming Inc. (2012), 2012 CarswellOnt 5802, 2012 ONSC 2182, 349 D.L.R. (4th) 431, 25 C.P.C. (7th) 110 (Ont. S.C.J.) — referred to

Visionwall Technologies Inc., Re (2002), 2002 ABQB 993, 2002 CarswellAlta 1397 (Alta. Q.B.) — considered

Statutes considered:

Assignments and Preferences Act, R.S.O. 1990, c. A.33
Generally — referred to

s. 4 — considered

s. 4(1) — considered

s. 4(2) — considered

s. 5(1) — considered

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

s. 2 "equity claim" — considered

s. 2 "insolvent person" — considered

s. 2 "property" — considered

s. 2 "transfer at undervalue" — considered

s. 4(2) — considered

s. 4(3) — considered

s. 4(4) — considered

s. 4(5) — referred to

s. 47 — considered

s. 81(1) — considered

s. 81.1(1) [en. 1992, c. 27, s. 38(1)] — considered

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

s. 95 — considered

s. 95(1) — considered

s. 96 — considered

s. 96(1) — considered

s. 96(1)(a) — considered

s. 96(1)(a)(iii) — considered

s. 96(2) — considered

s. 124 — considered

s. 124(4) — considered

s. 135 — considered

s. 135(1) — considered

s. 140.1 [en. 2005, c. 47, s. 90] — considered

s. 144 — considered

s. 170 — considered

s. 244 — considered

Business Corporations Act, R.S.O. 1990, c. B.16
Generally — referred to

s. 30 — considered

s. 30(2) — considered

s. 31 — considered

s. 32 — considered

s. 38 — considered

s. 38(3) — considered

s. 130 — considered

s. 130(2)(b) — considered

s. 130(2)(d) — considered

s. 130(2)(f) — considered

s. 130(4) — considered

s. 135(1) — referred to

s. 135(3) — referred to

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

s. 245 "complainant" (c) — referred to

s. 248 — considered

Fraudulent Conveyances Act, R.S.O. 1990, c. F.29
Generally — referred to

s. 2 — considered

s. 3 — considered

s. 4 — considered

Income Tax Act, R.S.C. 1985, c. 1 (5th Supp.)
Generally — referred to

Land Titles Act, R.S.O. 1990, c. L.5
s. 101(4) — referred to

Mortgages Act, R.S.O. 1990, c. M.40
s. 17 — referred to

Partnerships Act, R.S.O. 1990, c. P.5
s. 4 — considered

Planning Act, R.S.O. 1990, c. P.13
Generally — referred to

Real Property Limitations Act, R.S.O. 1990, c. L.15
Generally — referred to

Rules considered:

Rules of Civil Procedure, R.R.O. 1990, Reg. 194
R. 15.03(5) — considered

DETERMINATION of issues with respect to claims motion, preferences application, and motion for charging order.

***D.M. Brown J.*:**

I. Overview of these two proceedings

1 Starting in about 1999, Dr. Morris Goldfinger invested approximately $6.5 with Jack Lechcier-Kimel ("Kimel"), a real estate developer who owned a group of companies known as the Summit Glen group of companies. In 2007 their relationship soured, which led Goldfinger and Kimel to enter into settlement agreements in 2008 and 2009. Goldfinger's allegation that

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Kimel had breached the first, 2008 settlement agreement led him to sue Kimel and several of his companies. At the end of the day, several of the Summit Glen companies were placed into bankruptcy, with A. Farber & Partners Inc. ("Farber") appointed as trustee in bankruptcy.

2 Two proceedings were heard together by way of a hybrid trial. First, in the bankruptcy of one of the Summit Glen companies, Summit Glen Waterloo/2000 Developments Inc. ("SGW"), Goldfinger moved for the determination of the priority of several claims advanced against the $3.8 million in proceeds realized from the sale of the 105 University Avenue, Waterloo property once owned by SGW. In actual fact, the motion really involved the examination and determination of proofs of claim in the SGW bankruptcy under section 135 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B.3, an exercise which Farber, as trustee of SGW, had not performed. I will call that proceeding the "Claims Motion".

3 The second proceeding consists of an application commenced by Farber in which it asserted a number of preference-like claims against Goldfinger in its capacity as trustee in bankruptcy of three companies: Montor Business Corporation, which was not related to Kimel, as well as Annopol Holdings Limited and Summit Glen Brantford Holdings Inc., which were related to Kimel. I will call that proceeding the "Preferences Application".

4 Both proceedings were supported by extensive documentary records, including the transcripts of several out-of-court cross-examinations. In view of certain credibility issues surrounding some of the evidence, I conducted a hybrid trial of both proceedings in which focused *viva voce* evidence was heard from Kimel and two lawyers who had acted for Goldfinger at the time of the first, 2008 settlement.

5 Following the conclusion of the trial, Goldfinger changed lawyers. His trial lawyers, the Davis Moldaver LLP firm, thereupon moved for an order granting them a charging order over any proceeds Goldfinger obtained from these proceedings. I reserved judgment on that motion until the release of these Reasons on the two main proceedings.

6 These Reasons will first deal with the Claims Motion regarding the proceeds from the sale of 105 University, then with the Preferences Application and, finally, with the Charging Order Motion. To put those issues into their proper context requires a general description of the history of the business relationship between Goldfinger and Kimel.

II. The history of the relationship between Jack Lechcier-Kimel and Dr. Morris Goldfinger

A. The business relationship

7 Jack Lechcier-Kimel was in the business of developing real estate. To that end, he incorporated a number of companies, together known as the Summit Glen group of companies.

8 Kimel was a good friend of a radiologist, Dr. Morris Goldfinger. In about 1999 or 2000, Goldfinger agreed to provide money to some of Kimel's Summit Glen group of companies to fund the development and operational expenses of various properties. From February, 1999 until December, 2005, Goldfinger advanced about $6.5 million to Kimel's companies.[1]

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

9 In his November 4, 2008 affidavit Goldfinger described those advances as "interest free shareholder loans" and his arrangement with Kimel as a "joint venture" - "I had been a business partner, half-owner, and shareholder to the joint venture for more than seven years..."[2] In his September 6, 2011 affidavit Goldfinger deposed that under his arrangement with Kimel he would "have a 50% equity interest in each of the various properties", and Goldfinger was to receive 50% of the net profits realized from the sale of the properties in respect of which he was making loans - net, that is, of the repayment of his loans. As Kimel described the arrangement at trial:

> A. [Goldfinger] provided the capital, the equity with which to purchase properties and my function was to manage and redevelop the properties to a higher state where they could be sold for a profit that we would then share.
>
> Q. And do I understand that these moneys that Dr. Goldfinger advanced were loans to you or the companies and that he was to get no interest on the loans but he was to get 50% of the profits after they were resold?
>
> A. Yes, that's correct.
>
> Q. And, am I correct that there, this agreement was never reduced to writing?
>
> A. No, it wasn't.[3]

10 In one of his affidavits Goldfinger described the nature of his business relationship with Kimel as follows:

...we agreed upon the following terms:

> (a) Kimel suggested that I should participate as an equal business partner and 50% shareholder in the Summit Glen Companies (as defined herein). I would provide capital in the form of interest free shareholder loans, and in exchange, Kimel, acting as director and project operator, would provide ongoing property management at no fee or salary.
>
> (b) Both Kimel and I would retain a 50% interest in the joint venture, and a 50% ownership interest in each of the purchased properties. Kimel and I also agreed that I would become an equal business partner in the Raleigh Street Properties.
>
> (c) At all times, I retained the right to demand repayment of the shareholder loans, in addition to 50% of any growth or profit on the properties.
>
> (d) I was not obligated to provide financing to projects I did not agree to participate in. I was fully aware that Kimel had other ongoing business interests, and was not interested in providing financing to all of his projects. As such, we agreed that the projects I chose to fund would be kept separate from his other interests. Where I acted as financier, I would also act as guarantor for any first mortgage financing as would be reasonably required.[4]

11 In the Preferences Application Farber took the position that it was intended Goldfinger would be a 50% owner of the various SG group of companies into which he had invested his funds,[5] including Annopol.

B. The First Settlement: 2007/2008

12 In 2007 the business relationship between Goldfinger and Kimel broke down, and they began to negotiate its

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

dissolution. The negotiations resulted in the "First Settlement" memorialized by a Memorandum of Agreement dated December 11, 2007, but signed on May 20, 2008 and then amended on June 6, 2008. Under the First Settlement, Goldfinger would withdraw from the various projects by being repaid his shareholder loans of $6.5 million, as well as receiving an additional $5 million for what was thought at the time to be his equity in the properties by selling his shares in the various companies to Kimel.

13 As part of the negotiations of the First Settlement, Goldfinger was paid $2.5 million in December, 2007 and January, 2008. He described the payment as "consideration in contemplation of the settlement, without which I would not have proceeded to any kind of written settlement".[6] Kimel testified that the payments were "made in anticipation of the settlement".[7]

14 According to Kimel, the funds used to make that payment largely came from the sale in October, 2007 of a property owned by Summit Glen Fairway and the remortgaging of the Summit Glen Trayvan properties, with Kimel and his then wife, Mahvash Lechcier-Kimel, contributing about $200,000 of their personal funds.[8] (The actual details about the source of those payments will be discussed below.)

15 Farber, however, contended that the cheques issued in December, 2007 and January, 2008 to pay Goldfinger the $2.5 million came from Annopol, with those post-dated cheques describing the $2.5 million as payment for the "re-purchase shares". Farber also stated that the $2.5 million paid to Goldfinger came from (a) inter-company loans from related companies and (b) a loan by a third-party to Annopol. Farber asserted that Goldfinger was aware that Annopol was borrowing money to pay him.[9]

16 Although Goldfinger received that $2.5 million payment in late 2007, most of the transactions contemplated by the First Settlement did not close until June 8, 2008.

C. Kimel's breach of the First Settlement and Goldfinger's enforcement actions

17 Goldfinger contended that no sooner had Kimel entered into the 2008 First Settlement, than he breached it, in large part by dealing improperly with properties which formed part of the settlement — i.e. SG Trayvan gave a $4 million mortgage to Community Trust Company, and soon after Kimel sold the SG Fairway property.

18 In July, 2008, Goldfinger had made demands on SG Brantford and SG Bridge, as well as others, and delivered notices pursuant to s. 244 of the *Bankruptcy and Insolvency Act* to those companies.

19 On October 31, 2008, Goldfinger commenced an action seeking damages and the appointment of a receiver over a number of SG companies, including SG Brantford and SG Bridge (the "Goldfinger Action").

20 In November, 2008, Goldfinger moved in that action to appoint Zeifman & Partners Inc. ("Zeifman") as interim receiver of several SG companies, including Summit Glen Waterloo, SG Brantford and SG Bridge. By order made December 1, 2008 this Court appointed Zeifman & Partners as receiver of a number of the SG companies to which Goldfinger had made loans, including SGW, but not Annopol.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

21 The appointment of a receiver caused some of the SG companies to default on loans made to them by third party lenders. That ultimately resulted in Montor, a company owned by Jack Perelmuter, an accountant who had provided accounting services to Kimel's companies, making an assignment in bankruptcy on February 6, 2009. Farber was appointed Montor's trustee. As such, Farber then issued a series of bankruptcy applications which resulted in its appointment as trustee in bankruptcy for Annopol, SGW and SG Brantford:

(i) Kimel's wife, Mahvash Lechcier-Kimel, was the sole director of Annopol which was adjudged bankrupt on May 27, 2010; the date of the initial bankruptcy event was May 26, 2009. Farber was appointed the trustee;

(ii) SGW owned an apartment development located at 105 University Avenue, Waterloo. SGW was adjudged bankrupt on June 28, 2010; the date of the initial bankruptcy event was April 3, 2009. Farber was appointed trustee. As mentioned, in the SGW bankruptcy proceedings Farber sold that property and the proceeds of $3.8 million were paid into court;

(iii) Kimel owned all the shares of Summit Glen Group of Companies Inc. ("SGG") which was adjudged bankrupt and Farber was appointed its trustee in bankruptcy; and,

(iv) Kimel owned all the shares of SG Brantford, which was adjudged bankrupt on May 27, 2010; the date of the initial bankruptcy event was April 30, 2009. Again, Farber was appointed the trustee.

22 The appointment of the receiver also resulted in Goldfinger and Kimel defaulting on loans made to them by Community Trust Company which had been guaranteed by SGW.

23 A number of motions were brought in that receivership. Certain secured creditors successfully applied to remove properties out of the receiver's possession. Farber also moved to discharge the receiver over SG Brantford so that it could proceed with its bankruptcy application against that company, but the motion was never heard because Kimel and Goldfinger reached a new settlement of their dispute.

D. The Second Settlement: 2009

24 On December 16, 2009, Goldfinger and Kimel, Annopol and SGW settled the Goldfinger Action by entering into Minutes of Settlement (the "Second Settlement"). Goldfinger agreed to certain releases as part of that Second Settlement. Zeifman was discharged as receiver in May, 2010.

25 The key terms of the Second Settlement were as follows:

a) Goldfinger would receive a mortgage with a face value of $5 million on 40 Park Lane Circle, Toronto, a high-end property in the Bridle Path area, which Kimel earlier had bought in Mahvash's name for $9.5 million and upon which they were building a luxury house;

b) the mortgage granted to Goldfinger on SG Waterloo's property at 105 University as part of the First Settlement

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

would be discharged and replaced with a $5 million mortgage;

c) the payments to Goldfinger would be capped at $5 million. This would include any money Goldfinger had collected after the First Settlement, but not the $2.5 million he was paid in December 2007 or the $471,000 from the SG Brantford re-financing;

d) the legal proceedings would be discontinued; and,

e) the parties would exchange full and final mutual releases.

26 Goldfinger deposed that the Second Settlement represented a serious compromise of his interests: he gave up his right to further debt repayment, and mortgages he held were significantly downgraded. In his September 27, 2010 affidavit, Goldfinger deposed:

> I made significant compromises to my rights through the 2009 Settlement Agreement, as I was entitled to no further repayment of the debt that was owed to me.
>
> I agreed to significantly change the terms of my remaining security interests against 105 University and 41-67 Valleyview Road by converting them into long-term mortgages. In addition, I took on a long-term mortgage against a property that may never have sufficient equity to pay the outstanding debt to me, being Mahvash's uncompleted residential property at 40 Park Lane Circle, Toronto.
>
> The 2009 Settlement Agreement was precipitated by the fact that Jack was causing extensive costs to be incurred, and at the same time was likely to be adjudged bankrupt — which subsequently occurred when he made an assignment.
>
> This, together with the fact that little, if any, additional assets to which I had an entitlement appeared to be available — other than those already included in the Receivership — and the fact that the Receiver's requested information was not being forthcoming, were the factors that led to the 2009 Settlement Agreement.[10]

27 The Second Settlement was completed in January, 2010. Before that, Goldfinger waived registration of the $5 million mortgage on the SG Waterloo property. The $5 million mortgage on 40 Park Lane Circle was registered on January 29, 2010 in third position, behind HSBC's mortgage for $9.5 million and a judgment in favour of Community Trust Company for $4 million.

E. Post-Second Settlement Events

28 On March 19, 2010, Farber, in its capacity as trustee in bankruptcy for SGW, Annopol and SG Brantford, commenced the Preferences Application.

29 In August and September, 2010, Goldfinger acquired the shares of SGW through transactions with Kimel and his wife, Mahvash. That couple had separated in January, 2009 and divorced in November, 2010. Mahvash married Goldfinger shortly thereafter, on November 18, 2010.

30 I will deal in greater detail with some of these events at the appropriate points later in these Reasons. Let me turn, first, to the issues in the Claims Motion.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

III. The Claims Motion: the Summit Glen Waterloo Property

A. The property and its realization

31 Summit Glen Waterloo/2000 Developments Inc., an *OBCA* corporation incorporated on April 11, 2000, owned property located at 105 University Avenue, Waterloo (the "Property"). SGW had purchased 105 University pursuant to an agreement of purchase and sale with Bolliger Holdings Corporation dated January 12, 2000, for $950,000.

32 On April 3, 2009, Farber, acting as trustee of Montor, applied for a bankruptcy order against SGW. A bankruptcy order was made against SGW over a year later, on June 28, 2010. Farber was appointed trustee. Pursuant to a consent order made November 22, 2010, Farber sold 105 University for $3,807,504.68. Those funds were paid into court; the trial of the Claims Motion concerned the entitlement of certain claimants to those proceeds.

B. The claims and the issues

33 At trial, several claims were advanced against the proceeds of the sale of 105 University, Waterloo:

(i) *Montor Business Corporation*. Farber acts as Montor's trustee in bankruptcy and it advanced a secured claim of $500,000 in respect of a loan made to SGW in December, 2005 and extended twice. The loan was secured by a charge on title to the Property. There is no dispute that at the direction of SGW, Montor paid the proceeds of the loan to Annopol. 183 and Goldfinger took the position that by paying the loan proceeds to Annopol, Montor enjoyed no claim, secured or otherwise, against the SGW sale proceeds or, as put by Goldfinger in his December 16, 2010 affidavit: "[T]here is no credible evidence that... Montor advanced any funds to SG Waterloo in support of the secured interest that is registered in [its] favour". Montor also advanced a secured claim in the amount of $25,000.00.

(ii) *Annopol Holdings Limited*. Farber acts as Annopol's trustee in bankruptcy and asserted a claim against SGW based on inter-company loans with Annopol. SGW signed a $100,000 promissory note in favour of Annopol. As well, SGW granted Annopol a $100,000 charge against the Property and a $750,000 charge against the Property. 183 and Goldfinger opposed Annopol's claim on the basis that Annopol was merely a "conduit" for money loaned to the Summit Glen group of companies and therefore no indebtedness had arisen between Annopol and SGW.

(iii) *The Summit Glen Group of Companies Inc. ("SGG")*. Again, Farber acts as SGG's trustee in bankruptcy and asserted an unsecured claim against the sale proceeds in the amount of $565,998 based on inter-company loans and payments made by it for the benefit of SGW. 183 and Goldfinger opposed SGG's claim on the basis that the latter was merely a "conduit" for money loaned to Summit Glen companies and therefore no indebtedness had arisen between SGG and SGW.

(iv) *1830994 Ontario Limited*. The principal of 183 is Dr. Morris Goldfinger. 183 advanced claims against SGW based on an assignment to it from Community Trust Company of two mortgages granted to CTC by SGW in the amounts of $50,000 and $500,000; and,

(v) *Dr. Goldfinger*. As a lender of money to Kimel and his companies, Goldfinger asserted a constructive trust claim against the sales proceeds. Also, as the shareholder of SGW, Goldfinger asserted a claim to the sale proceeds. In his notice of motion initiating the Claims Motion, Goldfinger requested that following the determination of the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

priorities amongst 183, Montor and Annopol, the net surplus funds held in Court be paid out to him.

34 In terms of the registration of the various mortgages against the title to 105 University at the time of SGW's bankruptcy, there is no dispute that as a result of various postponements the CTC mortgages stood in first and second position, followed by the Montor mortgage and then the mortgages granted to Annopol.

35 As claimants, each of Montor, Annopol, SGG and 183 Ontario must prove their claims against SGW. I adopt, as a comprehensive summary of the principles which guide assessing any claim made by a creditor against the estate of a bankrupt the following passages from the decision of the Saskatchewan Court of Queen's Bench in *Mamczasz Electrical Ltd. v. South Beach Homes Ltd.*:

> [35] To succeed, the [the creditor] must establish that it has a claim provable in bankruptcy on the day on which the bankrupt became bankrupt... Section 121 of the *BIA* is the governing section and it provides:
>
>> 121. (1) All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or to which the bankrupt may become subject before the bankrupt's discharge by reason of any obligation incurred before the day on which the bankrupt becomes bankrupt shall be deemed to be claims provable in proceedings under this Act.
>
> [36] The scope of 'debt' and 'liability', employed in that provision, has been succinctly summarized in text authorities:
>
>> A debt is a sum due by certain and express agreement, a specified sum of money owing to some person from another, including not only the obligation of a debtor to pay, but the right of a creditor to receive and enforce payment. To be a provable claim, a debt must be due, either at law or in equity, by the bankrupt to the person seeking to prove a claim and must be recoverable by legal process.
>>
>> The meaning of the word "liability" is broader than that of the word "debt", including almost every character of hazard or responsibility and in particular, as provided in s. 121, includes all obligations to which the bankrupt is subject on the day on which he or she becomes bankrupt. [footnotes omitted] (Honsberger and DaRe, *Bankruptcy in Canada*, 4th ed, (Aurora: Canada Law Book, 2009) at p. 390)
>
> [37] Failure to disclose a claim in its records or in its statement of affairs does not affect the validity of the claim and has been found to be an irrelevant consideration. *Flewitt v. Agravoice Productions Ltd. (Trustee of)* (1986), 61 C.B.R. (N.S) 280.
>
> [38] Inasmuch as s. 121 deals with the substantive right to participate in estate assets, sections 121 and 135, read together, address the method and process employed to determine claims. These sections provide:
>
>> 124. (1) Every creditor shall prove his claim, and a creditor who does not prove his claim is not entitled to share in any distribution that may be made.
>>
>> (2) A claim shall be proved by delivering to the trustee a proof of claim in the prescribed form.
>>
>> . . .
>>
>> (4) The proof of claim shall contain or refer to a statement of account showing the particulars of the claim and any counter-claim that the bankrupt may have to the knowledge of the creditor and shall specify the vouchers or other evidence, if any, by which it can be substantiated.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> . . .
>
> 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.
>
> . . .
>
> (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.

. . .

[39] It is undisputed that a creditor who wishes to participate and share in estate dividends must prove its claim. (s. 124(1) *BIA*) This process begins with filing a proof of claim in the prescribed form which shows and/or includes:

> ... the particulars of the claim and any counter-claim that the bankrupt may have to the knowledge of the creditor and <u>shall specify the vouchers or other evidence, if any, by which it can be substantiated</u>." (s.124(4) *BIA*)

[40] The underlined words in s. 124(4) clearly impose an evidentiary burden on creditors to file sufficient and adequate material to enable the trustee to "make an informed decision as to whether the claim has merit." (Roderick Wood, *Bankruptcy & Insolvency Law*, (Toronto: Irwin Law, 2009) at p. 243) Subsection 135(1) imposes a corresponding duty on trustees to examine every proof of claim and the grounds in support to determine validity (s. 135(1) *BIA*). This duty extends to proposals. (*Re Toronto Permanent Furniture Showrooms Co.* (1960), 1 C.B.R. (N.S.) 16).

[41] Where a trustee is unsatisfied with the material provided in support of a claim, the trustee has both a right and duty to demand further evidence from the creditor. In the exercise of this duty, the trustee may conduct examinations or obtain the production of documents. (see s. 163 *BIA*; Houlden and Morawetz, *Bankruptcy and Insolvency Law of Canada*, 4th ed. looseleaf, vol. 2, p. 5-181)

. . .

[44] Decided cases have framed the issue of onus or burden of proof in terms of creditors' duties and sufficiency of response. In *Re Norris* (1988), 67 C.B.R. (N.S.) 246 (Ont. Sup. Ct.) the trustee requested additional material from the creditor (Canada Revenue Agency "CRA") in support of its claim. The CRA in reply provided a copy of the notice of assessment (*Income Tax Act*, R.S.C. 1985, c. 1 (5th supp.)) but nothing more. The trustee found this reply inadequate and disallowed the claim. Although ultimately overturned on appeal on the 'adequacy' issue ((1989), 75 C.B.R. (N.S.) 97 (Ont. C.A.)), the following comments are worth noting:

> In my opinion the proof of claim with a statement of account, vouchers and/or supporting evidence should be sufficient to enable the trustee to make an informed decision as to whether the claim represents a claim which has merit and should be allowed or whether it is a claim unsupported by particulars and supporting material being in the nature of a claim which the trustee should disallow.

[45] The British Columbia Court of Appeal in *Port Chevrole*, *supra*, considered the appeal from the perspective of creditor compliance with s. 124(4) of the *BIA*. Examined factually, the Court found the creditor had failed to specify the vouchers or provide any other probative evidence to support its claim, and in consequence had failed to meet the threshold of 'sufficiency' required by s. 124(4).

[46] Case authority is quite clear: the creditor bears the onus of establishing its claim. It does so by providing vouchers,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

statement of account or other evidence sufficient to substantiate it. Put another way, the creditor must provide sufficient evidence so as to enable the trustee to make an informed decision on the validity of the proposed claim. The test to be applied when examining proofs of claim has been described as follows:

> In deciding the validity of a claim, *certainty* is not the test. If the method used in calculating the amount of the claim is reasonable and the evidence in support of the claim is relevant and probative, the claim should be admitted. *Re HDYC Holdings Ltd.* 1995 CanLII 488 (BC SC), (1995), 35 C.B.R. (3d) 294. [Houlden and Morawetz p. 5-181; emphasis added]

[47] If a creditor adduces relevant and probative evidence from which a valid claim can be reasonably inferred, the test has been met and the claim is provable. In the face of that, particularly where a trustee has suspicions, the obligation shifts to the trustee to investigate further. Disallowing a claim based on a hunch or suspicion is not enough.

> The trustee is entitled to have all claims investigated and if, necessary, litigated before he or she can be called to pay....The trustee "is entitled to go behind such forms to get at the truth....When the trustee is in doubt as to whether a claim should be allowed or disallowed, the trustee may apply to the court for directions.
>
> [*Bankruptcy In Canada*, p. 409][11]

C. Some comments about the written record filed at trial

36 Farber reported that it had only been able to recover limited books and records for SGW and Annopol. At one point it had to resort to obtaining entry orders and search warrants to secure SGW records. That, no doubt, hampered Farber's ability to gain a clear picture of the financial history of both companies, however the determination of the various claims will have to be based on what documentation exists and was adduced at trial.

37 Much pre-trial skirmishing went on between counsel for Farber and counsel for Goldfinger over the production of documents in the possession of Farber, wearing its many trustee hats.[12] I wish to express my disappointment at the evident lack of co-operation between counsel, co-operation mandated by the "3Cs" principle of the Commercial List. That lack of cooperation resulted in an unnecessarily large and unfocussed evidentiary record, necessitating its lengthy review, and resulting in the delay in releasing these Reasons.

IV. Summit Glen Waterloo: Montor's claim

A. Evidence

38 Farber, as trustee of Montor, filed an April 29, 2011 proof of claim in the SGW bankruptcy proceeding for a secured claim of $583,486.06, plus interest and costs in accordance with the security. Although the proof of claim recorded the principal amount loaned as $525,000, Farber's January 11, 2011 Report stated that Montor was asserting a secured claim of $500,000, plus interest and costs.

39 Jack Perelmuter, an accountant, owned Montor which carried on business providing mortgage and other loans primarily to Kimel's companies, including SGW and Annopol. Through his accounting firm Perelmuter had provided accounting services to the Summit Glen group of companies, including Annopol, SGW and SGG.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

40 On his September 19, 2012 out-of-court examination, Perelmuter stated he could not recall Montor's mortgage transaction with SGW because there had been so many transactions with Kimel. Consequently, his evidence was given at a very general level and Perelmuter, by and large, let the documents speak for themselves.

41 In December, 2005, Montor agreed to loan SGW $500,000 secured by a charge over 105 University. Montor and SGW engaged counsel to document the loan. Kimel, in a December 1, 2005 email to his counsel, Mike McCarter, stipulated that the mortgage to Montor would stand in third place, behind the CTC charges, but ahead of Annopol's and, in addition:

> We would also like all funds from this mortgage to be paid directly to Annopol Holdings Limited rather than the borrower company. Will you please prepare the necessary direction to this effect, for execution by the borrower.

42 Kimel, in a December 2, 2005 email to Perelmutter, which he signed on behalf of SGW, directed that Montor make the cheques for the $500,000 loan payable to Annopol, not SGW, and continued:

> Notwithstanding this, we acknowledge that we [SGW] are solely responsible for the repayment of all and any monies advanced by you under this loan, and all interest that pertains, as it falls due and until maturity of the loan, whether monies were actually advanced to Annopol Holdings or to ourselves.

43 Montor did so. As a result, Montor wrote two December 5, 2005 cheques to Annopol, one for $165,000 and the other for $35,000. The same day Montor wrote a cheque to its lawyers for $300,000 in respect of the "2nd mortgage". Kimel signed a direction authorizing Montor's lawyers to pay the proceeds of the transactions to his own lawyers. That was done, and Kimel's lawyers wrote a cheque to Annopol. In the result, the $500,000 Montor loan was deposited into Annopol's account and, of that amount, about $413,000 was disbursed by Annopol to other SG companies. At trial Kimel did not dispute that Montor had disbursed the borrowed funds in accordance with his direction.

44 On December 12, 2005, Mahvash signed a director's resolution authorizing SGW to borrow $500,000 from Montor and to grant security for the loan.

45 SGW granted Montor a $500,000 charge on 105 University which was registered on December 15, 2005 (the "Montor $500K Charge"). As well, on December 5, 2005, Kimel, on behalf of SGW, executed a promissory note in the amount of $200,000 in favour of Montor. Although Farber could not locate a similar promissory note for the remaining $300,000 of Montor's $500,000 advance to SGW, Kimel testified that he had no doubt such a promissory note had existed.[13] In any event, a subsequent promissory note dated July 7, 2008, given on the extensions of the loan evidenced the $500,000 debt. As part of the December, 2005 transaction, Annopol postponed its two mortgages on the Property to that of Montor.

46 The terms of the loans were such that payments were interest only, and SGW provided Montor with post-dated cheques for the interest payments.[14] Farber adduced evidence that SGW made interest payments to Montor until the appointment of Zeifman as its receiver. Farber was not able to find any evidence that SGW had made payments against the principal amount of the loan.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

47 Prior to trial, in an August 24, 2009 affidavit, Kimel had deposed that the funds borrowed from Montor were used for purposes related to SGW.[15] Over a year later, in a November 16, 2010 affidavit, Kimel did an about-face, contending that SGW had received no funds from that mortgage.[16] At trial he questioned the correctness of his initial evidence:

> Q. In paragraph six, you indicate that the proceeds from the loan were paid out for three purposes, to discharge a collateral debt owing to Community Trust by Summit Glen Waterloo, to pay costs related to two Ontario Municipal Board zoning proceedings relating to Summit Glen Waterloo, to pay for the operating and related expense of Summit Glen Waterloo, that statement correct?
>
> A. I'm not sure that is entirely correct, no.[17]

Kimel did admit that some of the money Montor had advanced to Annopol was used to pay SGW, but when at trial he was asked why he was changing his affidavit evidence about the use of the Montor loan, Kimel's answer revealed that little stock can be put parts of his evidence:

> Q. Mr. Davis took you to payments out from Annopol to Summit Glen Fairway. So, could Fairway have been using those fund to pay down Community Trust company?
>
> A. I don't remember that any of the Montor funds were used to pay anything to Community Trust Company.
>
> Q. Okay, then why would you swear they were?
>
> A. In, uh, previous years, prior to my own bankruptcy, and, uh, the collapse of my business, I was involved in many different aspects of litigation, and, um, sometimes in doing affidavits or in providing responses at that point in time, I was often attempting to cater responses to allow for what I thought might still be the protection and ultimate salvation of my business. And, because of the constraints that I felt I may have coloured things in a certain fashion which, uh, was not entirely correct.
>
> Q. So you lied.
>
> A. Yes.[18]

48 At SGW's request, Montor twice renewed the loan and the charge, and Montor loaned an additional $25,000 to SGW by way of cheque dated November 25, 2008. On November 20, 2008, SGW signed a promissory note in favour of Montor for the sum of $525,000, which was accompanied by a "commitment to replace note with mortgage security". No new mortgage security in favour of Montor was registered following that commitment. Perelmuter testified that he was not sure whether Kimel ever gave the commitment to his lawyers:[19]

> And we're renewing it for $500,000 plus 25 which makes 525,000. So basically I would expect that there is going to be 525,000 renewal by a mortgage. I'm not sure that was ever done by him. At this point, this is 2008, maybe at this point he start letting things go.[20]

49 Although Montor's February 6, 2009 statement of affairs in its bankruptcy proceeding listed the amount of the security it held against SGW at $525,000, Montor's bankruptcy application against SGW estimated the value of its security at $500,000, with the amount of the total indebtedness at $525,000.[21]

50 SGW included in its March 31, 2006 and March 31, 2007 financial statements, and showed in its accounting records, the $500,000 debt owing to Montor.[22] Kimel swore a statement of affairs in SGW's bankruptcy which confirmed that SGW owed Montor $500,000 and that Montor enjoyed security over 105 University for that loan.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

51 At trial Kimel admitted that SGW was obliged to repay the Montor loan:

> Q. The money wasn't advanced to Annopol, it was paid to Annopol. The loan was to Summit Glen Waterloo, wasn't it?
>
> A. Yes.
>
> Q. And Summit Glen Waterloo was obliged to repay the funds, correct?
>
> A. Yes.[23]

52 Goldfinger and 183 took the position that Montor had failed to prove how much was owing to it on account of its security because it had not accounted for any monies realized from the various companies which had received the proceeds of the December, 2005 Montor loan. 183 and Goldfinger opposed Montor's claim on the ground that since SGW had directed Montor to pay Annopol the proceeds from the loan to SGW, the charge no longer had any effect as against the Property.

B. Analysis

53 There is no dispute that Montor lent $500,000 to SGW. As well, the evidence supports a finding that SGW gave promissory notes in that amount to Montor, both at the time the loan was advanced and on its extension, and I so find. The consideration necessary to support a promissory note includes not only a benefit conferred on the maker of the note, but also a benefit conferred on a third party at the request of the maker of the note. A party to a note may receive value for a note or consideration for a note even though it does not personally receive the proceeds of a loan pursuant to it.[24]

54 Farber submitted that Montor provided SGW with two kinds of consideration in support of the promissory notes — the advance of the $500,000 to the person directed by SGW and the extensions of the loans. Goldfinger contended that the extent of SGW's debt to Montor was limited to those borrowed funds which SGW used for its own corporate purposes. I accept the submission of Farber and reject the position advanced by Goldfinger. SGW, as debtor, directed that the funds it borrowed from Montor be paid to Annopol. Montor complied with the debtor's direction. How SGW, or its designated payee, Annopol, used the funds borrowed by SGW is not relevant to the question of whether SGW is indebted to Montor.

55 SGW granted the Montor $500K Charge to secure the debt evidenced by the promissory notes. 183 and Goldfinger did not question the validity of the charge.

56 Goldfinger argued that because Farber had never accounted for the monies received from the other Kimel Summit Glen companies which received the proceeds of the $500,000 Montor loan, Montor had not established the amount of the debt outstanding to it at the time of the bankruptcy of SGW. I disagree. The indebtedness was that of SGW to Montor. Certainly, if any monies had been re-paid to Montor on account of the $500,000 loan to SGW, either from SGW or from another Summit Glen company at SGW's direction, due account would have to be made for such amounts. However, notwithstanding the extensive documentary disclosure made in this proceeding about the affairs of Montor and SGW, no evidence of any such repayment was adduced. On the contrary, the evidence disclosed the following state of affairs:

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(i) The only repayments of the loan made by SGW or any other Summit Glen company prior to the appointment of Zeifman as receiver of SGW were the monthly payments of interest to Montor in accordance with the terms of the loan;

(ii) Kimel, in his sworn statement of affairs regarding SGW, confirmed that SGW owed $500,000 to Montor; and,

(iii) the financial statements of SGW for the years ended March 31, 2006 and 2007 recorded SGW's debt to Montor of $500,000 as part of its "mortgages payable" liabilities.

57 In light of that evidence, I conclude that Farber, in its capacity as trustee of Montor, has provided sufficient evidence in support of its claim that SGW, at the time of its bankruptcy, was indebted to Montor in the amount of $500,000.00, and that such indebtedness was secured by the Montor $500K Charge.

58 So, too, the evidence adduced by Farber, in its capacity as trustee of Montor, established that SGW was indebted to Montor for the further sum of $25,000 advanced on November 25, 2008. However, the evidence disclosed that SGW never gave security for that amount, so I allow that claim as an unsecured one.

59 Both claims are allowed with interest until the date of payment in accordance with the terms of the loans.

IV. Summit Glen Waterloo: Annopol's claim

A. The amounts claimed

60 Farber, in its capacity as the trustee in bankruptcy of Annopol, advanced claims in the SGW bankruptcy based on inter-company loans made over the years by Annopol to SGW in order to fund operating and development expenses for 105 University. As trustee of Annopol, Farber filed two proofs of claim dated February 28, 2011, in the SGW bankruptcy:

(i) The First Proof of Claim made an unsecured claim of $420,000 and a secured claim of $100,000. In support of its claim, Farber attached two charts.[25] One recorded payments by Annopol to SGW from its TD Bank account between June 27, 2000 and March 24, 2005, totaling $152,600. The other recorded transactions between Annopol and SGW from an HSBC account showing net payments to SGW of $367,400 between September 13, 2005 and December 4, 2008. In a response to a refusal made on the cross-examination of Martin Cyr, one of the trustees, Farber stated that it arrived at the amount of the claim based upon a review of the banking records of Annopol and SGW to identify inter-company loan transactions;

(ii) The Second Proof of Claim made a secured claim of $750,000. In support of the claim Annopol's trustee attached a SGW director resolution authorizing the borrowing and the Annopol $750,000 Charge. No other evidence to support advances under the charge was attached to the proof of claim. Although on a cross-examination Martin Cyr, the trustee, refused to explain why $750,000 was put in the proof of claim on the basis that the question went beyond the permitted scope of the examination,[26] in a subsequent response Farber stated that it used the $750,000 for Annopol's proof of claim because it "was the face amount of the charge/mortgage".

61 183 and Goldfinger took the position that SGW did not owe any money to Annopol because Annopol had not carried on any business, but merely had acted as a "conduit" for money loaned by third parties to SGW.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

62 In his trial evidence Kimel acknowledged that Annopol did carry on some business with third parties, specifically the making of short term loans,[27] and did own some properties, usually for *Planning Act* purposes. On a Statement of Personal Net Worth dated August 29, 2006, long before the breakdown in his relationship with Goldfinger, Kimel went even further, describing Annopol as a "50% joint venture partner in a number of Commercial/Industrial properties located in Southwestern Ontario" with a value of $8 million.[28]

63 As mentioned, Farber also is the trustee in bankruptcy of Annopol. According to a March 19, 2012 Claims Register for that estate, secured claims of about $578,000 and unsecured claims of approximately $6.848 million have been filed, of which Montor filed an unsecured claim for $2.7 million and Goldfinger filed a contingent proof of claim for $2.956 million.

B. Evidence: the Annopol $750K Charge

64 SGW's acquisition of 105 University closed on April 14, 2000. A few days before, on April 11, 2000, Mahvash, as sole director of SGW, passed a resolution authorizing SGW to borrow $750,000 from Annopol upon the terms of a draft mortgage.

65 When SGW acquired the 105 University property on April 14, 2000, Kimel caused Annopol to register against title the Annopol $750K Charge. It was not disputed that at the time of registration Annopol did not advance any money to SGW.[29] Goldfinger deposed that he did not learn about this mortgage until 2007, when his relationship with Kimel soured. I accept his testimony on that point.

66 By its terms, the Annopol $750K Charge required the on-going payment of interest only and the mortgage was to mature two years later. The terms contained in the Schedule to the Charge spoke only about the "principal sum hereby secured", and the Schedule contained the standard "no obligation to advance" clause. Farber was not able to locate any evidence that as of the date of registration Annopol had advanced $750,000 to SGW or that SGW had made a promissory note in that amount to Annopol.

67 In its January 18, 2011 Report Farber stated:

> Farber acknowledges that it does not have much information with respect to the Annopol $750,000 Charge.[30] This is due to the lack of books and records for SG Waterloo and Annopol.
>
> Based on the evaluation of information, it appears that the Annopol $750,000 Charge may have been intended to be collateral security for loans advanced by Annopol to other companies to protect third parties lending money to Annopol.

Farber did produce a schedule summarizing transfers Annopol made to other Summit Glen companies. By the same token, Annopol had the benefit of a number of charges against properties owned by other Summit Glen companies.

68 As of the time of its January 18, 2011 Report, Farber stated that "further evidence is required with respect to the Annopol $750,000 Charge". In its June 25, 2012 Report, Farber stated:

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Aside from the documentary evidence referenced in connection with the Annopol $100K Charge, Farber has not located any documentary evidence to establish that cash advances beyond the advances identified above [i.e. $557,600] were made by Annopol to SG Waterloo.

69 As to advances made by Annopol to SGW subsequent to the granting of the Annopol $750K Charge, Kimel's evidence at trial was inconsistent. On the one hand, under examination by counsel for Farber, Kimel testified as follows:

Q. Were there subsequent advances?

A. By Annopol to Waterloo?

Q. Yes.

A. Yes.

Q. Yes. So the mortgage would've secured those subsequent advances.

A. I suppose so, yes.

Q. That was what it was intended to do, to ensure that to the extent Annopol was advancing funds into Summit Glen Waterloo, those advances would be protected?

A. Yes.

Q. Thank you. Did you tell Dr. Goldfinger that?

A. No.[31]

. . .

Q. And then in 2009 when you settled with Goldfinger, those mortgages remained on the properties, correct?

A. Yes.

Q. And they would secure any advances, or intended to secure, any advances that Annopol made to Summit Glen Waterloo over the period to develop the property, correct.

MR. DAVIS: Sorry, I missed that question.

Q. Sorry. The intention of the mortgages was to secure advances made by Annopol to Summit Glen Waterloo, correct?

A. Yes.

Q. Thank you.[32]

On the other hand, under examination by Goldfinger's counsel, Kimel contradicted that evidence.[33]

70 On June 22, 2000, Kimel wrote to his lawyer asking that the amount secured by the $750,000 mortgage be increased to $850,000. He had so written in response to his lawyer's letter of June 14, 2000 asking whether Kimel had "had any further thoughts about securing your family's injection of monies into projects with registered mortgages".[34] In the result, the amount

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

of the $750,000 mortgage was not increased.

C. Evidence: The Annopol $100K Charge

71 An October 18, 2000 resolution of the director of SGW approving the Annopol $100K Charge indicated that the charge was to secure advances to be made by Annopol up to $100,000 and was "to better secure the present *and future indebtedness* of the Corporation to the Lender..." SGW executed a *five-year* promissory note dated October 18, 2000 for the lesser principal amount of: (a) $100,000 and (b) "the unpaid balance of all advances made by the Lender to the undersigned under the loan as recorded by the Lender on the grid on the reverse hereof." No amounts were recorded on the grid. On re-examination Kimel contended that he did not read the resolution or promissory note before they were signed.

72 By its terms, the Annopol $100K Charge registered on November 10, 2000, stated:

> This Charge is held by the Mortgagee as security for the payment of all indebtedness of the Company to the Mortgagee relating to loans to Summit Glen Waterloo/2000 Developments Inc. which indebtedness is referred to as the "Indebtedness".

73 It was not disputed that at the time of registration of the Annopol $100K Charge, Annopol did not advance any money to SGW.[35]

74 Kimel testified that there was no loan of money corresponding to the registration of each mortgage. Instead, the mortgages were placed on the property to secure the equity in the property in favour of a company controlled either by Kimel or his wife, Mahvash.

D. The state of the accounts between Annopol and SGW

75 Farber's Reports described three basic features of the financial relationship between Annopol and SGW:

> (i) Between 2000 and 2005 Annopol wrote cheques to SGW which were noted as shareholder loans. When the cheques written by Annopol were deposited into SGW's bank account, they were recorded as loans from Annopol. SGW wrote cheques to Annopol which were described as the repayment of loans;
>
> (ii) From 2005 to 2009 there were multiple transfers between the bank accounts of Annopol and SGW which were recorded as loans from Annopol to SGW and repayments by SGW to Annopol;
>
> (iii) Annopol borrowed funds from third parties which were deposited into its bank accounts, and in most cases the loans to Annopol from third parties did not parallel the transfers from Annopol to SGW in that the records did not disclose a deposit of third party funds into Annopol followed by an immediate payment out of Annopol's bank account to a SG group company;
>
> (iv) The accounting records of Annopol and SGW reflected an inter-company loan from Annopol to SGW, although the quantum of the loan reflected on the accounting records of Annopol and of SGW did not match each other, nor did the quantum match the amount of the inter-company loan determined by Farber based on the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

companies' banking records.

76 Farber, as trustee for Annopol, relied for its claim on the evidence concerning the intercompany transactions between Annopol and SGW. Farber reported that it had been able to reconstruct the inter-company account for Annopol and SGW for the period March, 2005 until May, 2010 from HSBC account records. In terms of the TD Bank records for the 2000 to 2005 period, Farber reported that they were not as extensive.

Bank account records

77 As mentioned, in support of its First Proof of Claim for an unsecured claim of $420,000 and a secured claim of $100,000 Farber attached two charts:[36]

(i) One recorded payments by Annopol to SGW from its TD Bank account between June 27, 2000 and March 24, 2005, totaling $152,600;

(ii) The other recorded transactions between Annopol and SGW from an HSBC account showing net payments to SGW of $367,400 between September 13, 2005 and December 4, 2008.

78 In its January 18, 2011 Report Farber stated that SGW owed Annopol no less than $519,600. It continued:

> Farber acknowledges that only $100,000, plus costs and interest, of the obligations owing by SG Waterloo to Annopol will be secured by the Annopol $100,000 Charge and the advances in excess of $100,000 will be an unsecured claim against SG Waterloo.

79 By the time of its June 25, 2012 Report, Farber was stating that between 2000 and 2008 Annopol "appears to have advanced no less than $557,600" to SGW. Farber explained the increase in this amount since the filing of the 2011 proofs of claim as the result of securing additional SGW records from the execution of entry orders and search warrants. Farber reported that based on its review of these additional records, it had determined that between January 27, 2000 and March 24, 2005, Annopol had advanced no less than $190,200 to SGW.[37] Virtually all of the cheques from Annopol, as well as many of the SGW bank deposit slips, contained the notation, "Loan Advance". Farber also adduced a few cheques from SGW to Annopol noted as "partial loan repmt".

Financial statements

80 The SGW unaudited, notice to reader financial statements for the years ended March 31, 2005, 2006 and 2008 did not show the Annopol charges as a liability of SGW. The company's unaudited financial statements for the year ended March 31, 2001 only showed a mortgage payable of $375,000 — i.e. the Bolliger VTB.

81 Annopol's unaudited balance sheet as at February 29, 2008, did record, as an asset, a loan to SGW in the amount of $200,460.00.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Other documents

82 Farber was not able to locate any loan agreements between Annopol and SGW. However, as noted, the October 18, 2000 SGW director's resolution did contemplate future indebtedness arising between SGW and Annopol.

83 In late 2005, when Kimel was trying to entice Perelmuter (of Montor) into lending money to his companies, he wrote a November 30, 2005 email in which he stated the only mortgages registered against 105 University were those held by Community Trust Company; he made no mention of Annopol's mortgages. But, a few days later, on December 1, 2005, in an email to his lawyer, Kimel did refer to an existing third mortgage in favour of Annopol which would have to be postponed to Montor's proposed $500,000 mortgage.

84 The June 28, 2010 statement of affairs for SGW signed by Kimel in the bankruptcy listed Annopol as an unsecured creditor for the amount of $600,000 on the basis that Annopol held security of $750,000, the estimated value of which was only $150,000.

85 Finally, it must be recalled that Farber issued an application for bankruptcy against SGW on April 30, 2009 and obtained a bankruptcy order on June 28, 2010. Farber did not adduce evidence of the net amount owing by SGW to Annopol, if any, on either of those dates.

86 On the cross-examination of Martin Cyr, the trustee at Farber who had ultimate carriage of the SGW bankruptcy file, counsel for Goldfinger sought to elicit information about efforts by Farber to ascertain the amounts owing by SGW to Annopol under each mortgage. Those efforts initially were met with refusals, as disclosed by the following exchanges on the transcript:

> Q. 40: What steps have you or anyone on behalf of Farber's taken to determine how much, if anything, was advanced under that $750,000.00 Annopol mortgage that was registered in April of 2000?
>
> A. What steps were taken as of is this just a general statement or as of the date of the affidavit?
>
> Q. 41: Let's start with as of the date of the affidavit, which is June 25, 2010.
>
> A. As I said, I don't have an answer to that.
>
> Q. 42: Can you undertake to find out and let me know, please?
>
> MR. SHEA: No. This is just going down a path. I would like you to focus on the issue of conflict, as per the order.
>
> Q. 43: And to this date can you tell me what steps, if any, Farber has taken to determine how much, if anything, was advanced pursuant to or in consideration of that mortgage security for $750,000.00?
>
> MR. SHEA: Don't answer the question.
>
> Q. 44 And can you undertake to tell me what steps Farber has taken to determine whether anything was advanced under the $100,000.00 Annopol mortgage?

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

MR. SHEA: Don't answer the question.[38]

87 By way of summary, the evidence about the state of accounts as between SGW and Annopol filed in support of Annopol's proofs of claim disclosed the following:

(i) Annopol did not advance any funds at the time SGW granted it the Annopol $750K Charge;

(ii) Annopol did not advance any funds at the time SGW granted it the Annopol $100K Charge;

(iii) SGW's financial statements for the years ended March 31, 2005, 2006 and 2008 did not record the Annopol charges as corporate liabilities;

(iv) Bank account records disclosed net payments from Annopol to SGW of: (i) $190,200 for the period June 27, 2000 through to March 24, 2005, and (ii) $367,400 between September 13, 2005 and December 4, 2008;

(v) Annopol's unaudited balance sheet as of February 29, 2008 recorded a loan to SGW in the amount of $200,460; and,

(vi) Notwithstanding that SGW and Annopol continued to operate until the dates of their bankruptcies (June 28, 2010 and May 27, 2010 respectively) - albeit SGW operated under receivership from December 1, 2008 until May, 2010 - Farber did not adduce evidence of the state of the inter-corporate indebtedness between SGW and Annopol as at the date of SGW's bankruptcy.

88 Before considering each of the proofs of claim filed by Annopol, it is necessary to deal with the main argument advanced by Goldfinger that no indebtedness arose during the course of dealings between SGW and Annopol.

E. The financial characterization of the dealings between SGW and Annopol

89 In its Reports Farber concluded that Annopol had acted as a kind of "bank" for the Summit Glen group of companies, including SGW, and had provided, in effect, an operating line of credit to SGW.

90 In response, Goldfinger submitted that the dealings between SGW and Annopol did not give rise to any indebtedness between the companies. Goldfinger advanced two main arguments: (i) a lack of documentation argument, and (ii) an "Annopol as mere conduit" argument.

The lack of documentation argument

91 Goldfinger submitted that Farber had refused his request to provide copies of all Annopol documents and, as a result, no Annopol bank records were placed into evidence save for one from December, 2005. This led Goldfinger to assert that Farber had not proved its "bald statements of loans from Annopol to SGW" and, therefore, Farber's claims with respect to the $850,000 of Annopol mortgages should be disallowed.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

92 I have reviewed the extensive materials filed by the parties on the issue of documentary production. While it would be easy to conclude that both parties demonstrated unreasonableness in the various positions they took prior to the hearing about the scope and terms concerning the production of documents, I am satisfied that ultimately Farber provided appropriate access to all relevant documents to counsel for Goldfinger.

93 Moreover, this argument was undermined by evidence which Goldfinger, himself, filed in his Responding Motion Record, Tab 14 of which contained a copy of Annopol's balance sheet and trial balance as at February 29, 2008. It is not clear who at, or who on behalf of, Annopol prepared those documents, although Goldfinger, relying on hearsay from Kimel, deposed that the company's bookkeeper or accountant, Perelmuter, had prepared them. Significantly, and not surprisingly, the balance sheet and trial balance recorded as assets "loans" made by Annopol to many other Summit Glen Companies, including SGW. Those internal Annopol documents strongly suggested that Annopol treated inter-company advances to SGW as creating loan assets.

The "Annopol as mere conduit" argument

94 Goldfinger also relied on evidence given by Kimel, both before and at trial, that Annopol had operated merely as a "conduit" for funds. As a conduit, he argued, no debtor/creditor relationship existed between SGW and Annopol in respect of any of the funds which flowed between the two companies.

95 At trial, in response to questions posed by counsel for Goldfinger, Kimel explained how Annopol had operated:

> Q. Now, we're going to talk about the fact that various moneys flowed through that company. What was the purpose behind using Annopol for your various business endeavours?
>
> A. Well, it became a conduit, a pass-through company. I was advised by the accountants that, uh, I was using at the time, that because I wasn't really certain of, uh, whether some of the entities that I was operating would have profits or losses, that it would be best to have a neutral entity through which I could register various advances or various writeoffs, then apply, where I felt, or they felt, it made sense from a tax perspective to then take losses or revenues into account.

. . .

> Q. So you used Annopol as the vehicle, um, for flowing that money through so that at the end of the year, you or your accountants could determine which company to take the expense under, is that right?
>
> A. Absolutely correct, yes.[39]

96 Notwithstanding that Annopol had received money from third parties and then disbursed funds to various Kimel companies, including SGW, at trial Kimel took the position that none of the flows of money between Annopol and SGW constituted loans:

> Q. Okay. Now, I'm going to read you another sentence from paragraph fifteen where my friend says, "Annopol also carried on business providing what were akin to operating lines of credit for various of the S.G. companies

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(that's Summit Glen) including Summit Glen Waterloo." So, the suggestion is that Annopol also carried on business providing operating lines of credit or something akin to that, is there anything to that statement, were operating lines credit provided by Annopol to anybody, or anything like an operating line of credit?

A. I don't believe that's, uh, that's a correct reflection of what Annopol was doing, no. Annopol had no revenues of it, of its own generated, no interest or administration, or brokerage fees of any kind, uh, it, uh, never took profits on anything. It, basically, raised money, or when I say raised, money was given to it from either other individuals or other companies to basically flow through it to some other entity. But, uh, a line of credit to me implies that it would've been charging interest or a fee for its services and none of that ever happened.

. . .

Q. And, similarly, money from other people that you raised in various arrangements, or money from financial institutions, were deposited to Annopol at you direction.

A. Yes.

Q. And that's so you could flow the money through Annopol to wherever you needed it.

A. That's correct.

Q. And when you flowed the money from Annopol to these other companies, such as Summit Glen Waterloo, Summit Glen Brantford, Summit Glen Trayvan, or any of the other companies, you never expected any of these companies to pay any of the money back to Annopol, correct?

A. That is correct.

Q. So, when my friend comes along and he says that loans were made by Annopol to others, that is incorrect agreed?

A. I agree.[40]

97 Kimel concluded on this point by testifying:

Q. And, also, am I right that moneys may have flowed from one company to another, but none of those moneys were ever a repayment of a loan?

A. Yes, you're right.

Q. And is it fair to say that you never expected any moneys that were advanced by Annopol, or Summit Glen Group to be repaid.

A. That's correct.

. . .

Q. And, if there are promissory notes given by Annopol, that was done as a mere convenience to paper the transaction?

A. Yes.[41]

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

98 For several reasons I do not accept Kimel's assertion that Annopol generally operated as a mere conduit of funds in the sense that no inter-company liabilities arose between Annopol and other SG companies, including SGW, with the result that at the date of its bankruptcy SGW could not be indebted to Annopol. First, Kimel's evidence revealed that he lacked honesty in his financial dealings with others, a characteristic which diminished the overall credibility of his evidence. For example, Kimel admitted during his testimony that he had misled lenders in the past, such as misleading Community Trust Company when attempting to arrange the take-out financing for 105 University:

> Q. Now, we've seen in the record, can't put my hands on it as we speak, a letter you wrote to Community Trust in advance of the loan suggesting that you put $400,000 into the property, remember that?
>
> A. Vaguely.
>
> Q. And, it's fair to say you never put the $400,000 in, that was a letter that you wrote just in an attempt to secure the financing?
>
> A. Yes, that's correct.[42]

99 Kimel also admitted to providing false statements of net worth:

> Q. And, the next thing I want to do is take you to tab 'H', and that's a statement of personal net worth dated August 29, 2006, did you prepare this?
>
> A. Yes, I did.
>
> Q. And two-thirds of the way down where it says equity incorporation net of debt, you show Summit Glen Group of Companies, and you describe it as parent umbrella of various subsidiaries, that wasn't the true statement, was it?
>
> A. No, it was just something I put, uh, for matter of convenience.
>
> Q. And you put a value of thirty-two million dollars on the Summit Glen Group of Companies, that wasn't true, was it?
>
> A. No.
>
> Q. And, similarly, over on the next page, at item 'C', you have Annopol Holdings Limited and it says, "fifty per cent joint venture partner in a number of commercial industrial properties located in Southwestern Ontario that you values at eight million dollars, that was completely untrue, correct?
>
> A. Yes.
>
> Q. And, if you go down below, it says Annopol U.S Holdings Corporation also fifty per cent owner of various properties that you valued at fourteen million dollars, that was also untrue.
>
> A. It was untrue.
>
> Q. And, similarly, the family trust that you referred to, not true, correct?
>
> A. They were not true.
>
> Q. And you put together this statement for the purpose of getting financing from financial institutions and, basically, you misrepresented the state of the various assets, right?

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

A. Yes.[43]

100 Second, Kimel denied the obvious by taking the position that notwithstanding the bank statements for his companies recorded certain transactions as loans from one Summit Glen company to another, those notations meant nothing:

Q. And, where it says, just, I know we might be beating, flogging a horse but, where it says in the bank statement, loan to this company or that company, they weren't really loans to that company, you were just using Annopol as a conduit, so you get the five hundred thousand from Montor and you distribute it wherever you need it and you never expected any of those companies to pay it back, right?

A. That's correct.[44]

Similarly, in respect of the records of SGG, Kimel testified:

Q. Now, I then want to take you to my friend's document brief at tab number one, or volume number one, I should say, tab number six, and you'll see here there's a series of cheques all drawn on the Summit Glen Group of Companies' account at TD Bank, you see that?

A. Yes, I do.

Q. And, pretty well every one of them, I think every one of them, has a reference saying loan advance, can you tell the Court whether or not these really were loan advances?

A. Well, they weren't loan advances, but the reason that I noted them as that were, was exactly what I, I think explained to you before, that all of these moneys were flowing through either Summit Glen Group or Annopol, and were being noted as, in this instance for example, loan advances, so that at some point in the future, they could be, they would have attribution against some other entity, uh, for purposes of writing them off or utilizing them.[45]

101 Third, Kimel acknowledged that the evidence he was giving at trial was inconsistent with the documentary record, but he was doing so in order to support Goldfinger's position at trial:

Q. Can you tell the Court why you have since provided information, documentation, and assistance to my client?

A. Previously I, um, thought that I had, uh, assets to protect, properties and family to protect and, uh, took steps that I thought were necessary to do that. And in the intervening period, I no longer have any properties or assets, I'm bankrupt, my business has been basically destroyed, my family life has been destroyed, and, uh, frankly I no longer have anything to lose. And, uh, at this point, I think it's only appropriate that I do what, uh, is correct to try to make amends, uh, and, um, assist in any way possible that I can to verify and, uh, point out what my intentions and what my thoughts were at the different points in time that you've asked me about in terms of, uh, documentation and such.[46]

102 Fourth, Kimel's favourable evidence in response to questions posed by Goldfinger's counsel describing Annopol as a mere conduit cannot be reconciled with answers he then gave at trial in response to questions posed by Farber's counsel. When questioned on the issue of funds advanced by individual third party investors to Annopol, Kimel took the position that

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Annopol owed those persons the monies advanced, hardly a position consistent with Goldfinger's theory of "Annopol as a mere conduit":

> Q. So, you don't know if Annopol, sorry, explain that to me. You don't know if Annopol borrowed money from them, but they advanced money to Annopol. I'm afraid that you're going to have to explain that to me. This is a list of debts, all sources?
>
> A. Yes.
>
> Q. So, who owed Mardarowicz [a third party investor] one point six million?
>
> A. The money was advanced to Annopol.
>
> Q. So, did Annopol owe him one point six million?
>
> A. Yes.
>
> Q. Annopol owed Jack Mardarowicz one point six million?
>
> A. Yes.
>
> Q. Fruma. Who owed Fruma the half a million dollars?
>
> A. Well, the moneys were advanced to Annopol but then they went through Annopol to other entities.
>
> Q. So when you say they went through Annopol to other entities, this is Mr. Davis's conduit argument.
>
> A. It's not an argument, it's, it's a fact.
>
> Q. So, we'll get to that in a moment, but your position is, then, that the funds were advanced by Fruma Srubiski to Annopol, but Annopol didn't owe him, or her, any money back?
>
> A. Well, they all understood that the money was going out of Annopol to other companies for other purposes.
>
> Q. Who owed them the obligation to pay the money back?
>
> A. They all asked for something from Annopol, which I gave them.
>
> Q. So, Annopol owed them the money back then.
>
> A. Yes.[47]

103 Fifth, Kimel testified that the inter-corporate accounting of funds passing between the various SG group companies usually recorded advances made by one company to another as loans:

> Q. So, how did you keep track of all of that?
>
> A. Well, internal bookkeeping.
>
> Q. How would you record, did you record it as loans?
>
> A. Yes, typically, again, based on accountant, uh, advice, every cheque I would write 'loan advance' or something

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

of that nature because, uh, in that fashion at the time that we were doing statements we would determine where we could attribute. If a company had profits and needed write-offs, it allowed us to utilize them where we, we could best utilize them.

. . .

Q. So, the statements would show an interest, so the statements for who, let's start with the statements for who. So, let's say Annopol was providing funds to Summit Glen Waterloo, cash would go across to Summit Glen Waterloo marked as a loan on the cheque, correct?

A. Yes.

Q. And then when you prepared your statements you would show interest paid from Waterloo to Annopol?

A. No.

Q. Okay, so how would you do it then?

A. We would, uh show the advance on, uh, well whoever it came from or whatever it came from, so that, uh, even though Annopol was the company making the advance, if the money had come through, uh, Trayvan or it had come through Raleigh Street, or it had come through some other entity, then that was the entity that we attributed the expense against, or in favour of.

Q. An expense. So, you would show on Trayvan's financial statement an expense that Summit Glen Waterloo had incurred?

A. No, we would show an outstanding loan, or an outstanding debt.

Q. And I still don't understand how that allows you, how an outstanding debt allows you to sop up an expense, oh, sorry, sop up profit.

A. By writing if off as uncollectable.

Q. So, but you would collect it sometimes?

A. No. We never expected, I never expected that any of these were loans that would ever be repaid, uh, these were advances that, uh, were used to support various companies at different points in their existence but it was never expected or anticipated that the loans would be repaid.[48]

104 Sixth, Goldfinger's "Annopol as a mere conduit" position also was undermined by the way in which he treated his own advances to Kimel and his companies over the years. In a January 9, 2012 letter Goldfinger's accountant described how the advances made by Goldfinger were treated on the financial statements of his companies, Goldfinger Jazwary Diagnostic Services Inc. and 2048754 Ontario Inc.: the amount of $50 was shown as share capital in each of the companies, including Annopol, and the rest of the advances were recorded as shareholder loans, including shareholder *loans* of $2.057 million to Annopol.

105 In a similar vein, evidence was filed regarding communications from Annopol to individual investors which certainly would lead the investor to believe that Annopol had placed the funds in an investment of a fixed duration on his behalf, and Annopol provided the investors with monthly cheques on its account to pay interest to the investor.[49] Also, Annopol issued T-5s to some investors for interest paid on their loans during a year. Kimel, in a February 27, 2007 letter on Annopol letterhead to Perelmuter's accounting firm, enclosed a list of people to whom Annopol had paid interest over the course of the year.[50]

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

106 Indeed, Kimel's evidence, when taken as a whole, revealed that the SG companies to which third party investors had advanced funds, including Annopol, were liable to those investors for the repayment of the invested funds, with the ability of that company to repay its investors dependent upon the performance of real estate developments undertaken by other SG companies in which the third party funds were invested. The following testimony by Kimel at trial encapsulated the point:

> Q. So, if the loans would never be repaid, how would, for example, let's use Annopol for the example since it's the company we're dealing with, *Annopol borrows money from Jack Mardarowicz, who you've agreed Annopol owed one point six million to, correct?*
>
> A. *Yes.*
>
> Q. So, Annopol takes Mr. Mardarowicz's money, we'll get to how some of that money was used in a moment, and transfers it to Summit Glen Waterloo reflected as a loan, correct?
>
> A. Well, his money wouldn't have gone necessarily to Summit Glen Waterloo.
>
> Q. Well let's just...
>
> A. Assuming, yeah.
>
> Q. Let's assume it did. Pick one of them. I'm just trying to do a hypothetical. So, the money goes to Summit Glen Waterloo. *Summit Glen Waterloo is never obliged to pay that money back, how would Annopol ever pay back Mr. Mardarowicz?*
>
> A. *Through the development and sale of Summit Glen Waterloo.*[51]

107 Seventh, Annopol's HSBC bank statements recorded "loans" to SGW from Annopol.[52]

108 Finally, on his examination Perelmuter, Annopol's former accountant, was not prepared to agree that Annopol was a mere conduit: "What you're saying is conceivable but not necessarily this is the whole truth about Annopol because he may have been involved in other deals".[53]

109 Whether the financial dealings between two entities are intended to create a debtor/creditor relationship is a matter to be determined from the specific facts of a particular case. Counsel for Goldfinger drew my attention to the decision of Power J. in *Coast Operations of Canada Ltd. (Trustee of) v. Ottawa Credit Exchange Ltd.*,[54] in which the court concluded that a flow of funds between two companies did not create a debtor/creditor relationship. In that case the trial judge accepted such an explanation for "questionable book entries", and the Court of Appeal did not interfere with that finding of fact. Such were the facts in that case. In the present case, however, I conclude that the evidence overwhelmingly demonstrated that Kimel operated the Summit Glen group of companies, including Annopol and SGW, on the basis that funds provided by a third party investor to one company, such as Annopol, would give rise to a liability from Annopol to that investor. Annopol, in turn, would advance those third party funds to another Summit Glen company, such as SGW, to finance various real estate developments, and that advance would give rise to a liability from the recipient company, such as SGW, to Annopol.

110 In light of that finding, I need not deal with the claim based on unjust enrichment advanced by Farber in its Factum.[55]

F. Analysis

F.1 Annopol's First Proof of Claim: $100,000 Annopol Charge and unsecured claim

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

111 Annopol's First Proof of Claim asserted an unsecured claim of $420,000 and a secured claim of $100,000, for a total claim of $520,000.

112 As to the secured claim, although Annopol did not advance funds to SGW at the time of the granting and registration of the Annopol $100K Charge, by its terms that charge granted security in respect of future indebtedness — "security for the payment of all indebtedness of the Company to the Mortgagee relating to loans to Summit Glen Waterloo/2000 Developments Inc." The SGW director's resolution of October 18, 2000 also expressed an intention that the charge would secure "present and future indebtedness".

113 The question then becomes, at the date of SGW's bankruptcy, June 28, 2010, what amount was due and owing from SGW to Annopol? Or, put another way, has Farber, as trustee of Annopol, adduced relevant and probative evidence from which a valid claim can be reasonably inferred — i.e. that Annopol, as a creditor of SGW, had, at the date of bankruptcy, the right to receive and enforce payment of the amount claimed?

114 Farber, as trustee of Annopol, did not file in support of its claim a reconciliation of the accounts between SGW and Annopol as at the date of bankruptcy. Instead, Farber has asked this Court to draw the inference that because bank account records showed net payments from Annopol to SGW during two periods of time ($190,200 from June 27, 2000 until March 24, 2005, and $367,400 from September 13, 2005 until December 4, 2008), the amount due from SGW to Annopol at the date of bankruptcy was the aggregate of the two amounts, i.e. $557,600.

115 The method used by Farber to calculate Annopol's claim suffers from several obvious difficulties. First, a gap exists in the bank account analysis, with several months unaccounted for — March 25 through to September 12, 2005. Second, the analysis stopped at December 4, 2008, some year and one-half prior to the date of bankruptcy. Third, while the unaudited financial statements of Annopol suffered from the fact that they were based on information provided by Kimel, a person of very low credibility, the company's unaudited balance sheet as at February 29, 2008 recorded a liability due from SGW of only $200,460. Also, the unaudited financial statements of SGW placed into evidence did not record the Annopol charges as a liability, an unusual omission given the evidence that at the time of their creation Kimel was attempting to preserve his family's "equity" in 105 University. If nothing else, Kimel was consistent in his drive to protect his own self-interest, so one would have expected some recognition of charges in favour of his related companies on SGW's financial statements had he thought the charges truly secured some amount of indebtedness. Finally, at least in respect of the unsecured portion of Annopol's claim, it relies on inter-company transactions which took place more than two years prior to the date of bankruptcy, raising questions about how much of the claim would not be sustainable because it was statute-barred at the date of bankruptcy.[56]

116 On the other side of the evidentiary ledger, one must recognize that Farber encountered significant difficulties in obtaining the books and records of Annopol and SGW. Further, although Farber's reconciliation of the amounts due from SGW to Annopol stopped a year and one-half prior to the date of SGW's bankruptcy, the evidence disclosed that the affairs of SGW did not improve after December 4, 2008, so it was most unlikely that SGW would have been in the position to reduce its indebtedness to Annopol between then and the date of its bankruptcy.

117 In light of these conflicting issues regarding the evidence adduced on behalf of Annopol's First Proof of Claim, I conclude that, when taken as a whole, the evidence supports a finding that at the date of SGW's bankruptcy it owed Annopol at least $100,000 and that indebtedness was secured by the Annopol $100K Charge. I allow that portion of the First Proof of

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Claim, with interest to the date of payment in accordance with the terms of the loan.[57]

118 As to the amount of any unsecured claim, the Court is hampered in this case by the absence of any analysis from a trustee in bankruptcy whose only interest lay with the estate against which the claim was made. Farber could not play that role because of the multiple hats it wore. In the ordinary course of the administration of an estate a trustee would consider whether all or part of any claim made against the estate was statute-barred. The analysis filed by Farber in support of this part of Annopol's claim disclosed that in the two years prior to the date of bankruptcy (June 28, 2008 - June 28, 2010), Annopol paid SGW a net amount of $44,600. Most of the unsecured claim, therefore, relates to payments made more than two years prior to the date of bankruptcy. At trial only cursory submissions were made regarding the limitations issue, but because the Court is acting in this case as a reviewer of first instance of these claims, I have concluded that the parties must make further submissions on the effect, if any, of any limitations period on this part of Annopol's claim. Accordingly, I require submissions from the parties on the issue of whether all or part of Annopol's unsecured claim is statute-barred:

(i) Farber may serve and file brief written submissions, together with any authorities, no later than November 30, 2013;

(ii) Goldfinger may serve and file brief responding written submissions, together with authorities, no later than January 15, 2014; and,

(iii) Farber may file brief reply submissions no later than January 22, 2014.

F.2 Annopol's Second Proof of Claim: the Annopol $750K Charge

119 I find that at the time SGW granted the Annopol $750K Charge no funds were advanced by Annopol to SGW.

120 The language used in that charge, when read in the light of the language used in the contemporaneous authorizing SGW director's resolution, leads to the conclusion that the charge was intended to secure an advance of funds made at that time, not to secure any future indebtedness of SGW to Annopol. On this point, the language in the Annopol $750K Charge differed from that used in the Annopol $100K Charge and the May 6, 2005 Annopol Charge granted by SG Bridge, discussed later in these Reasons, which stipulated that the charges stood as security for both present and future indebtedness.

121 It follows that since Annopol did not advance any funds to SGW at the time the latter granted it the Annopol $750K Charge, the charge, as registered, does not secure any indebtedness of SGW to Annopol.

122 Farber pointed to a February 21/22, 2005 email exchange between Kimel and Eden Cheng at HSBC as evidence that Kimel understood that the Annopol $750K Charge secured subsequent advances made by Annopol to SGW. I do not accept that submission. Cheng, in his email to Kimel, wrote: "I was asking you to fax to me anything you have regarding the CAD750M mortgage receivable you expect to receive in end-March..." On their faces, neither email referred to 105 University or SGW; the authors were discussing 41 Valleyview, Henry Street and 27 Bridge Street. SG Bridge had granted Annopol a $750,000 charge. In light of the absence in the mails of any reference to 105 University, I cannot conclude that this email exchange had anything to do with that Property.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

123 In its evidence filed in support of this Second Proof of Claim, Farber stated that it used the figure of $750,000 because it "was the face amount of the charge/mortgage". Absent proof that funds were advanced, the mere registration of the charge did not create an indebtedness from SGW to Annopol. As previously noted, the Schedule to the charge contained a standard "no obligation to advance" clause. In the event, Annopol made no advance secured by the Annopol $750K Charge. I therefore disallow this claim by Farber, as trustee of Annopol.

F.3 Summary of conclusion on Annopol's claims

124 By way of summary, I allow the claim of Farber, as trustee of Annopol, for a secured claim of $100,000 secured by the Annopol $100K Charge, with interest to the date of payment, and call for further submissions on the unsecured portion of Annopol's First Proof of Claim. I disallow the claim of Farber, as trustee of Annopol, for a secured claim in respect of the Annopol $750K Charge.

V. Summit Glen Waterloo: Claim by Farber as the trustee of Summit Glen Group of Companies Inc. ("SGG")

125 SGG was the management company for the entire Summit Glen group of companies, including Annopol and SGW. Starting in 2005, SGG had an operating line of credit with HSBC.

126 Farber, in its capacity as trustee of SGG, filed in the SGW bankruptcy a proof of claim "as of July 7, 2012" making an unsecured claim for $578,336. In support of its claim Farber simply appended extracts from its June 25, 2012 Report. Farber later filed a further proof of claim, for the same amount, dated July 9, 2012.

127 In its June 25, 2012 Report, Farber, as trustee of SGG, made its first reference to a possible *unsecured claim* against SGW on two bases: (i) a debt claim in the amount of $16,450 in respect of inter-company loans made by SGG to SGW to fund operating expenses for 105 University; and, (ii) a claim based on unjust enrichment in the amount of $565,998 for payments made by SGG for the benefit of SGW relating to costs concerning the re-development of 105 University.

128 183 and Goldfinger took the position that SGW did not owe any money to SGG because SGG had not carried on any business, but merely had acted as a "conduit" for money loaned by third parties to SGW.

A. SGG's Debt claim

129 Based on its review of cheques written by SGG, Farber stated that between May, 2003 and May, 2004, SGG had made direct advances to SGW totaling $16,450. Farber could not locate any loan agreements between SGG and SGW, nor did SGW grant SGG a charge over 105 University.

130 At trial Kimel admitted that SGG wrote cheques to SGW marked as loan advances.[58] He also agreed that in respect of the HSBC operating line obtained by SGG, if one of the SG group of companies sold a property, the proceeds would work their way back to HSBC through SGG.[59]

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

131 According to Farber's investigation, unlike Annopol, SGG did not receive significant advances from persons other than Goldfinger and Annopol. SGG did use an operating line of credit with HSBC under which it borrowed monies. HSBC has filed a $885,375 unsecured claim against SGG for amounts owing under that operating line, but HSBC has not filed a claim against SGW.

132 Goldfinger took the position that SGG was used as a conduit in the same manner as Annopol and, therefore, no debtor/creditor relationship ever arose between SGW and SGG. I reject Goldfinger's conduit argument for the reasons given above in rejecting his similar claim regarding Annopol.

133 Although that was the only objection raised by Goldfinger, the Court once again is hampered in the case of this proof of claim by the absence of any analysis from a trustee in bankruptcy whose only interests relate to the estate against which the claim is made. As mentioned earlier, in the ordinary course of the administration of an estate a trustee would consider whether all or part of any claim made against the estate was statute-barred. Farber has remained silent on that point. This particular claim for $16,500 raises obvious questions about the limitations period. According to the claimant, those inter-company payments were made in 2003 and 2004. Farber did not adduce any evidence that repayment of those amounts was due at a time other than their advance. SGW became bankrupt in June, 2010. Given that chronology, one could ask whether claims dating back to the period 2003 and 2004 might be statute-barred. Farber adduced no evidence to support a late discoverability argument in respect of this part of SGG's claim. I do not think that a court, when asked to consider a proof of claim in the first instance, can avoid asking the basic question of whether the claim might be statute-barred. Accordingly, before finally determining Farber's claim, as trustee of SGG, for $16,500, I require submissions from the parties on the issue of whether all or part of that claim is statute-barred:

(iv) Farber may serve and file brief written submissions, together with any authorities, no later than November 30, 2013;

(v) Goldfinger may serve and file brief responding written submissions, together with authorities, no later than January 15, 2014; and,

(vi) Farber may file brief reply submissions no later than January 22, 2014.

B. SGG's unjust enrichment claim

B.1 The positions of the parties and the applicable law

134 In its June 25, 2012 Report Farber stated that SGG made payments totaling $565,998 to third parties, such as architects, engineering firms and lawyers, who had provided services for the re-development of 105 University. Farber grounds its claim, as trustee of SGG, against SGW in unjust enrichment.[60]

135 The cause of action for unjust enrichment has three elements: (i) an enrichment of the defendant; (ii) a corresponding deprivation of the plaintiff; and, (iii) an absence of juristic reason for the enrichment.[61] The first element employs a "straightforward economic approach". An enrichment occurs when the plaintiff confers a tangible benefit on the defendant, such as the payment of money, or a negative benefit such as sparing the defendant an expense it would otherwise have incurred.[62] In addressing the third element — the absence of juristic reason for the enrichment — the Supreme Court of Canada, in *Garland v. Consumers' Gas Co.*, laid down the following analytical approach:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> [I]n my view, the proper approach to the juristic reason analysis is in two parts. First, the plaintiff must show that no juristic reason from an established category exists to deny recovery... The established categories that can constitute juristic reasons include a contract..., a disposition of law..., a donative intent..., and other valid common law, equitable or statutory obligations... If there is no juristic reason from an established category, then the plaintiff has made out a *prima facie* case under the juristic reason component of the analysis.
>
> The *prima facie* case is rebuttable, however, where the defendant can show that there is another reason to deny recovery. As a result, there is a *de facto* burden of proof placed on the defendant to show the reason why the enrichment should be retained. This stage of the analysis thus provides for a category of residual defence in which courts can look to all of the circumstances of the transaction in order to determine whether there is another reason to deny recovery.
>
> As part of the defendant's attempt to rebut, courts should have regard to two factors: the reasonable expectations of the parties, and public policy considerations. It may be that when these factors are considered, the court will find that a new category of juristic reason is established. In other cases, a consideration of these factors will suggest that there was a juristic reason in the particular circumstances of a case which does not give rise to a new category of juristic reason that should be applied in other factual circumstances. In a third group of cases, a consideration of these factors will yield a determination that there was no juristic reason for the enrichment. In the latter cases, recovery should be allowed. The point here is that this area is an evolving one and that further cases will add additional refinements and developments.[63]

136 Again, as in the case of the claim for the $16,500 loan by SGG, Goldfinger's objection to this claim was brief. He contended that SGG was used as a conduit in the same manner as Annopol:

> Accordingly, it never intended, or was capable of forming a debtor/creditor relationship with SG Waterloo.
>
> For the same reasons set out with respect to Annopol's claim, the claim of SG Group should be denied.[64]

Goldfinger raised no other objection to this claim.

B.2 Analysis

137 Having reviewed the description of SGG's claim in Farber's June 25, 2012 Report, together with the supporting documents filed in Volume 1 of its Brief of Documents of the same date, I am not satisfied that Farber has filed sufficient particulars regarding parts of this claim. Specifically:

> (i) as to the monies SGG paid to an architect, Joe Somfay Architects, although Farber reported that that firm was retained for the purpose of developing 105 University, all Farber filed in evidence was a summary of invoices, credit notes and payments prepared by Somfay. That summary was entitled, "Summit Glen Developments", not, as one might expect, "Summit Glen Group" if the payor were SGG. No invoices were produced for examination to ensure they related to work on 105 University nor was adequate evidence adduced to establish who the payor of any invoice was. The invoices totaled $346,029.13 and dated from 2002 until May 30, 2007;
>
> (ii) in respect of Courtland Engineering ($1,588.95 invoice dated May 10, 2004) and GSP Group ($10,406.51 of invoices from March 19, 2004 through to September 10, 2008), Farber did not file adequate documentation to support those claims, specifically copies of the invoices and cheques. The same was true for MTE's invoices. It was incumbent on Farber, as trustee of SGG, to put together a claim which complied with *BIA* s. 124(4) containing not only a statement of account showing the particulars of the claim, but "the vouchers or other evidence, if any, by which it can be substantiated". Farber, as trustee of SGG, did not provide the latter information;

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(iii) in respect of the Stikeman Elliott law firm, the Trustee adduced invoices rendered by that firm between November 18, 2004 and May 28, 2007. The client to whom those invoices were sent was Summit Glen Developments Limited, not SGG. It also adduced cheques payable to that firm between October 4, 2002 and April 30, 2005. Of those cheques, most were made by SGG; one was made by Summit Glen Trayvan Holdings Inc. There was no evidence of payment of the three invoices rendered after May 19, 2005;

(iv) Farber reported that the records of SGW disclosed that payments were made by SGG to Sze Straka who performed engineering services in respect of 105 University. The cheque stubs filed by the Trustee did not identify on their face that SGG had paid invoices rendered to SGW or for work performed for SGW, nor were the relevant invoices filed;[65]

(v) invoices from Minden Gross to SGG from February 27, 2007 through to November 27, 2007 were filed. On their face they do not refer clearly to work performed for or in respect of SGW or for 105 University; they simply were headed, "Housing Initiative". No evidence was adduced to explain the work recorded on the invoices. Those invoices appear to have been subject to a May 1, 2009 Order for Assessment. In its Report Farber asserted that SGG paid those invoices, but no evidence to support that statement was filed; and,

(vi) Farber reported that SGW's HST records indicated that SGG had paid an additional $62,943 in operating and other day-to-day operating expenses on behalf of SGW between the period May 16, 2003 and December 31, 2008, with most pre-dating 2007. No documentation was filed by Farber to support those assertions.

138 In sum, I am not satisfied that Farber, as trustee of SGG, has filed sufficient information in support of its claim as required by *BIA* s. 124(4). However, as will be seen from my treatment below of 183's claim under the CTC $50,000 Charge, I plan to give 183 an opportunity to file further evidence in support of its claim pursuant to *BIA* s. 135(1). Fairness dictates that Farber be given a similar opportunity. I give both parties these further opportunities in an effort to bring finality to the dispute by affording both the chance to deal with the substantive issues concerning their claims. Accordingly, I make the following orders:

(i) Farber shall provide Goldfinger with any evidence dealing with the deficiencies in its unjust enrichment claim which I have identified above no later than November 30, 2013 and file with the Court, to my attention, a report dealing with that issue;

(ii) Goldfinger shall file any further submissions on this issue no later than January 15, 2014;

(iii) I shall then release supplementary reasons deciding Farber's claim by February 14, 2014.

139 Also, as already noted, SGW went into bankruptcy on June 28, 2010. SGG made the payments claimed more than two years prior to the bankruptcy of SGW. One could ask whether claims dating back to that period would be statute-barred. Farber did not adduce evidence to explain why the discoverability date for those payments should be other than the time the payments were made. Before deciding that point, I will give the parties an opportunity to make brief written submissions on the point:

(vii) Farber may serve and file brief written submissions, together with any authorities, no later than November 30, 2013;

(viii) Goldfinger may serve and file brief responding written submissions, together with authorities, no later than January 15, 2014; and,

(ix) Farber may file brief reply submissions no later than January 22, 2013.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

VI. Summit Glen Waterloo: Claim by Goldfinger's company, 1830994 Ontario Ltd., based on the assignment of the CTC mortgages

A. Evidence

140 SGW acquired 105 University from Bolliger Holdings Corporation in 2000 for $950,000. Goldfinger advanced the required cash; Bolliger took back a $450,000 VTB with a term of six months, maturing on September 30, 2000. SGW did not pay out the VTB mortgage at that time.

141 Bolliger issued a notice of power of sale on January 5, 2001. To deal with the Bolliger VTB, two types of financing were arranged. First, SGW obtained $50,000 in direct financing from Community Trust Company ("CTC") secured by a charge against 105 University. Second, Goldfinger and Kimel each borrowed $250,000 from CTC and signed promissory notes in its favour. SGW guaranteed those personal loans. SGW granted a $500,000 charge as security for those guarantees. Goldfinger and Kimel each guaranteed the other's borrowing. They both signed directions that the proceeds from their personal loans be paid to SGW. There is no dispute that funds CTC lent to Goldfinger and Kimel were contributed to SGW.[66] Most of the money from the CTC financing went to SGW to pay the Bollinger VTB, tax arrears and other SGW expenses and the Bolliger VTB, on which about $355,000 was due, was paid out as a result of that financing. The refinancing did result in excess funds paid to counsel for SGW of about $113,000.

142 On April 27, 2001, SGW granted a charge against 105 University to Community Trust Company in the amount of $50,000 (the "CTC $50K Charge) securing the loan made to SGW. The same day SGW granted a charge against 105 University to CTC as collateral security for the two promissory notes in the amount of $250,000 given to CTC by each of Goldfinger and Kimel (the "CTC $500K Charge"). According to Kimel, this three-part financing structure was used at the insistence of CTC.

143 On the registration of the CTC mortgages, Annopol postponed its mortgages to CTC.

144 The personal loans were renewed on an annual basis. SGW paid CTC the interest on each of the Goldfinger and Kimel loans.[67] In his trial evidence Kimel described what happened was as follows:

> Summit Glen Waterloo didn't actually have the funds to, uh, available to it to make those payments, moneys had to be funneled into Summit Glen Waterloo to make those payments.[68]

Upon the appointment of Zeifman as receiver of SGW, those payments ceased and CTC commenced an action against Goldfinger and Kimel to recover the amounts due under the personal loans. CTC also sued SGW and obtained default judgment dated May 22, 2009 in the amount of $573,506 (the "CTC Default Judgment"). Farber contended that the CTC Default Judgment was obtained without any leave granted to lift the stay of proceedings in the receivership and therefore the estate of SGW was not bound by the CTC Default Judgment.

145 On May 28, 2010, CTC informed Farber, as trustee of Annopol, that it intended to sell 105 University under power of sale; this was a month before SGW was adjudged bankrupt. On July 12, 2010, CTC wrote to Farber's counsel enclosing loan

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

statements for its two mortgages, both of which showed the full amount of the principal outstanding. As well, both showed additional claimed expenses which brought the amounts due under each mortgage up to $142,819.10 and $582,690.76 respectively. CTC indicated that there would be additional unbilled legal fees and disbursements. CTC provided subsequent August 3, 2010 statements of mortgage showing the amounts due under each mortgage to be $151,239.26 and $586,034.58 respectively.

146 On August 4, 2010, CTC assigned both charges to a company which Goldfinger had incorporated, 1830994 Ontario Limited. Goldfinger deposed that 183 paid $751,000 for the two mortgages; Farber asserted that Goldfinger paid $742,273, which was the figure cited by CTC's counsel in its August 4, 2010 letter as the amount payable by 183. The assigned charges were registered on August 5, 2010. In addition, by assignments dated August 3, 2010, CTC assigned to 183 its CTC Default Judgment. Notice of that assignment was given to Farber's counsel on August 6, 2010.

147 183 filed a proof of claim dated September 17, 2010 for a secured claim of $765,792.38 in respect of the two charges.

B. The claim under the CTC $50K Charge

B.1 The position of Goldfinger and 183

148 Goldfinger argued that 183, as assignee of the two CTC mortgages, was entitled to stand in the same position as CTC because an assignee at law stands in the same position as the assignor in relation to the assigned chose in action. On this basis, 183 contended that it was entitled to claim from the estate of SGW the amounts it had paid to CTC in return for the assignments of the two mortgages, including interest on that amount, together with its solicitorclient costs.

B.2 The position of Farber

149 Farber did not oppose the technical validity of the CTC $50K Charge. Nor did Farber dispute that CTC had advanced $50,000 to SGW and that CTC would have been entitled to claim against SGW for any amounts owing under the CTC $50K Charge.

150 Farber opposed 183's claim in respect of the CTC $50K Charge on two grounds. First, Farber took issue with the quantum of the amount due under the charge. Second, Farber argued that a release given by Goldfinger to SGW in 2009 released this claim against SGW.

151 As to the quantum, Farber argued that as trustee it was entitled under *BIA* s. 135(1) to require from 183 evidence in support of its security, but 183 had failed to provide documentary evidence to support portions of its claim under the CTC $50K Charge. Farber contended that a claim against the estate of a bankrupt was determined on the merits of the underlying claim and therefore an assignee could not take the position that its claim should be based on the amount it paid for the chose in action, rather than on the state of accounts between the assignor and the bankrupt. On this basis, the trustee disputed the following amounts claimed by 183 under the CTC $50K mortgage:

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(i) Legal fees of $35,000, when the CTC August 3, 2010 statement of mortgage only indicated legal fees of $26,441.14;

(ii) Three months interest under section 17 of the *Mortgages Act*. Farber took the position that such an amount could not be claimed where a mortgagee was taking steps to enforce payment of amounts owing under a charge. It is worth observing that Farber did not dispute that amount in its Reports dated January 18, 2011 and July 23, 2011;

(iii) Realty taxes of $37,301.49 outstanding as at August 5, 2010. Farber contended that 183 did not provide any evidence about the amount of realty taxes in fact paid by CTC and that as of November 15, 2010, only $10,655 in realty taxes were owing for 105 University. Farber stated that all outstanding realty taxes were paid from the proceeds of sale;

(iv) Operating expenses of $25,283.67, subject to a credit of $8,921.70 in rental income. Farber reported that 183 had not provided any documentation to support claims that CTC had contributed cash to make a shortfall in operating costs for 105 University; and,

(v) "Estimated utility expenses for July to September" 2010 in the amount of $15,000. Farber reported that 183 had not provided any documentation to support those claims.

Accordingly, Farber argued that 183's claim based on the CTC $50K Charge should be fixed at $50,000, plus interest and nominal costs.

152 In correspondence that passed between counsel prior to the hearing, Goldfinger took the position that the documents supporting the amounts claimed under the charges were not relevant and that Goldfinger was entitled simply to rely on the CTC statement.[69] Goldfinger, in his August 8, 2012 affidavit, tried to mitigate the effect of that position by contending that the documents were not in his possession, leaving hanging the implication that he could not obtain them.

153 Finally, Farber took the position that 183's claim against SGW based on the August 5, 2010 assignments had been extinguished by the release given by Goldfinger to SGW as part of the December 16, 2009 Minutes of Settlement. Farber contended that Goldfinger was bound by the Second Settlement even if one of the transactions which formed part of that settlement (the charge against 40 Park Lane) was successfully challenged under the *BIA*.

B.3 Analysis

154 There is no dispute concerning the validity or enforceability of the assignment of the CTC $50K Charge from CTC to 183. The assignment was made for valuable consideration. Consequently, 183, as assignee, is entitled to payment of the principal amount of the CTC $50K Charge, together with interest until the date of payment, and I so order.

155 *BIA* s. 135(1) clearly provides that a trustee "may require further evidence in support of the claim or security". Consequently, Farber was acting well within the rights of a trustee to require 183 to provide further evidence of the various amounts claimed in respect of the CTC $50K Charge. 183's position that the trustee was not entitled to such information because 183 could claim the amount which it had paid its assignor was incorrect. The trustee could have asked for such further information from CTC; its assignee stood in no better position.

156 One can understand why Farber would have asked for further evidence in support of various amounts, given that the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

expenses claimed exceeded the principal amount of the charge.

157 Although I am tempted simply to disallow 183's claim for those expenses because of its unreasonable refusal to provide the further evidence requested by the trustee, unreasonableness has characterized the positions of both parties to this Claims Motion. Consequently, I make the following orders:

(i) 183 shall provide Farber, as trustee of SGW, with the further evidence previously requested in respect of the additional items claimed for the CTC $50K Charge no later than November 30, 2013;

(ii) Farber shall file with the Court, to my attention, no later than December 24, 2013, a further report providing its views about the sufficiency of the further evidence provided and its position on the amounts claimed in light of that further evidence;

(iii) 183 shall file any further submissions on this issue no later than January 15, 2014, with such submissions not to exceed 10 pages;

(iv) I shall then release supplementary reasons deciding 183's claim for those additional amounts by February 14, 2014.

158 From this it follows that I have rejected Farber's argument that 183's claim against SGW in respect of the CTC $50K Charge was extinguished by the release given by Goldfinger to SGW as part of the December 16, 2009 Minutes of Settlement.

159 The parties to the December, 2009 Second Settlement were Morris Goldfinger, on the one hand, and on the other: Jack Lechcier-Kimel, Summit Glen Trayvan Holdings Inc., Summit Glen Waterloo/2000 Developments Inc., Summit Glen Brantford Holdings Inc., Raleigh Street Investments Inc., Summit Glen Bridge Street Inc., Summit Glen Fairway Holdings Inc., Annopol Holdings Ltd. and Mahvash Lechcier Kimel. The Second Settlement required the parties to enter into Mutual Releases:

13. The parties hereto will promptly exchange full and final mutual releases in the form attached as schedule #1 once each of the following has occurred ("the Release Date"):

a) the Park Lane Mortgage has been registered; and

b) any existing mortgages in favour of the Plaintiff registered on the Remaining Properties have been discharged and replaced with the Valleyview/University Mortgages.

14. *The parties agree that the aforementioned releases are intended to release the Plaintiff* and the Defendants *from any claims they may have between each other arising from Community Trust Company's action against Jack Lechcier-Kimel and Morris Goldfinger (Hamilton Court file #09-8872)* and also from any claims relating to any possible flow of funds out of the defendant companies. (emphasis added)

160 As to the nature of the claims released, the operative language of the Full and Final Mutual Release read as follows:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> SAVE AND EXCEPT AS NOTED BELOW, HEREBY RELEASE, ACQUIT AND FOREVER DISCHARGE, EACH OTHER WJTHOUTQUALIFICATION OR LIMITATION:
>
> from all manner of actions, causes of action, suits, debts, dues, accounts, bonds, covenants, contract, complaints, claims and demands for damages, monies, losses, indemnity, costs, interest in loss, or injuries howsoever arising which hereto may have been or may hereafter be sustained by Goldfinger or the Kimel Parties directly, or indirectly, as a consequence of any agreement between the parties and from any and all actions, causes of action, claims or demands of whatsoever nature, whether in contract or in tort or arising as a result of a fiduciary duty or by virtue of any statute or upon or by reason of any damage, loss or injury arising out of the matters set forth above and, without limiting the generality of the foregoing, from any and all matters that were pleaded in, or could have been pleaded, in Ontario Superior Court of Ontario Action 00007823-00Cl (herein referred to as the "Action").
>
> . . .
>
> WITHOUT LIMITING THE GENERALITY OF THE FOREGOING, the parties hereto declare that the intent of this Full and Final Mutual Release subject to the specific exclusions set out herein, is to conclude all issues arising from the matters set forth above and from the Action and it is understood and agreed that this Release is intended to cover, and does cover, not only all known injuries, losses and damages, but also injuries, losses and damages not now known or anticipated but which may later develop or be discovered, including all the effects and consequences thereof.
>
> AND FOR THE SAID CONSIDERATION it is agreed and understood that Goldfinger and the Kimel Parties *will not make any claim or take any proceedings against any other person or corporation who might claim, in any manner or forum, contribution or indemnity* in common law or in equity, or under the provisions of any statute or regulation, including the *Negligence Act* and the amendments thereto and/or under any successor legislation thereto, and/or under the *Rules of Civil Procedure*, from each of Goldfinger and The Kimel Parties discharged by this Full and Final Mutual Release, *in connection with the matters outlined above and in the Action.*
>
> (emphasis added)

161 I have rejected Farber's submission that the 2009 Release applied to bar 183's claim as assignee of the CTC Charges for several reasons:

> (i) 183, the assignee of the CTC Charges, was not a party to that release. Although the 2009 Release included in the definition of "Goldfinger" any "successor corporations under his control", that term, when read in the context of the entire definition, referred to any successor corporation who was claiming "a right or interest *through him*" in respect of the matters released. 183 took assignments of the CTC charges in its own right and was not claiming a right or interest through Goldfinger;
>
> (ii) The assignments were made well after Goldfinger and the Kimel Parties had entered into the 2009 Release;
>
> (iii) The assignments were made for valuable consideration given at the time of the assignments;
>
> (iv) Finally, to the extent that the release may have caught post-execution events, the assignment of the charges by CTC to 183 did not fall within the matters released, which the 2009 Release described as matters:
>
> > ...which hereto may have been or may hereafter be sustained by Goldfinger or the Kimel Parties directly, or indirectly, as a consequence of any agreement between the parties and from any and all actions, causes of action, claims or demands of whatsoever nature, whether in contract or in tort or arising as a result of a fiduciary duty or by virtue of any statute...

C. The claim under the CTC $500K Charge

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

C.1 The position of Farber

162 Farber opposed 183's claim under the CTC $500K Charge on three grounds. First, Farber submitted that the assignment from CTC to 183 was incomplete. Second, Farber contended that the charge could not support a claim against SGW because of its collateral nature. Finally, Farber argued that a release given by Goldfinger to SGW in 2009 released this claim against SGW.

163 In its first argument, Farber contended that although 183 had taken an assignment from CTC of the charge "and any debt owing under the CTC Charges",[70] 183 had failed to take an assignment of the SGW Guarantee of the personal loans to Goldfinger and Kimel and also failed to take an assignment of the promissory notes given by Goldfinger and Kimel to CTC, with the result that "183 Ontario cannot rely on the SGW Guarantee or the CTC $500K Charge in circumstances where it is not able to assign to SGW, on payment, the debt owing by Goldfinger and [Kimel] to which the SGW Guarantee and the CTC $500K Charge relate."

164 In respect of its second argument, Farber stated that SGW had granted CTC the $500K Charge to stand as security for SGW's guarantee of the loans CTC had made to each of Goldfinger and Kimel in the amount of $250,000. Farber argued that if the estate of SGW was required to pay 183, as assignee of CTC, the full amounts due under the CTC $500K Charge, then Goldfinger, as the principal debtor on the personal loan from CTC, should be required to pay SGW (i) an amount equal to what SGW pays 183 in respect of its guarantee of the Goldfinger personal loan together with (ii) 50% of what SGW pays 183 in respect of the guarantee of the Kimel personal loan, the latter because Goldfinger had provided CTC with his own guarantee of the Kimel loan.

165 In effect, this argument by Farber did not deny the validity of the CTC $500K Charge, its assignment to 183 or the amount claimed under the charge. Farber argued that the potential claim-over by SGW against Goldfinger, both in respect of his personal loan and Kimel's loan, should trigger an immediate obligation by Goldfinger to pay SGW all but $125,000 of the amount paid by SGW to 183 under the CTC $500K Charge, plus interest and costs. Farber contended that its position on this point was supported by the fact that Goldfinger had provided 183 with the funds to acquire the CTC Charges. As the argument was put in its January 18, 2011 Report, Farber contended that:

> Farber understands that the CTC $500,000 Charge relates to these personal loans [to Goldfinger and Kimel]. Dr. Goldfinger is, by using 183 Ontario to acquire CTC's claim vis a vis the personal loans, attempting to recover a personal loan made to him and a personal loan made to Mr. Lechcier-Kimel that he guaranteed from SG Waterloo.

Or, as put by Farber's counsel in his letter of August 13, 2010 to 183:

> As the guarantor of the obligations owing by Dr. Goldfinger and Mr. Lechcier-Kimel by Community Trust, SG Waterloo is entitled, on the payment of the amount guaranteed, to take an assignment of the claims as against Dr. Goldfinger and Mr. Lechcier-Kimel. In this regard, 183 Ontario owes an obligation to the SG Waterloo bankruptcy estate not to prejudice SG Waterloo's interest as guarantor of the obligations now owing to 183 Ontario.

166 Finally, Farber contended that the Release given as part of the 2009 Second Settlement affected 183's ability to claim as assignee of the CTC Charges in two ways. First, Farber pointed to paragraph 14 of the Second Settlement which stated:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> The parties agree that [the full and final release is] intended to release the Plaintiff and Defendants from any claims they may have between each other arising from Community Trust Company's action against Jack Lechcier-Kimel and Morris Goldfinger...

Second, Farber argued that under the Release, Goldfinger was prohibited from making any claim that would result in any person claiming contribution or indemnity from Kimel, and since 183, a company controlled by Goldfinger, was now asserting a claim which could result in SGW seeking contribution and indemnity from Kimel, the Release barred such a claim.

C.2 The position of Goldfinger and 183

167 Goldfinger argued that 183, as assignee of the two CTC mortgages, was entitled to stand in the same position as CTC since an assignee at law stands in the same position as the assignor in relation to the assigned chose in action. On this basis, 183 contended that it was entitled to claim from the estate of SGW the amounts it had paid to CTC in return for the assignment of the two mortgages, including interest on that amount, together with its solicitor-client costs.

168 183 argued that Farber's arguments based on the nature of the CTC $500K Charge as collateral security for SGW's guarantee of personal loans to Goldfinger ignored the separate legal existence of 183. As put by Goldfinger and 183 in their Factum:

> 104. If 183 is not permitted to stand in the shoes of CTC as ranking as first mortgagee, the effect would be to put Farber in a better position than if 183 had not paid off CTC and the related encumbrances. Such a result would be unfair. Thus, if for some reason, 183 was not entitled to stand in the same position as CTC, subrogation would be an appropriate remedy in this case.

C.3 Analysis

First argument: The completeness of the assignment

169 In support of its argument that the assignment from CTC to 183 was incomplete, Farber relied on the decision of the Court of Appeal in *McLennan v. McLennan* [2003 CarswellOnt 401 (Ont. C.A.)].[71] One must approach applying that decision with some caution, turning as it did on complex facts concerning "unusual transactions". In that case the Court of Appeal was not prepared to interfere with the findings of fact made by lower courts that, properly interpreted in its factual matrix, the assignment of a collateral mortgage assigned only the mortgage, but not the debt secured by the mortgage.

170 By contrast, in the present case, the Assignment of Security and Mortgage Debt executed on August 4, 2010 by CTC and 183 (the "Assignment") in respect of both CTC Charges provided, in part:

> Whereas the Assignor holds first and second registered Mortgages/Charges on the lands and premises described municipally as 105 University Avenue East, Waterloo...
>
> . . .

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> *And Whereas the Assignor holds a Security Agreement as a Secured Party given by Summit Glen Waterloo/2000 Developments Inc. (the "Debtor"), on or about the 25th day of April, 2001.*
>
> . . .
>
> *[T]he Assignor assigns to the Assignee all of the outstanding Mortgage debt in and to the Mortgaged Lands,* debts, sums of money, choses in action, causes of action, Judgments and *all other right, title, and interest in the Mortgage debt and in the security it presently holds in respect of the debtors obligations as that term is defined in the Security Agreement* which is annexed hereto as Schedule "A", for the absolute use and benefit of the Assignor. (emphasis added)

171 The Security Agreement dated April 25, 2001 from SGW to CTC stated that it was given "as security for the repayment of all present and future indebtedness of the Debtor [SGW] to the Secured Party [CTC] and interest thereon and for the payment and discharge of all other present and future liabilities and obligations, direct or indirect, absolute or contingent, of the Debtor to the Secured Party (all such indebtedness, interest, liabilities and obligations being hereinafter collectively called the "Obligations")". Section 9 provided that default by SGW "under any of the Obligations" constituted a default under the Security Agreement, and section 10 provided that upon such a default CTC "may declare any or all of the Obligations to be immediately due and payable..." The liabilities and obligations of SGW to CTC were set out in the guarantee dated April 25, 2001 from SGW to CTC, under which SGW "guarantees payment to Community Trust of all debts and liabilities, present or future, direct or indirect, absolute or contingent, matured or not, at any time owing by the Borrower [Kimel and Goldfinger] to Community Trust or remaining unpaid by the Borrower to Community Trust..." Section 3 provided that CTC was not bound to exhaust its recourse against Kimel and Goldfinger before entitled to payment from SGW.

172 Given the assignment of the "Mortgage debt" and the definition of "Obligations" used in the Security Agreement, which was also assigned, I find that by its terms the Assignment assigned the debt created as between SGW and CTC. The language of the Assignment certainly evidenced an intention that it would assign the underlying debt to the assignee of the charges. Nor did CTC purport to retain for its own benefit any part of the guaranteed debt; it made a full assignment to 183.

173 Moreover, Farber's argument ignored the simple fact that 183 paid valuable consideration to CTC for the assignment of the CTC Charges. Given that 183 took out CTC by paying off what CTC contended was due to it on the mortgage debt, in the circumstances of this case the principle of equitable subrogation would apply to place 183 fully in the shoes of CTC in order to achieve fairness in light of all the circumstances.[72]

174 Finally, the right of action enjoyed by the estate of SGW to recover from the principal debtors amounts paid under the guarantee arises by operation of law.[73]

175 For these reasons I do not accept Farber's argument that the Assignment was not effective to enable 183 to enforce the debt secured by the CTC $500K Charge.

Second argument: the collateral nature of the Assignment

176 An assignee of a charge is subject to the state of account upon the charge as between the chargor and chargee, and the assignee can assert no greater rights than those held by its assignor of the charge.[74] More generally, an assignee steps into the shoes of the assignor and has the rights and is subject to the obligations of the assignor under the assigned agreement.[75]

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

177 If a third party other than 183 had taken an assignment of the CTC security for value, it is highly unlikely that Farber would be advancing arguments about the collateral nature of the charge. The assignee would take subject to the state of the account between SGW and CTC, and it would not be open to Farber to argue for the disallowance of the assignee's proof of claim by contending that the bankruptcy estate might enjoy some right to seek recovery from another person for the monies paid. I do not see how the identity of the assignee changes that analysis with respect to the validity of a claim against SGW under the CTC $500K Charge. 183 enjoys a separate legal personality from Goldfinger. 183 paid good and valuable consideration for the assignment; this is not a case involving some sort of sham transaction. As an assignee for value of the Charge and the mortgage debt, 183 is subject to the state of account between SGW and its predecessor, CTC, but is not subject to the state of account between SGW and some other person.

178 Whether the estate of SGW might enjoy some claim of recovery against some other person, such as Goldfinger or Kimel's bankruptcy estate, is a matter for the trustee to assess in light of all the circumstances, including the obligations imposed upon SGW by the releases exchanged as part of the 2009 Settlement — releases, which I should note, Farber did not attack.

179 In the circumstances of this case, I do not accept Farber's contention that as part of the process of reviewing a creditor's proof of claim under the *BIA*, the court notionally should entertain and determine the surety's potential *quia timet* "action" against one of the principal debtors, Goldfinger. Quite apart from the conflation which would result of a *BIA* proof of claim process with the determination of a civil cause of action, the proof of claim under review is that of a person — 183 — which enjoys a separate legal personality from the principal debtor, Goldfinger, and which paid valuable consideration for the Assignment.

Third argument: recovery under the Assignment is barred by the 2009 Settlement Release

180 I reject Farber's submission that the 2009 Release barred 183's claim under the CTC $500K Charge for the reasons given above rejecting a similar argument in respect of the CTC $50K Charge.

181 By way of summary, I allow 183's claim in respect of the CTC $500K Charge, with interest until the date of payment.

VII. Summit Glen Waterloo: Goldfinger's constructive trust claim

182 Although not specifically mentioned in his notice of motion, in his factum Goldfinger argued that since he had made all of the cash payments for the acquisition of 105 University by SGW, as well as a payment against the Bolliger VTB, he should be entitled to a constructive trust claim against the estate of SGW for those amounts.

Goldfinger's argument

183 Goldfinger deposed that in the first quarter of 2000, he had issued cheques totaling $130,000 to Summit Glen Fairway Holding which were used, in part, to pay the deposit for the 105 University property, title of which was taken in the name of SGW. The acquisition closed on April 14, 2000. Goldfinger deposed that he provided all the cash for the closing

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(about $415,000) by way of a $467,000 cheque dated April 13, 2000 to SGW, with Bolliger taking a $450,000 five-month VTB for the balance of the purchase price.

184 Although the Bolliger mortgage was to mature in September, 2000, the parties continued the arrangement for a period of time until the Community Trust Company refinancing took place. On October 16, 2000, SGW paid down $50,000 of the Bolliger VTB principal. Goldfinger deposed that the monies SGW used came from a $25,000 cheque he made out to SGW on July 6, 2000 and from an August 10, 2000, cheque for $35,000 which he provided to Summit Glen Fairway Holdings.

185 As part of the First Settlement, SGW was to deliver to Goldfinger a promissory note "in a principal amount equal to the unpaid Shareholder Loans of the company as set forth in Schedule 3". In the case of SGW, the amount of the Shareholder Loan, or "outstanding indebtedness to Goldfinger", was fixed by the parties at $867,556. The note, dated June 6, 2008, was to be paid in two installments ending in December, 2009. Kimel and each of the Summit Glen Companies, including SGW, severally guaranteed repayment of the Shareholder Loans, and each company was to grant to Goldfinger second mortgages on the Properties, which included 105 University. Annopol delivered a postponement, in favour of Goldfinger, of "all present and future debts and liabilities of whatever nature or kind due or accruing due to" it by, *inter alia*, SGW. Although the First Settlement contemplated that Goldfinger would deliver a release to Kimel and the Summit Glen Companies, he was only required to do so once they had fully complied with all of the terms of the First Settlement. They never did so.

Analysis

186 Section 81(1) of the *BIA* requires that any person who claims property in the possession of the bankrupt must file a proof of claim with the trustee; *BIA* s. 124 requires that every creditor shall prove his claim by delivery to the trustee of a proof of claim. Goldfinger did not file with the trustee of SGW a proof of claim in respect of a trust property claim or a proof of claim in respect of a related debt or liability claim. Goldfinger raised the issue for the first time in his factum. In light of Goldfinger's failure to comply with the claims mechanisms specified by the *BIA*, I disallow his "constructive trust" claim.

187 In any event, Goldfinger's claims also fails for substantive reasons. In *Credifinance Securities Ltd., Re*, the Ontario Court of Appeal considered the issue of claims in a bankruptcy founded on constructive trust:

> There is no question that the remedy of constructive trust is expressly recognized in bankruptcy proceedings. Both the case law and authors of texts make this clear, although the test for proving the existence of a constructive trust in a bankruptcy setting is high: L.W. Houlden & Geoffrey Morawetz, *Houlden and Morawetz Bankruptcy and Insolvency Analysis* (Toronto: WL Can, 2011) at F§5(1). The authors add this at F§5(8):
>
> > A constructive trust will ordinarily be imposed on property in the hands of a wrongdoer to prevent him or her from being unjustly enriched by profiting from his or her wrongful conduct" (citations omitted).
>
> . . .
>
> Thus, a constructive trust in bankruptcy proceedings can be ordered to remedy an injustice; for example, where permitting the creditors access to the bankrupt's property would result in them being unjustly enriched. The prerequisite is that the bankrupt obtained the property through misconduct. The added necessary feature is that it would be unjust to permit the bankrupt and creditors to benefit from the misconduct.
>
> . . .

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> Constructive trust is a discretionary remedy. In a bankruptcy there are other interests to consider besides those of the defrauder and the defraudee: there are other creditors. Thus, the exercise of remedial discretion must be informed by additional considerations than in a civil fraud trial.[76]

188 The evidence does not support Goldfinger's claim for a constructive trust in respect of the monies which he advanced to SGW in 2000 to finance part of the purchase price for 105 University and to make a payment against the Bolliger VTB. On his own evidence, Goldfinger made those advances, as well as all his other advances to SG companies, on the expectation that his loans would be repaid from the successful re-development of those properties and, in addition, he would share in the ultimate net profit from the resale of the properties. In the present case, the redevelopment of 105 University was not successful and SGW went into bankruptcy. In making his investments Goldfinger assumed the risk of an investor who looked to the profits of the undertaking to recoup his investment. At the time he extended his loans to Kimel's companies, it was open to Goldfinger to require that they grant him security in return; he did not obtain such security, yet advanced funds.

189 Goldfinger argued that it would be inequitable to deny him a constructive trust on some of the assets of SGW because Kimel deceitfully placed the Annopol mortgages on the property without the knowledge of Goldfinger. On his own evidence, Goldfinger became aware of Kimel's activities in 2007. He then entered into the First Settlement with Kimel. When Kimel breached that settlement, Goldfinger commenced the Goldfinger Action. The Second Settlement resolved that action. Neither the First nor Second Settlement gave Goldfinger a constructive trust over some of the assets of SGW.

190 Finally, the 2009 Release precludes Goldfinger from asserting such a claim at this point of time. The claim falls within the matters released, and Goldfinger executed that release with full knowledge of the long history of Kimel's misconduct against him and others.

191 Given those circumstances, I see no substantive basis for Goldfinger's constructive trust claim — there was no injustice which required a remedy by way of constructive trust. For these reasons, I dismiss Goldfinger's constructive trust claim.

VIII. Goldfinger's claim as the sole shareholder of Summit Glen Waterloo

A. Evidence

192 From the incorporation of SGW in April, 2000 until 2008, Mahvash was its sole registered shareholder.

193 According to Goldfinger, during that period of time he believed he should have an equity interest in SGW and other SG companies. After Goldfinger and Kimel had arrived at an agreement in principle to resolve their dispute in the Fall of 2007, Goldfinger engaged two lawyers at the Minden Gross firm, Reuben Rosenblatt and Carl Schwebel, to flesh out and paper their agreement. Both lawyers testified at the trial. Both testified that while Goldfinger thought that he had been promised shares in the Summit Glen group of companies, neither lawyer had ever seen any share certificates which evidenced his shareholding in SGW or other Summit Glen companies.[77]

194 As part of the closing structure of the First Settlement, Mahvash transferred 50% of the shares of SGW to Goldfinger

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

who immediately transferred them to Kimel. The transfer from Mahvash to Goldfinger reflected the following acknowledgement contained in the First Settlement:

> Notwithstanding that the shares of the Summit Glen Companies have not been formally issued, Goldfinger is, and for all purposes shall be deemed to be, the legal and beneficial owner of 50% of the share capital of each of the Summit Glen Companies...

SGW was included in the definition of "Summit Glen Companies". On the closing of the First Settlement, Goldfinger transferred all his "deemed" shares in the Summit Glen Companies to Kimel for $5 million, half of which had been satisfied by the late 2007 and early 2008 payments of $2.5 million, and the rest was to be paid out by the end of 2009. It never was.

195 As part of their later matrimonial separation arrangement, Kimel transferred his 50% shareholding to Mahvesh. Goldfinger ultimately acquired the outstanding shares of SGW from Mahvesh for $50,000 through a Transfer of Shares dated September 27, 2010.

196 Although Farber argued that Goldfinger had been a shareholder of SGW from its inception, pointing to statements contained in (i) 2007 memoranda prepared by Minden Gross LPP, (ii) Goldfinger's accountant's recording of $50 for Goldfinger's capital contribution to SGW, and (iii) recitals in the First Settlement, the corporate records of SGW contained no entry showing Goldfinger as a shareholder or the issuance of any shares to Goldfinger.

197 Goldfinger moved for an order that the net surplus of monies remaining from the sale of 105 University, after payment of proper amounts owing to creditors, be paid to him. Farber opposed Goldfinger's request for a distribution of any of the sale proceeds to him as the sole shareholder of SGW on the basis that the administration of the SGW bankruptcy was not yet complete and therefore it was unclear whether any surplus funds would be available for distribution to an equity claimant.

198 Farber contended that the transactions through which Goldfinger acquired the shares of SGW *prima facie* would be void against the trustees of the estates of Kimel and Mahvash (in the event that a bankruptcy order issued against her) under the *BIA*. That issue is not before me for determination. Farber is not the trustee of the Kimel's estate. No claim to that effect by Kimel's trustee is before me. Mahvash has not been adjudged bankrupt; Farber is not the trustee proposed in the bankruptcy proceedings against Mahvash.

B. Analysis

199 Goldfinger's claim to part of the proceeds of the sale of 105 University as sole shareholder of SGW clearly is an "equity claim" as defined by *BIA* s. 2. Section 140.1 of the *BIA* provides that a creditor is not entitled to a dividend from the estate in respect of an equity claim until all claims that are not equity claims have been satisfied. Further, section 144 of the *BIA* stipulates that the bankrupt only is entitled to any surplus following payment to the bankrupt's creditors and payment of the costs, charges and expenses of the bankruptcy proceedings.

200 Farber, as trustee of SGW, reported that the administration of that bankrupt's estate was not yet complete. In my view, it would be premature to make any order regarding the distribution of any surplus of the estate of SGW until the trustee

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

reports that all claims of nonequity creditors have been paid and the costs of administration satisfied. Accordingly, I am not prepared to make the order sought by Goldfinger for a distribution of surplus to him in his capacity as shareholder of SGW.

201 That said, it is important that the administration of the estate of SGW be completed within a reasonable period of time. Accordingly, I am seizing myself of all court proceedings involving the SGW estate, and I require counsel to appear before me on a 9:30 appointment before the end of November, 2013, to report on what further steps remain in the administration of this estate and the anticipated timing for their completion.

D. Allegations of conflict of interest against Farber by Goldfinger

202 Goldfinger submitted that by acting as trustee in bankruptcy of SGW, as well as trustee for claimants against SGW, such as the estates of Montor, Annopol and SGG, Farber stood in a conflict of interest position, had failed to act impartially in respect of the claims advanced against the estate of SGW and had failed to provide full information to interested parties, in breach of the *BIA Rules* governing the conduct of trustees. Goldfinger also contended that the reports filed in this proceeding by Farber adopted an adversarial position and went beyond the scope of such reports as mandated by *BIA* s. 170.[78]

203 On the latter point I would note that Goldfinger previously brought a motion in the Preferences Application to strike out one of Farber's reports. That motion was dismissed on March 31, 2011.

204 While my review of Farber's reports does not raise undue concerns about the trustee's attempt to provide the Court with full and impartial information, the various hats worn by Farber in this proceeding causes some concern. The proof of claim scheme created by the *BIA* contemplates that the trustee of the bankrupt will examine every proof of claim and then either allow or disallow the claim. A trustee must give reasons for its determination or disallowance, and the trustee's decision is final and conclusive unless the claimant appeals to the court. That scheme assumes that the trustee who examines and determines a claim has no interest in the claim. In the present case, Farber was acting as trustee both for the bankrupt, SGW, and several of the claimants: Annopol, Montor and SGG. In light of those mandates, Farber could not act impartially in considering the claims filed by Annopol, Montor and SGG. Thus resulted this motion where the court, in effect, played the role of the trustee under section 135 of the *BIA* in examining and determining claims.

205 In my view, such a procedure for considering claims against a bankrupt should be avoided to the extent possible. The *BIA* squarely places the responsibility for the examination and determination of proofs of claims in the hands of the trustee. In order to be able to discharge that duty, a trustee should avoid taking on any mandate which might put it in a conflict of interest situation where it is contemplated that there may be a highly contested claims process. I am concerned that Farber, by acting as trustee for both the bankrupt and claimants, did not afford the court the full benefit of independent arguments in respect of the claims on behalf of the estate, on the one hand, and the claimants, on the other. That said, I am satisfied in the present case that Farber placed before the court a sufficiently fulsome record relating to the claims advanced, and I am not persuaded, as argued by Goldfinger, that Farber's obvious conflict of interest in the claims procedure caused an inadequate record to be placed before the court, although I have required Farber to provide more sufficient information for SGG's unjust enrichment claim.

IX. Summary of conclusions on the Claims Motion

206 A summary of the orders disposing of the Claims Motion can be found towards the end of these Reasons in Part XIV.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

X. The Preferences Application: Summary of the allegations against Dr. Goldfinger

207 In the Preferences Application, Farber, in its capacity as the trustee in bankruptcy of the estates of Montor, Annopol and SG Brantford, has advanced claims to set aside a number of transactions which formed part of, or which were related to, the First Settlement (2008) between Goldfinger, on the one hand, and Kimel, Mahvash and their companies on the other. Specifically, according to Farber's July 3, 2012 Fresh as Amended Notice of Application, it seeks the following orders:

(i) repayment of the $2.5 million paid by Annopol to Goldfinger in December, 2007 and January, 2008 in anticipation of the First Settlement;

(ii) alternatively, an order requiring Mahvash, as a director of Annopol, to pay the $2.5 million to the Annopol estate;

(iii) setting aside the charges/mortgages of land granted by SG Brantford to Goldfinger over a property at 176 Henry Street in Brantford, Ontario (the "Goldfinger 176 Henry Charges");

(iv) setting aside charges/mortgages of land granted by Summit Glen Bridge Street Inc. ("SG Bridge") to Goldfinger over a property located at 70 Bridge Street in Kitchener, Ontario (the "Goldfinger 70 Bridge Charges");

(v) setting aside subordinations made by Annopol of charges/mortgages of land granted by SG Brantford (the "Annopol 176 Henry Charges") and SG Bridge (the "Annopol 70 Bridge Charges") in favour of the Goldfinger Charges on those properties (the "Annopol Subordinations");

(vi) the repayment of $471,000 paid by SG Brantford to Goldfinger in November, 2008 to discharge the Goldfinger 176 Henry Charges; and,

(vii) payment to the Annopol estate of the surplus from the sale of 70 Bridge (the "Bridge Surplus") currently being held in trust for the benefit of Goldfinger's counsel, Davis Moldaver LLP ("Davis") and Farber's counsel, Gowling Lafleur Henderson LLP ("Gowlings").

208 Although Farber initially also attacked the 2009 Second Settlement, by the time of trial it had amended its application to limit its preference claims to the $2.5 million paid under the First Settlement, the $471,000 payment made in November, 2008, and Goldfinger's claim to the surplus of SG Bridge.[79]

209 Goldfinger contended that Farber's position was unfair in that it sought to deprive him of substantial benefits negotiated under the First Settlement while holding Goldfinger to releases which he gave in the Second Settlement (2009). Goldfinger deposed that he would not have entered into the Second Settlement without having obtained the payments which formed part of the First Settlement.

XI. The 2007/2008 $2.5 million settlement payments to Goldfinger

A. The allegations and positions of the parties

210 Farber seeks the repayment of the $2.5 million paid by Annopol to Goldfinger in December, 2007 and January, 2008

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

in anticipation of the execution of the First Settlement. The date of the initial bankruptcy event in the Annopol bankruptcy was May 26, 2009; the date of bankruptcy was May 27, 2010. Farber seeks to void or set aside the $2.5 million payment on several grounds:

> (i) as a transfer at undervalue under s. 96 of the *BIA*;
>
> (ii) as a voidable transaction under the *Fraudulent Conveyances Act*, R.S.O. 1990, c. F. 29 (the "*FCA*") or the *Assignments and Preferences Act*, R.S.O. 1990, c. A.33 (the "*APA*");
>
> (iii) as relief for a finding of oppressive conduct made under s. 248 of the *OBCA*; or,
>
> (iv) on the basis of unjust enrichment.

Farber did not attack the payments under *BIA* s. 95.

211 Goldfinger opposed any such findings or remedies.

B. The First Settlement: 2008

212 As mentioned, in May and June, 2008, Goldfinger, Kimel and many of his companies signed the First Settlement. The parties to it were Goldfinger, on the one hand, and Kimel, Mahvash, Annopol, as well as several of Kimel's companies on the other, collectively referred to as the Summit Glen Companies (the "SG Companies"), which included Summit Glen Brantford Holdings Inc. ("SG Brantford") and Summit Glen Bridge Street Inc. ("SG Bridge"). Annopol was not included in the definition of the SG Companies. All parties acknowledged in the First Settlement having been represented by independent counsel. Farber is trustee for three of the signatories (Annopol, SG Brantford, SG Waterloo) and a petitioning creditor for yet another (Mahvash).

213 The First Settlement was designed in such a way as to repay to Goldfinger the amounts already lent to the SG Companies and to enable Goldfinger to extract an amount representing his notional equity or profit in the various real estate developments. The material terms concerning the repayment of amounts already advanced by Goldfinger were as follows:

> (i) The SG Companies acknowledged that they were indebted to Goldfinger in the amount of $6.5 million, which amount was termed the "Shareholder Loans". (As noted, the SG Companies did not include Annopol.) Those companies provided Goldfinger with promissory notes in the amount of the unpaid Shareholder Loans, with payment of half the principal amount due December 11, 2008, and the balance on December 11, 2009;
>
> (ii) Kimel and each of the SG Companies guaranteed repayment of the Shareholder Loans;
>
> (iii) As collateral security for the repayment of the Shareholder Loans, the SG Companies granted to Goldfinger what were called the Shareholder Mortgages, each in the amount of $6.5 million on specified properties, including 176 Henry Street, Brantford owned by SG Brantford and 70 Bridge Street West, Kitchener, owned by SG Bridge.

214 Although shares in the SG Companies had never been issued, the First Settlement deemed Goldfinger to own

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

beneficially 50% of the shares of each company and went on to provide that:

> (i) The SG Companies would purchase Goldfinger's 50% interest in the companies for $5 million, or what was termed the Share Purchase Price. The parties agreed that the $2.5 million previously paid to Goldfinger represented a partial payment of the Share Purchase Price. Kimel would provide Goldfinger with a secured promissory note for $1.5 million, with the final payment due December 11, 2009, and Kimel would provide Goldfinger with an unsecured promissory note for $1 million, again with the final payment due by December 11, 2009;
>
> (ii) Each SG company guaranteed payment of both notes, and granted Goldfinger $1.5 million Third Mortgages on each property;
>
> (iii) Also, each member of the Kimel Group, which included Annopol, postponed all their claims against the SG Companies to the prior payment of the Shareholder Loans and both notes. Annopol also agreed to postpone $750,000 charges it held on the 176 Henry and 70 Bridge properties in favour of Goldfinger's Shareholder Mortgages and Third Mortgages.

215 The Kimel Parties agreed that until all of the payments to Goldfinger were made, the SG Companies would not sell or encumber the properties, except the Valleyview and Fairway properties. If either property was sold or mortgaged, the proceeds would be paid out in accordance with an agreed formula.

216 The First Settlement contained an Indemnity under which Kimel and the SG Companies would indemnify and hold Goldfinger harmless from certain claims:

> On closing, Kimel and each of the Summit Glen Companies shall jointly and severally, covenant and agree to indemnify and hold harmless Goldfinger, his personal representatives, heirs, executors, administrators, successors and assigns (collectively, the "Indemnified Parties"), from and against any and all claims, damages, losses, liabilities, demands, suits, judgments, causes of action, legal proceedings, penalties or other sanctions and any and all costs and expenses arising in connection therewith, including, without limitation, reasonable legal fees and disbursements on a solicitor and his own client substantial indemnity basis, which may be suffered or incurred by any of the Indemnified Parties howsoever resulting from or arising out of: (i) a breach or inaccuracy of any of the representations or warranties made by the Kimel Group or the Summit Glen Companies (or any of them) in this Agreement; (ii) any non-observance or nonperformance of any of the covenants, obligations and agreements of the Kimel Group or the Summit Glen Companies (or any of them) under this Agreement; (iii) any liabilities, debts, contracts or obligations of the Summit Glen Companies, whether present or future, absolute or contingent, direct or indirect; and (iv) any claims, suits and proceedings which are pending or hereafter made against the Summit Glen Companies.

217 The First Settlement also required Kimel, Mahvash, Annopol and the SG Companies to provide Goldfinger with a release containing the following language:

> IN CONSIDERATION of the sum of TWO DOLLARS ($2.00), the completion of the transactions contemplated in the Memorandum of Agreement and other good and valuable consideration (the receipt and sufficiency of which are hereby acknowledged), [Kimel, Mahvash, Annapol and the SG Corporations] (collectively, the "Releasing Parties") [do] hereby irrevocably release, remise, and forever discharge each and all of [Goldfinger, his personal representatives, heirs, executors, administrators, successors and assigns], their respective officers, directors, shareholders, heirs, personal representatives, successors and assigns, from any and all manner of Claims which the Releasing Parties or any of them has or in the future may have, suffer or incur, by reason of, arising from or in connection with, or in any way relating to,

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

the Properties and other assets, undertaking, operations and liabilities of the Summit Glen Companies.

And for the same consideration, each of the Releasing Parties further agrees not to make any Claims, or take any proceedings in connection with any Claims released herein against any other person or corporation who might claim contribution or indemnity under the provisions of any statute or otherwise from any of the Released Parties.

218 The lawyers who papered the First Settlement for Goldfinger, Messrs. Rosenblatt and Schwebel of the Minden Gross firm, were not involved in the negotiation of the $2.5 million payment; they understood that Goldfinger and Kimel had agreed on that amount before approaching the lawyers. Schwebel understood that conceptually the $2.5 million payment would represent a partial payment to Goldfinger of his notional equity in all the properties, while the mortgages issued by the SG Companies would serve to secure repayment of Goldfinger's Shareholder Loans.[80] However, the lawyers also testified that the allocation of the indebtedness due to Goldfinger amongst the SG Companies which were party to the First Settlement was not based on valuations of the properties, but on an agreement reached amongst the two parties.[81]

219 The First Settlement was completed on June 8, 2008, at which time Goldfinger received the promissory notes, guarantees, postponements, and mortgages due to him under it.

220 As part of the closing of the First Settlement, shares in SG Waterloo were transferred to Goldfinger from Mahvash, and then immediately transferred to Kimel.

221 In the Preferences Application Farber has not challenged the validity or enforceability of the Indemnity or the Release contained in the First Settlement.

C. Farber's claim under BIA s. 96

C.1 The statute

222 Farber seeks to set aside or declare void the $2.5 million payment to Goldfinger made prior to the execution of the First Settlement as a transfer at undervalue under *BIA* s. 96. Although Farber's amended notice of application and factum were not as clear as they could have been on this point, presumably Farber brought its challenge to the transaction in its capacity as trustee in bankruptcy of Annopol, the entity from which the cheques were issued to Goldfinger. Section 96 of the *BIA* provides as follows:

96. (1) On application by the trustee, a court may declare that a transfer at undervalue is void as against, or, in Quebec, may not be set up against, the trustee — or order that a party to the transfer or any other person who is privy to the transfer, or all of those persons, pay to the estate the difference between the value of the consideration received by the debtor and the value of the consideration given by the debtor — if

(a) the party was dealing at arm's length with the debtor and

(i) the transfer occurred during the period that begins on the day that is one year before the date of the initial bankruptcy event and that ends on the date of the bankruptcy,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(ii) the debtor was insolvent at the time of the transfer or was rendered insolvent by it, and

(iii) the debtor intended to defraud, defeat or delay a creditor; or

(b) the party was not dealing at arm's length with the debtor and

(i) the transfer occurred during the period that begins on the day that is one year before the date of the initial bankruptcy event and ends on the date of the bankruptcy, or

(ii) the transfer occurred during the period that begins on the day that is five years before the date of the initial bankruptcy event and ends on the day before the day on which the period referred to in subparagraph (i) begins and

(A) the debtor was insolvent at the time of the transfer or was rendered insolvent by it, or

(B) the debtor intended to defraud, defeat or delay a creditor.

(2) In making the application referred to in this section, the trustee shall state what, in the trustee's opinion, was the fair market value of the property or services and what, in the trustee's opinion, was the value of the actual consideration given or received by the debtor, and the values on which the court makes any finding under this section are, in the absence of evidence to the contrary, the values stated by the trustee.

(3) In this section, a "person who is privy" means a person who is not dealing at arm's length with a party to a transfer and, by reason of the transfer, directly or indirectly, receives a benefit or causes a benefit to be received by another person.

C.2 The transfers

223 *BIA* s. 2 defines a "transfer at undervalue" as "a disposition of property or provision of services for which no consideration is received by the debtor or for which the consideration received by the debtor is conspicuously less than the fair market value of the consideration given by the debtor". That section includes "money" in the definition of "property", so a payment of money falls within the definition of a disposition of property.

224 The evidence established that Goldfinger received payments totaling $2.5 million from Annopol. The company's bank statements showed that on December 5, 2007 Annopol transferred $1.5 million to Goldfinger. Annopol also issued four cheques to Goldfinger which he negotiated in December, 2007 and January, 2008: December 12, 2007 ($300,000); December 21, 2007 ($200,000); December 28, 2007 ($300,000); January 10, 2008 ($200,000). Each cheque bore the notation: "re-purchase shares".

225 Goldfinger, in his September 6, 2011 affidavit, deposed that he had "no idea as to the source of the funds" for the $2.5 million payment "or that there was any issue regarding the solvency of Kimel, Mahvash or any of the SG companies":

> At the time I received the payment, Kimel told me that approximately $1.5 million came from Mahvash's inheritance, and the balance came from an elderly gentleman who attended the same synagogue as Kimel. I was further told that Kimel was required to sign an "I.O.U" in front of the synagogue's rabbi.[82]

226 Farber stated that the $2.5 million paid to Goldfinger came from (a) inter-company loans from related companies and

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(b) a $200,000 loan by a third-party, Mr. Srubiski, to Annopol.[83]

227 According to Kimel, the funds used to make the payments largely came from three sources. First, part came from the proceeds of the sale on October 4, 2007 of a property owned by Summit Glen Fairway (the 293 Fairway property). Of the net sale proceeds of about $1 million, Kimel testified that half was paid to Annopol. That company's bank statement showed the deposit of $485,000 received on October 5, 2007 from SG Fairway.[84] Annopol had a mortgage registered against that property which was discharged on the closing.

228 It is not self-evident from the record that funds from the SG Fairway property sale were used to fund part of the payments to Goldfinger. All payments to Goldfinger were made out of Annopol's HSBC bank account. On December 2, 2007, three days before the first payment (wire transfer) to Goldfinger, the balance in Annopol's HSBC account was just over $1,000.00, raising questions about what had been done with the early October deposit of funds Annopol had received from SG Fairway. Kimel testified that the funds could have been put into a term certificate or "temporarily utilized to pay down a line of credit in another company, or various things".[85] The records for that bank account disclosed that the funds Annopol used to cover the $1.5 million wire transfer to Goldfinger consisted of a December 5 transfer to Annopol from SG Trayvan ($1 million), together with a series of transfers on that date to Annopol from a variety of Summit Glen companies, with SG Fairway contributing only $24,000.00.

229 One must note that Annopol's opening bank account balance on December 5, before the wire transfer to Goldfinger, was just over $6,000.00, with a $39.64 closing balance following the wire transfer to Goldfinger. That banking history leads me to find that Annopol used monies from other Summit Glen companies transferred to it on December 5, 2007 to fund its $1.5 million wire transfer to Goldfinger. That wire transfer had no material impact on Annopol's bank account balance for that day.

230 Second, Kimel testified that another source of the funds which enabled Annopol to pay Goldfinger were proceeds from the re-financing of the Trayvan properties (41-67 Valleyview) in the Fall of 2007. Annopol's HSBC bank statements do show a transfer from SG Trayvan to Annopol of $1 million immediately prior to the $1.5 million wire transfer sent to Goldfinger on December 5, 2007.

231 As to the balance, Kimel variously testified that about $200,000 might have come from his wife, Mahvash, or from a third party investor, Srubiski.[86]

232 Turning from the wire transfer to the Annopol cheques provided to Goldfinger, Annopol's HSBC bank records disclosed the following transactions:

(i) the initial cheque of December 12, 2007 for $300,000 was debited from Annopol's HSBC account on December 14, 2007. The account's closing balance on December 12 was just over $2,000.00. On December 13 a number of deposits were made, most identified as coming from other Summit Glen companies, including a $25,000 transfer from SG Fairway. Following the negotiation of the cheque to Goldfinger, the closing balance in Annopol's bank account was just over $18,000;

(ii) the December 21 cheque for $200,000 was debited from Annopol's HSBC account the same day. The closing balance on December 20 was about $2,000. The cheque to Goldfinger was covered by the deposit on December 21

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

of a $200,000 cheque from another HSBC account and a $10,000 transfer from SG Fairway. Kimel was unsure whether those funds came from his wife or from a third party investor, Mr. Srubiski. The closing balance at the end of December 21 was just over $10,000;

(iii) the December 28 cheque for $300,000 was debited the same day from Annopol's HSBC bank account. The cheque was covered by a $300,000 transfer of funds from SGG the same day. SGG had an operating line of credit with HSBC; the cheque to Annopol drew that line of credit up over the $2 million mark. On December 28 the HSBC account's opening balance was just over $10,000; its closing balance was an overdraft of about $3,000, largely the result of other cheques written that day on the account;

(iv) the January 10, 2008 cheque for $200,000 was debited the same day from Annopol's HSBC account. The prior opening balance was about $2,500. The cheque to Goldfinger was covered by a transfer to Annopol from SGG which SGG, in turn, funded by drawing on its HSBC line of credit, pushing it up to $2.376 million. The day's end closing balance on Annopol's account was the same as the opening balance.

In sum, Annopol's bank records disclosed that it relied on transfers of funds from other Summit Glen companies just prior to the negotiation of the cheques in order to cover the amounts paid to Goldfinger. SGG's HSBC line of credit statements showed that it borrowed $500,000 from its line to fund, through Annopol, that amount of the payments made to Goldfinger. It is not possible from the record to determine the ultimate source of the other funds transferred by the other Summit Glen companies in order to cover the cheques paid to Goldfinger.

C.3 Was the transfer at undervalue?

233 Mr. Baigel, one of the trustees at Farber, deposed, in his August 15, 2012 affidavit, that the value of the $2.5 million paid by Annopol to Goldfinger obviously was $2.5 million and Annopol did not receive any consideration from Goldfinger in return for the $2.5 million or, if there was consideration, the value of that consideration was zero. Farber pointed to *BIA* s. 96(2) which requires the trustee to state its opinion about the value of the actual consideration received by the debtor, and then goes on to provide that "the values on which the court makes any finding under this section are, in the absence of evidence to the contrary, the values stated by the trustee". Farber then argued that Goldfinger had not adduced any evidence to question the correctness of the trustee's opinion as to value, so "the Court must, as a result, conclude that Goldfinger provided no consideration in return for the $2.5 million".

234 I disagree. Additional evidence regarding the value of the consideration was filed, in particular the text of the First Settlement, together with evidence explaining how the First Settlement came about.

235 By its terms the First Settlement constituted the compromise of a dispute between Kimel and Goldfinger. Section 1(e) stated:

> This Agreement accurately records our understanding of the discussions that have taken place between the Parties to date in connection with the resolution of the existing shareholders' dispute.

Section 17 provided that if the Kimel Group and the Summit Glen Companies performed all their obligations under the settlement, Goldfinger would be required to deliver a release in their favour from all claims relating to the Properties and other assets of the companies. Annopol would be a beneficiary of such a release.

236 Goldfinger argued that the First Settlement constituted a legitimate exchange of value: a compromise of Goldfinger's

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

claims to recover his $6.7 million investment and a surrender of some mortgage security, in return for only some of the misappropriated money from Kimel and his companies. He deposed that he entered into the First Settlement after "formal demand" had been made by his lawyers against Kimel.[87] Goldfinger also deposed that he would not have entered into the First Settlement without the prior payment of the $2.5 million: "Rather I would have immediately commenced and continued the litigation against the Kimels and their various companies."[88] Goldfinger deposed that over the course of his dealings with Kimel, $2.956 million of his money had been deposited into Annopol.[89]

237 Forbearance from suit, either actual or promised, can constitute good consideration to support a transaction.[90] Under cross-examination Goldfinger agreed that instead of commencing legal proceedings against Kimel, he sat down with him and negotiated a resolution of their dispute.[91] Indeed, in November, 2007, Goldfinger had threatened litigation and had gone so far as having counsel prepare a draft affidavit for him to swear in an action he was thinking of bringing against Kimel and several Summit Glen companies, including Annopol, for the appointment of a receiver over a number of the properties.[92] In the context of a dispute where one party had invested $6.5 million with the other, the partial repayment of $2.5 million of that investment in return for the investing party compromising and fixing his rights in accordance with the terms contained in the First Settlement, does not strike me as a circumstance where the "the consideration received by the debtor is conspicuously less than the fair market value of the consideration given by the debtor". I therefore conclude that the payments of $2.5 million by Annopol to Goldfinger did not constitute a "transfer at undervalue".

238 In the event that I am wrong about that conclusion, let me proceed to examine the other elements a trustee must establish under *BIA* s. 96.

C.4 Were Goldfinger and Annopol at arm's length?

239 Different tests apply depending upon whether the party, Goldfinger, was or was not dealing at arm's length with the debtor, Annopol. Persons who are related to each other are deemed not to deal with each other at arm's length: *BIA*, s. 4(5). The evidence disclosed that at the time of the First Settlement, Goldfinger was not a registered shareholder of Annopol. Although the First Settlement "deemed" Goldfinger to be a shareholder of Annopol, taken as a whole the evidence regarding the First Settlement indicated that such a designation was merely a technical device, probably tax-driven, by which to structure the deal. Viewed substantively, prior to the execution of the First Settlement (and indeed thereafter), Goldfinger never exercised any control over the affairs of Annopol, or any other Summit Glen company. I therefore find that Goldfinger and Annopol were not related persons within the meaning of *BIA* s. 4(2) and (3).

240 That does not end the inquiry. *BIA* s. 4(4) provides that "it is a question of fact whether persons not related to one another were at a particular time dealing with each other at arm's length". An oft-cited statement of the test for ascertaining whether parties, in fact, are acting at arm's length, can be found in the decision in *Abou-Rached, Re*[93] which followed the test in *Gingras, Robitaille, Marcoux Ltée v. Beaudry*[94] as follows:

> ... a transaction at arm's length could be considered to be a transaction between persons between whom there are no bonds of dependence, control or influence, in the sense that neither of the two co-contracting parties has available any moral or psychological leverage sufficient to diminish or possibly influence the free decision-making of the other. Inversely, the transaction is not at arm's length where one of the co-contracting parties is in a situation where he may exercise a control, influence or moral pressure on the free will of the other. Where one of the co-contracting parties is, by reason of his influence or superiority, in a position to pervert the ordinary rule of supply and demand and force the other to transact for a consideration which is substantially different than adequate, normal or fair market value, the transaction is questions is not at arm's length.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

More recently, the Alberta Court of Appeal, in *Piikani Nation v. Piikani Energy Corp.*, held that factors which have been developed in the jurisprudence under the *Income Tax Act* concerning "not dealing at arm's length" can provide helpful guidance in the *BIA* context, in particular three factors identified by the Supreme Court of Canada in *McLarty v. R.*:[95] (i) was there a common mind which directs the bargaining for both parties to a transaction; (ii) were the parties to the transaction acting in concert without separate interests; and, (iii) was there *de facto* control?[96]

241 Farber submitted that Goldfinger did not act at arm's length with Annopol, whose affairs were directed by Kimel, because he was a close personal and family friend of Kimel, as well as his business associate. While it is true that Goldfinger had been close friends with Kimel, one must look at the nature of their relationship at the time the payments of $2.5 million were made. The evidence disclosed that although Goldfinger had lent a large amount of money to Kimel and his companies, he had not been involved in the operation of the Summit Glen companies and had quite limited information about their affairs. In 2007 Goldfinger discovered that he had been misled by Kimel, in particular learning that many of the Summit Glen properties were encumbered with mortgages about which Goldfinger was not aware. Goldfinger sought explanations and a return of his money, but Kimel stalled. Settlement discussions commenced only after Goldfinger had retained counsel who, in letters dated November 12 and 13, 2007, required Kimel to respond to a settlement proposal, failing which proceedings would be commenced against him in this Court. Each side was represented by their own counsel. Although the amount of the initial $2.5 million repayment was arrived at by Goldfinger and Kimel, the overall structure and details of the First Settlement were negotiated with the assistance of counsel. In my view, those facts do not disclose bonds of "dependence, control or influence" which generally are necessary in order to find that two parties are not acting at arm's length.

242 Farber relied on a few cases to argue that a broader view should be taken of those relationships which could qualify as not at arm's length. In *Piikani Nation v. Piikani Energy Corp.*,[97] the Alberta Court of Queen's Bench considered an application by a trustee under *BIA* s. 95 to set aside payments to two individuals and one of their wholly-owned corporations at a time when the two individuals were directors and officers of the bankrupt corporation. The payments in issue represented the unearned portion of one person's service contract with the bankrupt and a severance payment to the other. In finding both individuals to be not at arm's length to the bankrupt, the court focused on the process by which a corporation, such as the bankrupt, would make decisions to pay others. Both individuals were directors of the corporation which had made the challenged payments, and the court stated that "it is hard to think that such decisionmakers could be at arm's length to the corporation when they make payment decisions, especially to themselves".[98] That decision recently was over-turned on appeal.[99]

243 Farber also relied on another decision of the Alberta Court of Queen's Bench, this one in *Visionwall Technologies Inc., Re.*[100] That case did not involve sections 95 or 96 of the *BIA*, rather the unpaid supplier provisions of *BIA* s. 81.1(1), specifically the ability of a supplier to repossess goods as long as at the time of demand the goods had not been resold at arm's length and were not subject to any agreement for sale at arm's length. In dispute was whether the Export Development Corporation was an arm's length purchaser of the materials in question. EDC had guaranteed the performance bond which had been issued to the bankrupt for the completion of a construction contract, for which the materials in question had been ordered. When the bankrupt company encountered financial difficulties, a plan was developed which would see the construction contract completed by another company and, to facilitate that plan, EDC agreed to purchase the materials in question. As put by the court, if the construction contract was not completed and EDC was called on its guarantee of the bond, it would face a potential hit of $3 million. Against that background the court concluded that EDC was not at arm's length to the bankrupt because it was "a vital cog" in the transaction to complete the construction contract and "stood to lose $3,000,000 if the contract was not completed". That financial interest in the transaction meant EDC was not an arm's length purchaser of the materials.[101] Also, the court noted that the trustee had dealt the materials to EDC after it had received notice from the supplier for their return.

244 The present case is distinguishable from that in *Visionwall*. When considering a transaction under *BIA* s. 96, the party who dealt with the bankrupt necessarily had a financial interest in the transaction. The question is whether the transfer was at

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

undervalue. Consequently, the existence of a financial interest by the party to the transfer cannot, in and of itself, turn that party into a person not dealing at arm's length with the bankrupt. Something more is required.

245 For those reasons, I conclude that in respect of the payments of $2.5 million, Goldfinger was dealing at arm's length with the debtor, Annopol.

C.5 Did the transfer take place within one year before the date of the initial bankruptcy event?

246 In light of that finding, *BIA* s. 96(1)(a) governs the balance of the analysis. Did the payments occur "during the period that begins on the day that is one year before the date of the initial bankruptcy event and that ends on the date of the bankruptcy"? In the case of Annopol, the date of the initial bankruptcy event was May 26, 2009 and the date of bankruptcy was May 27, 2010. Accordingly, the review period for transfers under *BIA* s. 96 commenced May 26, 2008. The $2.5 million payments occurred in the period between December 5, 2007 and January 10, 2008, prior to and outside of the statutory review period.

247 Consequently, the transfers of $2.5 million are not reviewable under *BIA* s. 96 and Farber's claim, as trustee of Annopol, under that section must fail.

248 Notwithstanding that conclusion, I shall deal with the remaining elements of a challenge under *BIA* s. 96 since they involve some of the same factual issues as arise in Farber's claims under provincial preferences legislation.

C.6 Was Annopol insolvent at the time of the transfer or was Annopol rendered insolvent by it?

249 Section 2 of the *BIA* defines an insolvent person as one who is not bankrupt, but (i) who is unable to meet its obligations as they generally come due, (ii) has ceased paying its current obligations in the ordinary course of business as they generally become due, or (iii) the aggregate of whose property, at fair valuation, would not be sufficient to enable payment of its obligations, due and accruing due.

250 As set out in a response to an undertaking given on the examination of Michael Baigel, Farber stated that it was relying on the following evidence in support of its assertion that Annopol was insolvent at the time the $2.5 million payments were made to Goldfinger: (i) Mr. Baigel's affidavit of August 15, 2012; (ii) Annopol's financial statements for 2007 and 2008; and, (iii) the fact that Annopol had to borrow funds to pay its expenses and interest.

251 Baigel, in his March 19, 2010 affidavit, deposed simply that "based on the value at which the Goldfinger/Kimel Properties were sold, it appears that the Goldfinger/Kimel Companies are and have always been insolvent." Annopol was not included in Baigel's definition of the "Goldfinger/Kimel Companies".

252 The Statement of Affairs signed by Kimel for Annopol on June 14, 2010 showed that liabilities of $12.875 million greatly exceeded assets of $350,000.

253 Perelmuter prepared Annopol's financial statements at the material time, but he did so on a "notice to reader" basis, relying largely on information provided to him by Kimel. Perelmuter conceded that he was familiar "to some degree" with the financial affairs of Kimel's company, and he testified that in December, 2007[102] and August, 2008 he had assumed that Annopol was solvent.[103]

254 This evidence does not establish that at the time of the transfers (December, 2007 and January, 2008) Annopol had ceased paying its obligations or was unable to meet its obligations as they became due. Annopol's bank account statements for that period disclosed that it received funds from other Summit Glen companies, and perhaps third parties, which enabled it to meet its on-going obligations. However, applying the balance sheet test of insolvency, its assets certainly were insufficient to meet its liabilities, as disclosed by the 2008 unaudited notice to reader financial statements, and that circumstance was corroborated by the 2010 statement of affairs signed by Kimel which showed liabilities greatly exceeding assets.

255 Against that evidence, Goldfinger advanced several reasons in support of his argument that Annopol was not insolvent at the time it made the $2.5 million payments to him. First, pointing to Montor's proof of claim in the Annopol bankruptcy which showed loans and payments made by Montor after the date of the payments to Goldfinger, he argued that Montor most likely would not have made those payments to Annopol (which amounted to about $500,000) had it known Annopol was insolvent at the time, particularly since Annopol's principal, Perelmuter, was the accountant for Annopol.[104] That evidence certainly tends to show that Perelmuter and Montor did not believe Annopol to be insolvent at the time of the transfers, but their perception of Annopol's affairs is not the same thing as whether Annopol, in fact, was solvent or insolvent.

256 Goldfinger also argued that since Annopol was not the ultimate source of the funds used to pay him the $2.5 million - rather the funds came from other Summit Glen companies or Kimel family money - one should not treat the payments, for purposes of assessing Annopol's solvency, as coming out of Annopol's assets. In the same vein Goldfinger deposed that at the time of the First Settlement, he received a June 11, 2008 statutory declaration from Kimel and Mahvash which led him to believe that the SG companies were financially viable.[105] Goldfinger also argued that since Annopol was merely a flow-through conduit for Kimel and the SG group of companies, Farber's claims on its behalf were "specious". Specifically, Goldfinger argued in his factum:

> 59. The $2.5 million paid to Goldfinger under the First Settlement was not Annopol's money as Farber, again, wrongly alleges. The money came principally from the sale of the Summit Glen Fairway property, and the refinancing of SG Trayvan's Valleyview property.

257 Earlier in these Reasons I reviewed how each payment to Goldfinger was funded through Annopol's bank account. Other Summit Glen companies transferred funds to Annopol to enable it to cover the cheques issued to, or wire transfer made to, Goldfinger and, in the result, those payments had no net impact on Annopol's bank accounts. In that sense, the payments did not render Annopol insolvent, at least on a cash-flow basis. But, those transfers in and out would have given rise to credits and debits on Annopol's balance sheet, and the 2008 financial statements, unaudited though they may have been, were based on information which came from Kimel and showed a very significant excess of liabilities over assets.

258 Consequently, I find that at the time of the December, 2007 and January, 2008 transfer of $2.5 million from Annopol to Goldfinger, Annopol was insolvent under the balance sheet test.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

C.7 Did Annopol intend to defraud, defeat or delay a creditor?

259 That then leads to the final inquiry under *BIA* s. 96(1)(a)(iii): did the debtor, Annopol, intend to defraud, defeat or delay a creditor by making the transfers to Goldfinger? For the purposes of this analysis, I accept Farber's submission that the intention of Annopol at the time should be determined by reference to the intention of Kimel, the person who directed the company's affairs.[106]

The case law concerning ascertaining the debtor's intention

260 The general approach to ascertaining the intention of the debtor in respect of a transfer or transaction was summarized by Rouleau J., as he then was, in *Conte Estate v. Alessandro* [2002 CarswellOnt 4507 (Ont. S.C.J.)]:[107]

> In this type of case it is unusual to find direct proof of intent to defeat, hinder or delay creditors. It is more common to find evidence of suspicious facts or circumstances from which the court infers a fraudulent intent.
>
> These suspicious facts or circumstances are sometimes referred to as the "badges of fraud." These badges of fraud are evidentiary indicators of fraudulent intent and their presence can form the *prima facie* case needed to raise a presumption of fraud...
>
> The presence of one or more of the badges of fraud raises the presumption of fraud. Once there is a presumption, the burden of explaining the circumstantial evidence of fraudulent intent falls on the parties to the conveyance. The persuasive burden of proof stays with the plaintiff; it is only the evidentiary burden that shifts to the defendants.

261 The decision of Anderson J. in *Fancy, Re*[108] often is referred to as a classic enumeration of the badges of fraud. In the 1988 decision of *Nuove Ceramiche Ricchetti S.p.A. v. Mastrogiovanni* this Court dealt with *Fancy, Re* as follows:

> The law on the subject of fraudulent conveyances is accurately stated by Mr. Justice Anderson in *Re Fancy* (1984), 51 C.B.R. (N.S.) 29....
>
>> The plaintiff must prove that the conveyance was made with the intent defined in that section [i.e. section 2 of the *Fraudulent Conveyances Act*]. Whether the intent exists is a question of fact to be determined from all of the circumstances as they existed at the time of the conveyance. Although the primary burden of proving his case on a reasonable balance of probabilities remains with the plaintiff, the existence of one or more of the traditional "badges of fraud" may give rise to an inference of intent to defraud in the absence of an explanation from the defendant. In such circumstances there is an onus on the defendant to adduce evidence showing an absence of fraudulent intent. Where the impugned transaction was, as here, between close relatives under suspicious circumstances, it is prudent for the court to require that the debtor's evidence on bona fides be corroborated by reliable independent evidence.
>
> The "badges of fraud" referred to by Mr. Justice Anderson are those et [*sic*] out in *Re Dougmor Realty Holdings Ltd.* (1966), 59 D.L.R. (2d) 432:
>
>> (1) Secrecy
>>
>> (2) Generality of Conveyance
>>
>> (3) Continuance in possession by debtor

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> (4) Some benefit retained under the settlement to the settlor.

The above passages set out the test to be applied. The badges of fraud alleged by the plaintiff are established.[109]

262 The case law[110] has identified the following circumstances as constituting "badges of fraud" for purposes of ascertaining the intention of a debtor: (i) the transferor has few remaining assets after the transfer; (ii) the transfer was made to a non-arm's length person; (iii) there were actual or potential liabilities facing the transferor, he was insolvent, or he was about to enter upon a risky undertaking; (iv) the consideration for the transaction was grossly inadequate; (v) the transferor remained in possession or occupation of the property for his own use after the transfer; (vi) the deed of transfer contained a self-serving and unusual provision; (vii) the transfer was effected with unusual haste; or, (viii) the transaction was made in the face of an outstanding judgment against the debtor.

The evidence and analysis

263 The direct evidence adduced by the Trustee on the issue of the intention of Kimel/Annopol in respect of the $2.5 million payments was given by Michael Baigel. His evidence, in actual fact, was limited to the state of Goldfinger's knowledge. On his cross-examination Baigel was asked to identify the information which the Trustee possessed about Goldfinger's knowledge about the financial status of Annopol at the time:

> Q. 208. What evidence do you have that Goldfinger even knew that Annopol had other creditors at that point in time?
>
> A. I assume — well, I can't assume.
>
> Q. 209. Right.
>
> A. So I'll just say the evidence is that he was heavily involved with these people. Surely he wouldn't have just gone ahead and taken this, and he didn't have access to financial statements. He was investing heavily with these people. Wouldn't he have known that there were liabilities out there? I can't believe he would have put however many millions of dollars he says he's put in without following up and just trusting — especially where he was, Jack Lechcier-Kimel, and saying, yeah, that's okay. You've got no liabilities.
>
> Q. 210. I take it from that, that you have no evidence that Goldfinger even knew Annopol had other creditors in December of 2007 or January of 2008. Correct?
>
> A. Well, but hold on. There was back in one of his affidavits he starts talking about that he wasn't aware that Jack Lechcier-Kimel put other securities on the various properties. Annopol had related properties, and surely when he was talking about that — I think that started in July 2007 from memory — he would have been aware of all these other liabilities out there.
>
> Q. 211. Isn't it fair to say that you have it backwards, that what he wasn't aware of was the mortgages in favour of Annopol on these various properties, not loans or monies owing by Annopol? It was mortgages to Annopol that he was unaware of, correct?
>
> A. I agree with you on that, but I'm not sure it's backwards. It's because that obviously diminishes what he has available if there's mortgages there.[111]

. . .

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Q. 214. You've told me about mortgages that I suggested to you were backwards. I'm asking you a really simple question. What evidence do you have that Goldfinger knew that Annopol had creditors? If you have no such evidence, just tell me.

A. At this point in time I would like to get back to you with anything that I do have.

Q. 215. So today —

A. Today I'm saying I can't remember.

264 In an answer to an undertaking given on that examination, Farber stated:

Farber does not know what Goldfinger knew vis-à-vis Annopol as at December of 2007 or January of 2008. However:

a. Goldfinger was aware that the $2.5 million was being paid to him by Annopol. He was, for example, given post-dated cheques from Annopol.

b. In an e-mail exchange between JLK and Goldfinger on 9 December 2007, JLK indicated to Goldfinger that money to pay the $2.5 million was being borrowed.

c. In paragraph 118 of his Affidavit sworn 6 September 2011 Goldfinger swears that he was told by JLK that the $1 million of the $2.5 million paid to him by Annopol was borrowed.

d. Rubin Rosenblatt has confirmed that JLK advised that money to make the $2.5 million payment was being borrowed.

265 The direct evidence of Kimel comes from his cross-examinations. On one of them Kimel was asked whether he had considered the impact the payment of the $2.5 million to Goldfinger would have on other creditors:

Q. 100. Please answer the question. Did you consider the impact of providing security to Goldfinger and subordinating Annopol's charge would have on the ability of Annopol to recover under the charge?

A. No, I didn't consider that.

Q. 101. You will agree that subordinating the charge...so $6.5 million in security to Goldfinger would make it difficult for Annopol to recover, correct?

A. I didn't, at that time, even think in terms of any of the concepts you are broaching.

Q. 102. So what were you thinking about at the time you granted the security?

A. Simply arriving at a fair and equitable settlement to buy his share back of the business...or buy him out of the business in total.

Q. 103. So you were not thinking about the other creditors of the companies or the other stakeholders in these businesses?

A. I didn't think in terms of any other stakeholders. I didn't consider there were any.

Q. 104. What about the people that were lending money to Annopol which is being advanced onto companies like

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

SG Bridge?

A. Well, they had always advanced the money on the basis of properties being rezoned and redeveloped and being repaid from the redevelopment of those properties.

Q. 105. But by placing $6 million in security ahead of them, did you not prejudice their right to recover from the redevelopment?

A. I think you are asking me to look in hindsight and these were not items that...or thoughts that I, in any way, thought I had to consider at that time.

Q. 106. Okay, fair enough. So you didn't consider other interests except the interests of yourself and Dr. Goldfinger?

A. Yes.[112]

266 Elsewhere on that cross-examination Kimel testified:

Q. 386. When you were negotiating your settlement with Dr. Goldfinger, did you consider the possible impact that settlement might have on creditors like HSBC and Community Trust?

A. As I mentioned before, no, none of these situations were evident. The collapse hadn't taken place. The receivership hadn't occurred. I had no reason to assume that things wouldn't progress from a settlement to the ultimate plans that I had for redevelopment of the many properties.

Q. 387. But I guess...so you never considered their interests?

A. No.

Q. 389. When the first settlement got made, the one we call the December 2007 settlement, or the one that was finally finalized in June 2008, none of the companies who participated in that settlement had defaulted on any payments to anyone at all, right?

A. That's correct.

Q. 390. And as you understood it, none of those companies were insolvent, they were all companies with really strong potential for the various developments they were involved in, correct?

A. Yes, that's correct.[113]

267 Kimel testified that although his wife, Mahvash, was the sole owner and director of Annopol, he ran that company on a day-to-day basis and he did not discuss its affairs with her in any detail. Mahvash signed any documentation Kimel asked her to.[114] According to Kimel, Mahvash was aware of the $2.5 million payment to Goldfinger, but she had not been involved in the settlement negotiations.[115]

268 As to the direct evidence from Mahvash, she deposed that Kimel managed and controlled all of the family's finances and did not provide her with information about the companies' affairs. Mahvash stated that she became aware of the $2.5 million payment to Goldfinger in June, 2008, when she signed documents for the First Settlement, but only in 2010 did she become aware of the source of the funds for that payment. She stated that she had no way of knowing whether her personal funds had been used to fund that payment because Kimel had exercised complete control over all of the family's assets and

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

he had not discussed with her the source of the settlement funds. In May, 2010, Mahvash deposed:

> In summary, I did not cause any of the challenged transactions or payments to have been made, nor was I even aware that they were being made at the time that they occurred. I have only learned of these transactions as a result of the litigation instituted against me by Dr. Goldfinger and others during the past year and a half.

269 Goldfinger testified that he was not aware of the day-to-day business affairs of Kimel's companies nor did Kimel provide him with their financial statements.[116] He stated that Kimel provided him with "extremely limited information" about the companies.[117]

270 Finally, at trial the two lawyers who had represented Goldfinger during the negotiation of the First Settlement gave some evidence on the issue of the impact of that deal on other creditors. Schwebel testified that he did not recall any discussion with Goldfinger about the impact which the $2.5 million payment might have on the ability of the SG Companies to repay their creditors, but Schwebel described Goldfinger's understanding of those companies' state of affairs at that time as follows:

> A. Well, my understanding was that these — these properties had appreciated considerably in value and that there was a fair — a lot of equity in this — in this group of companies over and above the mortgages that were secured against them, and that — um, I think it was my understanding that Annopol or that the Kimels were the only other creditors of these companies.

. . .

> Q. Was any consideration ever given to the impact that this settlement might have on the companies' ability to repay those loans?
>
> A. The — the understanding was that these mortgages would be paid out on the sale or refinancing of the property, um, at which time, the other mortgages would have to as well be taken account of.[118]

271 On that point, Rosenblatt testified as follows:

> Q. And at that point in time, it was likely — well, let me rephrase that for a moment. So, they weren't paying their debt to Dr. Goldfinger. Did you have any knowledge with respect to the value of their properties?
>
> A. We never did appraisals, but when we were — when Dr. Goldfinger and Mr. Kimel were negotiating what the "equity" was, is Dr. Goldfinger, I think, thought it was worth — the equity was 11 or 12 million dollars over and above the mortgages, Mr. Kimel thought they were around 9 million and Dr. Goldfinger thought his share was worth five and a half million, Mr. Kimel felt four and a half million. And that's how they worked it out at the five million. Other than that, we did not do appraisals. They — uh, they seemed to know the values, they agreed on the values, and that's what we thought the values were.[119]

272 When inquiring into the intention of a debtor for the purposes of *BIA* s. 96(1)(a)(iii) — and the provincial preferences statutes for that matter — a court must ascertain the intention at the time of the transfer or transaction in light of the information known at that time. A court must resist the temptation to inject back into the circumstances surrounding the

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

impugned transaction knowledge about how events unfolded after that time. The focus must remain on the belief and intention of the debtor at the time, as well as the reasonableness of that belief in light of the circumstances then existing.

273 When looked at that way, the direct and circumstantial evidence, taken together, lead me to conclude, on the balance of probabilities, that by making the $2.5 million payments to Goldfinger, Kimel and Annopol did not intend to defraud, defeat or delay other creditors. I reach this conclusion for several reasons.

274 First, the terms of the First Settlement, which originated around the time the payments were made, indicated that the parties thought the Summit Glen companies would continue as going concerns and would generate sufficient value to repay fully Goldfinger for the advances he had made within two years — by December 11, 2009. The evidence disclosed that the parties to that agreement believed the properties owned by the Summit Glen companies possessed significant future value, a value which would prove sufficient to pay off those companies' liabilities and generate a profit for Kimel and Goldfinger to share. In hindsight one might question the reasonableness of that belief, but the evidence given by Schwebel and Rosenblatt about the parties' thinking at the time indicated a genuine belief in the value of the properties. I place significant weight on that evidence.

275 For the settlement to work, the parties had to expect that the Summit Glen companies would continue as going concerns and that the underlying real estate projects would generate a net benefit for division between the parties. Otherwise, the security granted to Goldfinger would have no value. As part of the closing documentation for the First Settlement, Goldfinger received a statutory declaration made by Kimel and Mahvash, in paragraph 6 of which they declared:

> There is no fact, matter or event which is known to me which has not been disclosed to Goldfinger which is likely to have a material adverse effect on the performance of the respective obligations of the Kimel Group and/or the Summit Glen Companies under this Agreement or which has or is likely to have a material adverse effect on the Properties or the operations of the Summit Glen Companies.

276 Of course, within half a year of the execution of the First Settlement the North American credit markets had collapsed, with a general depressing effect on real estate values. The parties did not adduce expert valuations of the properties at the time of the payments or the First Settlement. The monies paid into Court from the sale of 105 University and the prospect of full recovery in that estate of both secured and unsecured claims (subject to the issue of the Trustee's costs of administration) suggest that some of the properties had a net worth.

277 Second, the First Settlement was not put together in a rush; it was the product of over six month's negotiation. Both parties were represented by counsel.

278 Third, as I have found, they were dealing at arm's length.

279 Fourth, there was consideration for the settlement.

280 Fifth, the payment and the First Settlement were not put in place in the face of claims by judgment creditors against

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

the debtor.

281 In sum, I conclude that the payments of $2.5 million to Goldfinger made in December, 2007 and January, 2008, were not made by the debtor, Annopol/Kimel, with the intent to defraud, defeat or delay a creditor.

282 For these reasons, I dismiss Farber's claim for a declaration under *BIA* s. 96(1) to set aside the payment of $2.5 million to Goldfinger pleaded in paragraph IV(a) of its July 3, 2012 Fresh as Amended Notice of Application.

D. Farber's claim under the Assignments and Preferences Act and Fraudulent Conveyances Act

283 In paragraph III(a) of its Fresh as Amended Notice of Application, Farber sought declarations that the $2.5 million payment to Goldfinger was void as a preference or fraudulent conveyance pursuant to the provincial *Assignments and Preferences Act* and the *Fraudulent Conveyances Act*.

The Assignments and Preferences Act claim

284 Sections 4(1)(2) and 5(1) of the *Assignments and Preferences Act* ("*APA*") provide:

> 4. (1) Subject to section 5, every gift, conveyance, assignment or transfer, delivery over or payment of goods, chattels or effects, or of bills, bonds, notes or securities, or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made by a person when insolvent or unable to pay the person's debts in full or when the person knows that he, she or it is on the eve of insolvency, with intent to defeat, hinder, delay or prejudice creditors, or any one or more of them, is void as against the creditor or creditors injured, delayed or prejudiced.
>
> (2) Subject to section 5, every such gift, conveyance, assignment or transfer, delivery over or payment made by a person being at the time in insolvent circumstances, or unable to pay his, her or its debts in full, or knowing himself, herself or itself to be on the eve of insolvency, to or for a creditor with the intent to give such creditor an unjust preference over other creditors or over any one or more of them is void as against the creditor or creditors injured, delayed, prejudiced or postponed.
>
> . . .
>
> 5. (1) Nothing in section 4 applies to an assignment made to the sheriff for the area in which the debtor resides or carries on business or, with the consent of a majority of the creditors having claims of $100 and upwards computed according to section 24, to another assignee resident in Ontario, for the purpose of paying rateably and proportionately and without preference or priority all the creditors of the debtor their just debts, nor to any sale or payment made in good faith in the ordinary course of trade or calling to an innocent purchaser or person, nor to any payment of money to a creditor, nor to any conveyance, assignment, transfer or delivery over of any goods or property of any kind, that is made in good faith in consideration of a present actual payment in money, or by way of security for a present actual advance of money, or that is made in consideration of a present actual sale or delivery of goods or other property where the money paid or the goods or other property sold or delivered bear a fair and reasonable relative value to the consideration therefor.

285 Although any payment of money to a creditor, whether or not the payment is intended to prefer the creditor and

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

defeat other creditors, is protected under s. 5(1) of the *APA*,[120] in the present case Goldfinger has filed what he termed a "contingent" proof of claim in Annopol's bankruptcy, taking the position that he would only assert a claim as a creditor in the event the Court set aside the $2.5 million payment. In light of that position, the saving condition in *APA* s. 5(1) is not available to Goldfinger.

286 Considering Farber's claim under *APA* s. 4(1), I repeat my finding above that at the time of the $2.5 million payments Annopol was insolvent. I also repeat my finding that the debtor, Kimel/Annopol, did not intend to defeat, hinder, delay or prejudice creditors, and I rely on the same evidence for that finding to make the additional finding that neither did Goldfinger possess such an intent, to the extent such a finding might be necessary. On the latter point, Farber, in its February 8, 2013 Factum, stated that it was not asserting that in receiving the payments of $2.5 million or $471,000 (SG Bridge) Goldfinger had intended to defeat, hinder or delay creditors.

287 As to Farber's claim under *APA* s. 4(2),[121] Goldfinger did not file an unconditional proof of claim as a creditor, and Farber, in paragraph 129 of its February 7, 2013 Factum, was prepared to proceed on the basis that the payment of $2.5 million could not be attacked on the basis that Goldfinger was a creditor of Annopol. In any event, the evidence I have relied upon to make the findings above with respect to the intent of Kimel/Annopol and Goldfinger also leads me to conclude that at the time of the payments neither possessed the intent to give Goldfinger an unjust preference over other creditors.

The Fraudulent Conveyances Act claim

288 The *Fraudulent Conveyances Act* provides, in part, as follows:

> 2. Every conveyance of real property or personal property and every bond, suit, judgment and execution heretofore or hereafter made with intent to defeat, hinder, delay or defraud creditors or others of their just and lawful actions, suits, debts, accounts, damages, penalties or forfeitures are void as against such persons and their assigns.
>
> 3. Section 2 does not apply to an estate or interest in real property or personal property conveyed upon good consideration and in good faith to a person not having at the time of the conveyance to the person notice or knowledge of the intent set forth in that section.
>
> 4. Section 2 applies to every conveyance executed with the intent set forth in that section despite the fact that it was executed upon a valuable consideration and with the intention, as between the parties to it, of actually transferring to and for the benefit of the transferee the interest expressed to be thereby transferred, unless it is protected under section 3 by reason of good faith and want of notice or knowledge on the part of the purchaser.

As put by Sedgwick J. in *Dapper Apper Holdings Ltd. v. 895453 Ontario Ltd.* [1996 CarswellOnt 440 (Ont. Gen. Div.)]:

> If the court is satisfied that a conveyance is made with intent on the part of the grantor to defeat, hinder, delay or defraud creditors and others, the parties to the conveyance (the grantor and the grantees) must show that it was made for good consideration and good faith and to a person (or persons) who was (or were) without notice or knowledge of the grantor's fraudulent intent. *Bank* of *Montreal v. Jory* (1981), 39 C.B.R. (N.S.) 30 (B.C. S.C.). Otherwise, the conveyance is void against creditors of the grantor.

122

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

289 The evidence reviewed above concerning the intent of Kimel/Annopol and Goldfinger applies equally to Farber's claim under the *FCA*. Based on that evidence, I find that they did not possess the intent "to defeat, hinder, delay or defraud creditors or others of their just and lawful actions, suits, debts, accounts, damages, penalties or forfeitures" as required by *FCA* s. 2.

Summary

290 For the reasons set forth above, I dismiss Farber's claim to set aside the $2.5 million payment to Goldfinger under the *APA* and *FCA* as pleaded in paragraphs III (a)(ii) and (c) of its Fresh as Amended Notice of Application.

E. The oppression claim under OBCA s. 248.

291 Next, Farber challenged the payment of $2.5 million to Goldfinger under the oppression provisions found in section 248 of the *Ontario Business Corporations Act*. Farber submitted that as trustee of Annopol it was a proper "complainant" under *OBCA* s. 248. Goldfinger contended that the court possessed the discretion to recognize a trustee as a complainant under *OBCA* s. 245(c), but it should not do so in the present case.

292 Where the bankrupt is a party to an impugned transaction, the court possesses the discretion to determine whether, in the circumstances of the particular case, the trustee is a proper person to act as a complainant.[123] In the *Olympia & York Developments* case, the Court of Appeal held that where it was likely the creditors of a bankrupt corporation would have been recognized as complainants for the purpose of challenging a transaction under *OBCA* s. 248, then it was proper to recognize the trustee of the bankrupt as a complainant "in effect on behalf of the creditors of" the bankrupt.[124] I will proceed with my analysis on the basis that Farber, as trustee of Annopol, has status as a "complainant" for purposes of *OBCA* s. 248.

293 The oppression remedy concerns the reasonable expectations of the stakeholders of a corporation and whether the corporation has acted in a way to violate those reasonable expectations by conduct which is "oppressive or that unfairly prejudiced" or "unfairly disregarded" those reasonable expectations.[125]

294 In its factum Farber framed the reasonable expectations it was advancing in the following terms:

> 77./ Applying these factors to the relationship between Annopol and its third-party creditors, the most basic reasonable expectations of those creditors are that:
>
> > (a) Annopol would not make payments to reproduce salaries or by way of equity distributions (or gratuitous payments) where: (i) Annopol's financial situation was such that it was not be able to repay creditors; or (ii) the payments would result in Annopol being unable to repay its creditors;
> >
> > (b) Annopol would pay stakeholders only in accordance with the relative priority of their claims against Annopol; and,
> >
> > (c) Annopol would not take steps or enter into agreements that would prejudice the company's ultimate ability to pay its creditors.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

295 I accept that creditors of a corporation possess a reasonable expectation that the company will not engage in conduct which runs afoul of the provincial preferences legislation or the preference/ transfer for undervalue provisions of the *BIA*. However, for the reasons set out above, I have concluded that the payment of $2.5 million by Annopol to Goldfinger did not run afoul of *BIA* s. 96, the *Assignments and Preferences Act* or the *Fraudulent Conveyances Act*. In reaching that conclusion I found that at the time of the payments neither Annopol/Kimel nor Goldfinger possessed the intent to defeat, hinder, delay or defraud creditors. I would rely on the same findings to conclude that Annopol's payment to Goldfinger did not violate the reasonable expectations of its creditors.

296 Although that part of Farber's argument seems duplicative of what it submitted under the *BIA*, *APA* and *FCA*, in its factum it put forth an additional submission:

> 84./ The payment of $2.5 million to Goldfinger could not possibly have been foreseen by Annopol's third-party creditors and there is nothing those creditors could have reasonably done to protect themselves from JLK and MLK causing Annopol to pay $2.5 million to Goldfinger.
>
> 85./ The detriment to Annopol's creditors caused by the $2.5 million payment is obvious. As a result of the $2.5 million payment, *Annopol was completely stripped of assets and incurred further debt in order to make a prohibited equity payment or distribution to Goldfinger*. The result has been the bankruptcy of Annopol and a significant loss to Annopol's creditors. By way of contrast, *Goldfinger recovered a $2.5 million equity payment*.

Farber argued that Goldfinger in fact was a shareholder of Annopol at the time the $2.5 million payment was made and that the payment constituted the re-purchase of his issued shares or the making of a capital dividend in contravention of *OBCA* ss. 30(2) and 38(3) which prohibit such actions where there are reasonable grounds to believe that the corporation is not solvent.

297 In December, 2007 and January, 2008, Goldfinger was not a shareholder of Annopol. He had not subscribed for any shares; Annopol had not issued any shares to him. As set out in paragraph 193 above, the two lawyers who acted for Goldfinger on the First Settlement never saw any share certificates issued to him by any of the Summit Glen group of companies. Also, Farber possessed the minute book for Annopol, which included a shareholder register, but it could not locate any share certificates or other documents which indicated that Goldfinger was a shareholder of Annopol. Although Goldfinger thought that under his arrangement with Kimel he would become a shareholder in many of the Summit Glen companies, that never came about.

298 It is true that each of the December, 2007 and January, 2008 cheques to Goldfinger bore the notation, "re-purchase of shares", but a notation on a cheque does not alter the state of a corporation's records or corporate treasury. Moreover, about six months after the $2.5 million payments were made, the First Settlement closed. As mentioned, in the First Settlement the parties acknowledged that no shares in the SG Companies (which did not include Annopol) had been issued to Goldfinger, but that for purposes of the settlement "Goldfinger is, and for all purposes shall be deemed to be, the legal and beneficial owner of 50% of the share capital of each of the Summit Glen Companies". Kimel then agreed to purchase Goldfinger's shares in the capital of the SG Companies (which did not include Annopol) for $5 million and, in respect of the payment of the Share Purchase Price, Goldfinger acknowledged "receipt prior to the execution of this Agreement of the sum of $2,500,000.00 on account of the Share Purchase Price". The SG Companies identified on Schedule 1 to the First Settlement consisted of those which owned properties. Given that the First Settlement agreement purported to be made as of December 11, 2007, but it was not executed until early June, 2008, its provisions concerning the purchase of Goldfinger's "deemed" shares in the SG Companies strongly suggest that the "repurchase shares" notation found on the cheques paid to him in December, 2007 and January, 2008 actually referred to the notional re-purchase of the deemed shares in the SG Companies, not to the re-purchase of Annopol shares.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

299 It follows that since Goldfinger was not a shareholder of Annopol at the time the $2.5 million was paid to him, those payments did not constitute the purchase of shares which had been issued to him nor the payment of a dividend. On the latter point, no corporation resolution declaring a dividend was placed in evidence.

300 Moreover, when one steps back and takes a look at the substance of what happened under the First Settlement, Goldfinger received the re-payment of $2.5 million of the funds which he had loaned to Kimel and his companies, as well as some additional security. None of the properties into which his loans had been placed had yet been redeveloped to the point where they could be sold and, according to the initial arrangement between Kimel and Goldfinger, profit or equity would not be extracted until the properties were resold. The business substance of the December, 2007 and January, 2008 payments was that Goldfinger received back some of the principal he had invested; there was no profit or equity yet available for distribution.

301 I would observe that Farber, through Baigel's August 15, 2012 affidavit, speculated that "the $2.5 million was intended to be in respect of Goldfinger's equity interest in Annopol", not the return of part of his shareholder loans. Yet, four paragraphs later in that affidavit Baigel referred to a November 20, 2007 memo to file by Goldfinger's lawyers of a meeting with their client that "if the 2.5 million dollars is paid, then 4 million dollars are outstanding on the shareholder loan". I have great difficulty understanding how a trustee could forcefully characterize a payment as a return of equity while at the same time relying, for other purposes, on a contradictory characterization of it as a repayment of a loan.

302 Finally, in its written and oral argument Farber occasionally intimated that Goldfinger could be considered the legal partner of Kimel. That position was inconsistent with the main thrust of Farber's argument that at material times Goldfinger was a shareholder in Summit Glen companies, including Annopol. The evidence does not support a finding that Goldfinger and Kimel were legal partners; instead, Goldfinger lent money to Kimel's companies on the expectation that upon the successful redevelopment of the properties his money would be repaid and he would share in the up-side of the projects. In the meantime, Goldfinger took no role in the management of the affairs of those companies. Their business understanding was not reduced to writing, so section 4 of the *Partnerships Act* does not apply.[126] And, finally, Farber has not attempted to recover from Goldfinger any of the investments made by third parties to SG companies on the basis that Goldfinger was liable as a partner in those real estate ventures.

303 For these reasons, I dismiss Farber's claims under *OBCA* ss. 130(4) and 248 as advanced in paragraphs II (e) and V (b) of its Fresh as Amended Notice of Application.

304 In its February 7, 2013 Factum Farber also advanced a claim sounding in unjust enrichment on the basis that the $2.5 million payments were a re-purchase of shares or equity distribution. For similar reasons, I dismiss that claim.

F. Farber's claim for the $2.5 million payment against Mahvash

305 Farber also sought repayment of the $2.5 million from Mahvash, in her capacity as a director of Annopol, on two grounds. First, Farber asserted that the payment contravened section 130 of the *OBCA*. Sections 130(2)(b), (d) and (f) provide that directors of a corporation who vote for or consent to a resolution authorizing a purchase, redemption or other acquisition of shares contrary to *OBCA* ss. 30, 31 or 32, a payment of a dividend contrary to section 38, or a payment to a shareholder contrary to section 248, are jointly and severally liable to restore to the corporation any amounts so distributed or paid and not otherwise recovered by the corporation. Since I have found that the payments to Goldfinger were not payments made under *OBCA* ss. 30 or 38 nor a payment to a shareholder contrary to section 248, this part of Farber's claim against Mahvash

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

fails. Moreover, there was no evidence that a meeting of Annopol's directors was held at which a resolution was passed regarding the $2.5 million payment or action taken in that regard, or that Mahvash was present at a meeting of Annopol's directors at which share purchase or dividend declaring resolutions were passed.[127]

306 Second, Farber argued that Mahvash, as a director, was a "person who was privy to the transfer" of $2.5 million to Goldfinger and therefore was liable to repay Annopol that amount under *BIA* s. 96(1). Since I have dismissed Farber's claim under *BIA* s. 96(1), it follows that its claim against Mahvash under that section as a privy also is dismissed.

307 For these reasons, I dismiss Farber's claim against Mahvash as pleaded in paragraph V (a) of its Fresh as Amended Notice of Application.

G. Summary in respect of the repayment of $2.5 million

308 By way of summary, for the reasons given above, I dismiss Farber's claims against Goldfinger and Mahvash for the return of the $2.5 million paid to Goldfinger by Annopol in December, 2007 and January, 2008.

XII. Claims in respect of the SG Brantford transactions

A. The history of the charges granted to Goldfinger on 176 Henry Street, Brantford

309 Summit Glen Brantford owned property at 176 Henry Street in Brantford. SG Brantford was adjudged bankrupt on May 27, 2010 as a result of an application for bankruptcy issued April 30, 2009. Farber was appointed trustee and eventually sold 176 Henry on August 31, 2010 for $3.6 million. According to the February 25, 2011 Statement of Affairs for SG Brantford, claims by secured creditors totaled $3.55 million, while unsecured claims amounted to $1.426 million. From the sale the SG Brantford estate received about $183,000 in net proceeds.

310 As disclosed in Schedule 2 to the First Settlement, as of June, 2008 the property at 176 Henry Street was subject to three existing mortgages: $2.85 million to First National Financial Corporation (June 7, 2007), $450,000 to Montor (November 16, 2005) and $750,000 to Annopol (December 20, 2005), or total of $4.05 million in charges registered against the property. Since those charges were listed on a schedule to the First Settlement, Goldfinger knew about them.

311 As part of the First Settlement, the SG Companies, which included SG Brantford, gave collateral mortgages over their properties as security for the payment of the Shareholder Loans and Share Purchase Price. On June 13, 2008, two charges granted by SG Brantford to Goldfinger were registered on title (the "Goldfinger 176 Henry Charges"); so, too, were two postponements granted by Annopol in favour of Goldfinger (the "Annopol 176 Henry Postponements").

312 About five months after the First Settlement, in November, 2008, the loan by First National Financial to SG Brantford secured by the first charge/mortgage came due. SG Brantford negotiated a re-financing with First National to renew and increase the loan by approximately $470,000 to be secured by a new charge/mortgage over 176 Henry.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

313 To close the re-financing with First National, SG Brantford required that Montor subordinate the Montor 176 Henry Charge to the new charge/mortgage to be provided to First National. While back in 2007 Montor had agreed to subordinate its charge to permit financing from First National, according to Farber its review of the books and records of Montor disclosed no agreement on its part to subordinate to First National's new security on the November, 2008 re-financing. Farber alleged that Kimel had forged Montor's signature on a subordination for the re-financing.[128]

314 On or about November 26, 2008, the re-financing with First National closed. SG Brantford paid $471,000 to Goldfinger and on that day the two Goldfinger 176 Henry Charges were discharged.

315 Just prior to that re-financing, on October 31, 2008, Goldfinger had started his action against Kimel and his companies, including SG Brantford. In that action Goldfinger alleged and deposed that SG Brantford had refused or neglected to pay obligations owing to him. On December 1, 2008, less than one week after the $471,000 was paid to Goldfinger, he obtained in his action against Kimel the appointment of Zeifman as interim receiver of SG Brantford pursuant to *BIA* s. 47.

B. The relief sought by Farber

316 In respect of SG Brantford, Farber, as trustee in bankruptcy of SG Brantford and Annopol, seeks relief in respect of the conduct of those companies which took place at two different points of time:

> (i) in respect of the First Settlement which closed on June 8, 2008, orders setting aside the security which Goldfinger received in respect of SG Brantford and 176 Henry: i.e, setting aside the two Goldfinger 176 Henry Charges, the two Annopol 176 Henry Postponements, as well as the guarantees given by SG Brantford to Goldfinger at that time; and,
>
> (ii) the repayment of the $471,000 paid by SG Brantford to Goldfinger on November 26, 2008 to discharge the Goldfinger 176 Henry Charges.

Accordingly, Farber seeks relief in respect of transactions which occurred in June and November, 2008. The date of bankruptcy of SG Brantford was May 27, 2010; the date of the initial bankruptcy event was April 30, 2009; both impugned transactions took place within one year prior to the date of the initial bankruptcy event.

A. Challenges to the First Settlement security granted to and in favour of Goldfinger

317 Farber seeks to set aside the Goldfinger 176 Henry Charges and the SG Brantford guarantees on three grounds: (i) as a transfer at undervalue under *BIA* s. 96; (ii) under the *APA*; or, (iii) under the *FCA*. Farber seeks to set aside the Annopol 176 Henry Postponements under *OBCA* s. 248.

318 Farber submitted that the grant of the charges on 176 Henry constituted "dispositions of property" within the meaning of the definition "transfer at undervalue". Goldfinger did not address this point. This Court has held that the definition of "transfer" should be interpreted liberally and in a purposive manner.[129] While I query whether a charge and guarantee fall within the ambit of a "disposition of property", especially given that *BIA* s. 95(1) distinguishes a "transfer of property" from a

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

"charge on property", in light of Goldfinger's lack of opposition to Farber's position on this point, I am prepared to proceed on the basis that the granting of the charge and guarantee fell within *BIA* s. 96(1).

319 Previously I found that Goldfinger was at arm's length from Kimel and his companies. In the present case, the First Settlement closed less than one year prior to the date of the initial bankruptcy event.

320 Was SG Brantford insolvent at that time or rendered insolvent by the transfers? The unaudited, notice to reader financial statements for SG Brantford for the year ended September 30, 2007 showed liabilities ($3.908 million) exceeding assets ($3.687 million), with gross revenue ($421,000) falling below operating expenses ($526,690). Those for the year ended September 30, 2008, showed liabilities ($3.940) exceeding assets ($3.548), again with revenue ($424,231) falling short of expenses ($595,254). The December 17, 2008 First Report of the Receiver, Zeifman, reported that SG Brantford was operating on a cash deficit basis.

321 Under the First Settlement, the SG Companies, which included SG Brantford, each granted collateral mortgages to Goldfinger in the amounts of $1.5 million to secure payment of the Share Purchase Price and $6.5 million to secure payment of the Shareholder Loans. Schwebel, Goldfinger's lawyer on the First Settlement, acknowledged that the aggregate amount of all mortgages registered against 176 Henry following the closing of the First Settlement exceeded the value of the property.[130]

322 That said, two pieces of evidence could suggest that on a going-concern basis SG Brantford was not insolvent at the time. First, in the SG Brantford bankruptcy Farber, as trustee of Montor, filed a proof of claim in respect of which the last payment made by Montor to SG Brantford was one in the amount of $450,000 made on August 14, 2008, two months after the closing of the First Settlement. Perelmuter, however, testified that at the time he did not know about the First Settlement.

323 Second, Goldfinger pointed out that the $471,000 paid to him came from the First National refinancing, an event, he argued, which would not have occurred had SG Brantford been insolvent. As a result of the discharge of the Goldfinger 176 Henry Charges in November, 2008, it may well be that the secured liabilities of SG Brantford did not exceed the value of the property, its sole asset. Indeed, Farber realized a small net profit on the eventual sale of the property.

324 Nevertheless, the evidence disclosed that on a balance sheet basis, SG Brantford was insolvent at the time it granted the Goldfinger 176 Henry Charges and made the guarantees.

325 However, for the reasons previously set out in paragraphs 274 to 280 above, I find that at the time of the closing of the First Settlement Kimel and his signatory companies, which included SG Brantford, did not intend to defraud, defeat or delay creditors. Accordingly, Farber's claim under *BIA* s. 96(1) fails.

326 Similarly, in respect of Farber's claims founded on the *APA* and *FCA*, I previously concluded in paragraphs 274 to 280 above that neither Kimel nor his companies, nor Goldfinger, intended to defeat, hinder, delay or defraud creditors by making the $2.5 million payment which formed part of the First Settlement. The evidence in support of that conclusion also supports a finding that the granting of the security from SG Brantford to Goldfinger as part of the First Settlement was not done by Kimel/SG Brantford (or Goldfinger) with the intent to defeat, hinder, delay or defraud creditors. Accordingly, Farber's claims under the *APA, FCA* and *BIA* s. 96 fail.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

327 I would rely on the same findings to conclude that Annopol's subordination of its security to Goldfinger as part of the First Settlement did not violate the reasonable expectations of its creditors and therefore no remedy under *OBCA* s. 248 is justified.

328 For those reasons, I would dismiss the claims pleaded by Farber in paragraphs II(b),(c)(i) and (ii), (d), III (b) and IV (b) of its Fresh as Amended Notice of Application as they relate to Annopol and the grant by SG Brantford of the Goldfinger 176 Henry Charges and guarantees.

B. Challenge to the November 26, 2008 payment to Goldfinger

329 In order to re-finance with First National in November, 2008, SG Brantford had to deal with the other mortgages on title which, in order of priority, were Montor, Goldfinger and Annopol. In the result, Goldfinger was paid $471,000 from the re-financing to discharge both the Goldfinger 176 Henry Charges, Annopol subordinated to First National, as did Montor, although the circumstances surrounding its subordination require special attention.

330 Farber seeks to set aside the payment of $471,000 to Goldfinger under *BIA* s. 96(1), the *APA* and the *FCA*. The evidence I relied upon to find that SG Brantford was insolvent at the time of the First Settlement in June, 2008, also supports a finding that SG Brantford was insolvent, on a balance sheet basis, on November 26, 2008.

331 I have found that the Goldfinger 176 Henry Charges did not offend *BIA* s. 96(1), the *APA* or the *FCA*. SG Brantford paid Goldfinger the $471,000 pursuant to, and in order to discharge, that security. The face amounts of those charges greatly exceeded $471,000.[131] Consequently, I give no effect to Farber's argument that the payment constituted a transfer at undervalue. In my view, the appropriate focus of the analysis should be on the *APA, FCA* or *OBCA* s. 248.

332 Section 4 of the *APA* does not apply to this payment of money because section 5(1) of the *APA* provides that section 4 does not apply "to any payment of money to a creditor". As noted earlier, any payment of money to a creditor, whether or not the payment is intended to prefer the creditor and defeat other creditors, is protected under s. 5(1) of the *APA*.[132] Under the terms of the First Settlement, SG Brantford had agreed to pay certain sums to Goldfinger. By signing the First Settlement, both Goldfinger and SG Brantford acknowledged that Goldfinger was a creditor of SG Brantford. I so find, notwithstanding that the evidence suggested that the allocation of Goldfinger's investment funds against various properties set out in the settlement agreement was derived by his lawyers at Minden Gross and he did not verify whether the allocation numbers were accurate.[133]

333 That leaves the *FCA* and *OBCA* s. 248.[134] In terms of the *FCA*, I conclude that the payment by SG Brantford to Goldfinger of $471,000 in preference to the payment of that amount to Montor, a chargee which stood in priority to Goldfinger, violated *FCA* s. 2 and was not saved by *FCA* s. 3.

334 I reach that conclusion because the evidence regarding the intent of both Kimel/SG Brantford and Goldfinger as of November 26, 2008 differed materially from the state of affairs prevailing on June 8, 2008, at the time of the First Settlement. More specifically:

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(i) Goldfinger deposed that no sooner had Kimel entered into the 2008 Settlement, than he breached it, in large part by dealing improperly with properties which formed part of the settlement — i.e. SG Trayvan gave a $4 million mortgage to Community Trust Company, and soon after Kimel sold the SG Fairway property;

(ii) In July, 2008, Goldfinger made demands for payment on SG Brantford and SG Bridge, as well as others, and delivered notices pursuant to *BIA* s. 244 to those companies;

(iii) In the late summer and early fall of 2008 Goldfinger negotiated agreements with Kimel under which he gained rights to control the business of SG Brantford;

(iv) On October 31, 2008, Goldfinger commenced an action seeking damages and the appointment of a receiver over a number of SG companies, including SG Brantford and SG Bridge;

(v) On November 4, 2008, Goldfinger swore an affidavit in his action in which he deposed that the defendants had refused to pay the amounts demanded and that Kimel had advised he would no longer provide funds to operate the properties, including 176 Henry Street and 70 Bridge Street; and,

(vi) On November 26, 2008, Goldfinger moved in his action to appoint Zeifman as interim receiver of several SG companies, including SGW, SG Brantford and SG Bridge.

In sum, as of November 26, 2008, Goldfinger knew that Kimel and his companies, including SG Brantford, had defaulted on their obligations to him and were refusing to pay him. Goldfinger had commenced legal process to pursue his remedies.

335 As of November 26, 2008, Goldfinger also knew that Montor held a mortgage in the amount of $450,000 on 176 Henry Street in priority to his own, and he was aware that there were not sufficient funds to pay the Goldfinger 176 Henry Charges if the Montor 176 Henry Charge was paid from the proceeds from the First National re-financing. As stated at trial by Carl Schwebel, one of Goldfinger's lawyers at the time, when asked about his client's state of knowledge about the consequences of the payout:

Q. So, there was not sufficient proceeds from the refinancing to pay Dr. Goldfinger. If you had to refinance First National, you had to pay Montor, there wouldn't be enough to pay Dr. Goldfinger.

A. The Dale & Lessmann requisition letter that I was given said that it was an open question whether Montor's mortgage would be discharged or postponed. If the mortgage was going to be — if the Montor mortgage was going to be paid out, then there was not money to pay out the Goldfinger mortgages.

Q. And was Dr. Goldfinger aware of that?

A. Yes.[135]

Since Goldfinger knew that state of affairs, it is reasonable to draw the inference that Kimel did as well, and I so find.

336 Schwebel was also asked about Goldfinger's understanding of the priority of the Montor mortgage at the time of the re-financing:

Q. Do you have any knowledge with respect to the subordination of Montor's charge at that point in time?

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

A. I — I understood at the time of closing that Montor had subordinated its charge.

Q. Did you see a copy of the subordination?

A. Not at the time of the closing, not prior to the closing.

Q. At the closing, who delivered the subordination; do you recall?

A. I — I don't know. It would have involved Dale & Lessmann and Mr. — the company — Mr. Kimel's companies' lawyers.[136]

337 In a 2010 affidavit Kimel had deposed that he did not tell Montor's principal, Perelmuter, about the $471,000 payment before it was made.[137]

338 While Farber submitted that Kimel had forged Montor's signature on its postponement of charge to First National, there is insufficient evidence to make such a serious finding of fact. The evidence does support a finding, however, that the Montor postponement was signed by Kimel purporting to act as the Secretary-Treasurer of Montor, and that Montor's sole shareholder, Perelmuter, was not aware that part of the proceeds of the First National refinancing would be paid to a junior secured party and Kimel deliberately refrained from disclosing that fact to Perelmuter. At a minimum, Montor's postponement of its charge resulted from Kimel/SG Brantford deliberately misrepresenting the true state of affairs to Montor and, I find that Kimel/SG Brantford did so in order to defeat, hinder, delay or defraud Montor of its just and lawful debts.

339 I further find that Goldfinger had notice or knowledge of that intent within the meaning of *FCA* s. 3. As a result of events since the closing of the First Settlement, Goldfinger knew that Kimel/SG Brantford had defaulted on their obligations to him and did not intend to pay him, and he knew as well that not only did Montor stand in priority to his charge, but the re-financing would not generate sufficient funds to pay out both Montor and himself. Given that state of affairs, it is reasonable to find, as I do, that Goldfinger knew that the payment of the $471,000 to him would prefer his interests over those of Montor. I therefore find that Goldfinger sought and obtained the payment of the $471,000 to him with the intent to defeat, hinder, delay or defraud another creditor, Montor.

340 I therefore declare void the November 26, 2008 payment of $471,000 from SG Brantford to Goldfinger, and I order Goldfinger to repay that amount to Farber, in its capacity as trustee in the bankruptcy of SG Brantford. Farber stated, in paragraph 31 of its February 8, 2013 Factum, that in the event Goldfinger was ordered to repay that money, he could file a claim in the SG Brantford bankruptcy proceeding in accordance with the *BIA*.

341 I would have reached a similar result under *OBCA* s. 248. A secured creditor, such as Montor, reasonably expects that if its consent is requested for the postponement of its security to that of another, the borrower seeking the postponement will make full and fair disclosure about all material circumstances concerning the reasons for the request, including the effect that the postponement would have on the secured position of the postponed party. It is clear Kimel did not make such disclosure to Montor, and Kimel was the directing mind of SG Brantford. For this reason, I find that such non-disclosure effected an oppressive result on Montor, as a creditor of SG Brantford, and the appropriate remedy, given Goldfinger's knowledge of the consequences of the transaction on Montor, is to order him to repay the $471,000 to Farber in its capacity as the trustee in bankruptcy of SG Brantford.

342 Consequently, I grant the relief sought by Farber in respect of the $471,000 payment to Goldfinger sought in

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

paragraphs II(b), (c), (f) and III(b) of its Fresh as Amended Notice of Application.

XIII. Claim in respect of SG Bridge

343 Summit Glen Bridge Street Inc. owned property located at 70 Bridge Street, Kitchener. SG Bridge is not bankrupt. Kimel and Mahvash are the sole officers and directors of SG Bridge. SG Bridge's only asset was 70 Bridge, which was a vacant piece of land that generated no revenue. Zeifman, the interim receiver, sold property in August, 2009. After the payment of Zeifman's professional fees and the uncontested charges/mortgages registered against the property, there was a surplus of approximately $280,000 — the Bridge Surplus.

344 On May 6, 2005, prior to the First Settlement, SG Bridge had granted a $750,000 charge in favour of Annopol.[138] The charge's "Additional Provisions" section provided, in part, as follows:

> This Charge shall secure the aggregate of all present and future indebtedness and liabilities of the Chargor to the Chargee (direct or indirect, absolute or contingent, matured or not, wheresoever and however incurred as principal or surety, whether incurred alone or with another or others, and whether arising from dealings between the Chargee and the Chargor or from other dealings or proceedings by which the Chargee may become a creditor of the Chargor) including without limitation the outstanding balance of the Principal Amount advanced to the Chargor from time to time, interest thereon at the Interest Rate and all other present and future indebtedness and liabilities of the Chargor to the Chargee payable under or by virtue of the Charge.

According to Farber, between September 13, 2005 and November 21, 2008, Annopol loaned the net amount of $211,550 to SG Bridge.

345 As part of the First Settlement SG Bridge granted Goldfinger charges over 70 Bridge — a $6.5 million charge and a $1.5 million charge - as collateral security for the obligations to pay the Shareholder Loans and Share Purchase Price (the "Goldfinger 70 Bridge Charges"). As well, Annopol subordinated its $750,000 mortgage on 70 Bridge to Goldfinger's charges. Schedule 3 to the First Settlement stipulated that the parties agreed SG Bridge owed Goldfinger $1,011,027 in Shareholder Loans.

346 Chaitons LLP provided Zeifman with a February 23, 2010 opinion on the validity of the Goldfinger 70 Bridge Charges Subject to the standard qualifications and exceptions, Chaitons opined that both charges were validly and properly registered against title to the property.

347 In respect of the mortgage SG Bridge had granted to Annopol, Kimel testified:

> 406. Q. Mr. Shea showed you a mortgage from Summit Glen Bridge to Annopol for $750,000 dated May 6th, 2005, do you remember?
>
> A. I do.
>
> 407. Q. And that's just like all the other $750,000 mortgages in that no monies were advanced under that mortgage,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

correct?

A. That's correct.[139]

That mortgage covered future indebtedness, and Farber filed reports which stated that SG Bridge owed a net amount to Annopol of at least $211,000.

348 A dispute exists about whether Goldfinger or Annopol is entitled to the Bridge Surplus. The dispute turns on whether the Goldfinger 70 Bridge Charges and the Annopol Subordinations are valid or voidable. No process was put in place by Ziefman to determine the validity of Goldfinger's claim to the Bridge Surplus which presently is held in an RBC bank account for the benefit of counsel for the parties. Farber seeks the following relief:

(i) to set aside the Goldfinger 70 Bridge Charges and the guarantees granted by SG Bridge to Goldfinger as part of the First Settlement;

(ii) to set aside subordinations by Annopol of its charge over 70 Bridge as part of the First Settlement; and,

(iii) to determine entitlement to the surplus from the sale of 70 Bridge.

349 SG Bridge is not bankrupt. The *BIA* does not apply. Farber seeks to set aside or declare void the Goldfinger 70 Bridge Charges either under (i) the *FCA* or (ii) the *APA*. As well, it seeks to set aside the Annopol subordinations regarding 70 Bridge under *OBCA* s. 248.

350 The unaudited financial statements of SG Bridge for the year ended September 30, 2007, showed that liabilities (($1.223 million) slightly exceeded assets ($1.021 million), and that revenues (Nil) exceeded expenses ($24,364). Zeifman, in its December 17, 2008 First Report stated that SG Bridge was operating on a cash deficit basis.

351 Since the claims Farber asserts in respect of the package of security Goldfinger received for 70 Bridge as part of the First Settlement mirror the claims it asserted under the *APA*, *FCA* and *OBCA* s. 248 in respect of the package of security granted by SG Brantford as part of the First Settlement, it follows that the analysis I undertook in respect of the SG Brantford-related security applies with equal force to the SG Bridge-related security. I therefore dismiss Farber's claims to set aside the Goldfinger 70 Bridge Charges, the guarantees granted by SG Bridge and the Annopol subordinations in respect of 70 Bridge, all as pleaded in paragraphs II(b), (c), (d), (g) and III (a) and (d) of its Fresh as Amended Notice of Application.

XIV. Summary and costs on the Claims Motion and Preferences Application

A. Summary of orders on the Claims Motion

352 For the reasons set out above, I make the following orders in the Claims Motion:

Montor claim

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(i) The secured claim of Montor in the amount of $500,000 is allowed, together with interest until the date of payment in accordance with the terms of the loan;

(ii) An unsecured claim of Montor in the amount of $25,000 is allowed, together with interest until the date of payment in accordance with the terms of the loan;

Annopol's First Proof of Claim

(iii) In respect of Annopol's First Proof of Claim, its secured claim of $100,000 is allowed, together with interest until the date of payment in accordance with the terms of the loan;

(iv) In respect of the unsecured portion of Annopol's First Proof of Claim, I require submissions from the parties on the issue of whether all or part of Annopol's unsecured claim is statute-barred on the following timetable:

a. Farber may serve and file brief written submissions, together with any authorities, no later than November 30, 2013;

b. Goldfinger may serve and file brief responding written submissions, together with authorities, no later than January 15, 2014; and,

c. Farber may file brief reply submissions no later than January 22, 2014.

Annopol's Second Proof of Claim

(v) I disallow Annopol's Second Proof of Claim for a secured claim in the amount of $750,000.

SGG's debt claim

(vi) In respect of SGG's Debt Claim against SGW, I require submissions from the parties on the issue of whether all or part of the $16,500 claim is statute-barred:

a. Farber may serve and file brief written submissions, together with any authorities, no later than November 30, 2013;

b. Goldfinger may serve and file brief responding written submissions, together with authorities, no later than January 15, 2014; and,

c. Farber may file brief reply submissions no later than January 22, 2014.

SGG's unjust enrichment claim

(x) In respect of SGG's unjust enrichment claim against SGW:

a. Farber shall provide Goldfinger with any evidence to deal with the deficiencies in its unjust enrichment claim which I identified no later than November 30, 2013 and file with the Court, to my attention, a report dealing with that issue;

b. Goldfinger shall file any further submissions on this issue no later than January 15, 2014, with such submissions not to exceed 10 pages;

(iv) Further, I require submissions from the parties on whether any part of this claim may be statute-barred on the following timetable:

a. Farber may serve and file brief written submissions, together with any authorities, no later than November 30,

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

2013;

b. Goldfinger may serve and file brief responding written submissions, together with authorities, no later than January 15, 2014; and,

c. Farber may file brief reply submissions no later than January 22, 2013.

183's Proof of Claim

(xi) I allow 183's proof of claim in respect of the CTC $50K Charge to the extent of $50,000, together with interest until the date of payment in accordance with the terms of the loan. As to the balance of that claim:

a. 183 shall provide Farber, as trustee of SGW, with the further evidence previously requested in respect of the additional items claimed for the CTC $50K Charge no later than November 30, 2013 and file that evidence with the Court;

b. Farber shall file with the Court, to my attention, no later than December 24, 2013, a further report providing its views about the sufficiency of the further evidence provided and its position on the amounts claimed in light of that further evidence; and,

c. 183 shall file any further submissions on this issue no later than January 15, 2014, with such submissions not to exceed 10 pages;

(v) I allow 183's claim in respect of the CTC $500K Charge, with interest until the date of payment in accordance with the terms of the loan;

Goldfinger's constructive trust claim

(vi) I dismiss Goldfinger's constructive trust claim.

Goldfinger's claim for the distribution of surplus funds to him as shareholder

(vii) No order shall be made at this time regarding a distribution to Goldfinger of any surplus in the SGW estate in his capacity as the sole shareholder of SGW. I am seizing myself of all court proceedings involving the SGW estate, and I require counsel to appear before me on a 9:30 appointment before the end of November, 2013, to report on what further steps remain in the administration of this estate.

B. Summary of orders on the Preferences Application

353 By way of summary, I make the following orders in the Preferences Application:

(i) The November 26, 2008 payment from SG Brantford to Goldfinger is set aside, and Goldfinger shall pay to Farber, in its capacity as the trustee in bankruptcy of SG Brantford, the sum of the $471,000; and,

(ii) In all other respects, the Preferences Application is dismissed.

C. Costs

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

354 In respect of the matters on which further submissions are to be made, I shall release supplementary reasons by February 14, 2014, and I defer the scheduling of cost submissions until that time.

XV. Motion by Goldfinger's trial counsel for a charging order

A. Background and position of the parties

355 Several months after the conclusion of the trial, counsel for Goldfinger, 1830994 Ontario Limited and Goldfinger Jazrawy Diagnostic Services Ltd. ("Diagnostic"), the Davis Moldaver LLP firm, moved for a charging order against any proceeds or monies payable to any of Goldfinger, 183 and Diagnostic in the Claims Motion or Preferences Application, together with an order removing the firm as lawyers of record in the Claims Motion. The Davis Moldaver firm had acted for Goldfinger in five proceedings, including the Claims Motion and Preference Application. Notices of changes of lawyers ultimately were served by Goldfinger in all proceedings.

356 About a week after the conclusion of final submissions in the Preferences Application, Goldfinger issued a notice of action against the Davis Moldaver firm and subsequently issued a statement of claim alleging professional negligence in regards to legal services provided by the firm in 2009 and 2010. The plaintiffs seek damages of $8 million. Goldfinger's claim has nothing to do with the services the Davis Moldaver firm provided in these proceedings, but alleges that the Davis Moldaver firm failed to inform Goldfinger that he enjoyed potential causes of action against the Minden, Gross firm in respect of services they had provided Goldfinger relating to the implementation of the First Settlement. Their client's commencement of an action against them placed the Davis Moldaver firm in a conflict and they could no longer act for Goldfinger.

357 According to the evidence filed, a significant amount remains unpaid on accounts rendered by Davis Moldaver to Goldfinger (the "Unpaid Amount"). Consequently, Davis Moldaver seeks a charging order over the interest of Goldfinger, 183 and Diagnostic in the proceeds of the Claims Motion and Preferences Application. Goldfinger deposed that he had already paid the Davis Moldaver firm far more than the Unpaid Amount in fees for the two proceedings, and he thinks the fees invoiced have been excessive. Goldfinger intends to assess his former lawyer's accounts.

358 Goldfinger acknowledged that Davis Moldaver was entitled to a charging order, but submitted that such an order should be subject to several conditions:

(i) First Condition: the order would be without prejudice to his rights to assess the invoices rendered by Davis Moldaver;

(ii) Second Condition: the order would be without prejudice to his rights to pursue any claims against Davis Moldaver;

(iii) Third Condition: Davis Moldaver be required to provide him with a copy of all his files in the five proceedings; and,

(iv) Fourth Condition: any monies which might become the subject matter of a charging order would be paid into Court or a solicitor's trust account pending assessment of the invoices

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

359 Davis Moldaver agreed with the First and Second Conditions. The firm opposed the Third Condition, arguing that its solicitor's lien over the files should only be lifted in the event the clients' rights were in jeopardy and no such jeopardy or prejudice existed in this case because the trial had been completed. As to the Fourth Condition, the firm contended that any recovery under the charging order should be paid to the lawyers, with the lawyers under an obligation to repay the client any amounts determined through the assessment process. Davis Moldaver noted that Goldfinger had not made any effort to pay the outstanding accounts; on the contrary, Goldfinger has stated he refuses to pay them.

360 In response, Goldfinger submitted that potential prejudice could arise in these proceedings if copies of the files were not turned over because cost submissions would be required and there might be an appeal. Also, he argued that the other three files remained active, with some steps scheduled for November or December, although details were not provided.

361 I would note that as a result of directions given in these Reasons in the Claims Motion, Goldfinger may wish to make further submissions on some issues.

B. Analysis

362 Goldfinger acknowledged that a charging order should issue. What amounts will such an order likely charge? In the Claims Motion, I have found that the claim filed by 183 should be allowed, in large part, with an opportunity to provide further information on specified points. 183 therefore will recover at least $550,000 from the proceeds of the sale of 105 University. On the other hand, in the Preferences Application, I have ordered Goldfinger to repay the $471,000 received from SG Bridge in November, 2008. So, while the charging order may well have some value, it most likely will fall short of the Unpaid Amount claimed by Davis Moldaver. In other words, the charging order will have some value as security for amounts unpaid, but most likely will not provide full security.

363 When a client discharges a lawyer without just cause, the lawyer may exercise a lien for fees over the documents in his possession, and the lawyer may retain the file material until he is paid, subject to the court's jurisdiction to interfere with the exercise of the lien, without actually nullifying it, to protect the interests of third parties.[140]

364 In the present case Davis Moldaver was entitled to assert a solicitor's lien. It had no choice but to get off the record because its client had sued the firm. Since the charging order most probably will not provide sufficient security to cover the Unpaid Amount, Davis Moldaver is entitled to some continuation of its solicitor's lien. Under Rule 15.03(5) of the *Rules of Civil Procedure* the Court may impose such terms as are just in connection with the lien.

365 In the present case, Goldfinger has made no effort to satisfy the Unpaid Amount. The evidence filed by the parties did not disclose what, if any, work remained to be done on the three other proceedings. Until he started the new action against Davis Moldaver, Goldfinger had been making payments almost every month to that firm in the range of $20,000 to $25,000; this is not a case where the client is impecunious.

366 In these two proceedings, Goldfinger enjoys the right to make further submissions on aspects of the Claims Motion, as well as making submissions on costs. The further submissions in the Claims Motion concern the following issues:

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(i) securing and adducing any evidence to support the expenses claimed on the CTC $50K Charge;

(ii) responding to any additional information Farber provides in respect of the SGG unjust enrichment claim; and,

(iii) making submissions on what, if any, limitations period issue exists in respect of Annopol's unsecured claim against SGW and SGG's unjust enrichment claim against SGW.

367 I think fairness requires that the solicitor's lien be lifted to the extent of requiring Davis Moldaver to deliver to Goldfinger those portions of its files dealing with the documentation relating to those three issues. The parties provided me with an electronic copy of the entire trial record, so the delivery to Goldfinger of the ordered materials should not require much in the way of time or expense to effect.

368 At the same time, fairness requires a *quid pro quo* because Goldfinger has not made any payments against the Unpaid Amount and he precipitated the present difficulty when he started the new action against Davis Moldaver. In light of the solicitor-client confidences contained in the motion records for the charging order, I am not prepared to disclose the amount of the Unpaid Amount. However, given the discrete and limited nature of the remaining liability issues on which submissions may be made, I conclude that requiring Goldfinger to pay Davis Moldaver the sum of $40,000 against the Unpaid Amount, without prejudice to any right he may enjoy to assess that firm's accounts, would constitute a reasonable and proportionate condition for lifting the lien to that extent to enable Goldfinger, or his new counsel, to deal with the remaining issues.

369 Although Goldfinger also may make submissions on costs, I am not prepared to lift the lien any further without Goldfinger making a substantial further payment against the Unpaid Amount. Goldfinger possesses the invoices from the Davis Moldaver firm which describe the work they performed in these two proceedings. To the extent he requires the assistance of his trial counsel to understand and respond to any cost submissions made by Farber, it was Goldfinger's conduct in initiating action against Minden Gross and Davis Moldaver which has deprived him of his trial counsel's assistance. In those circumstances, I see no basis for the court to interfere any further with the solicitor's lien.

370 Finally, I am not prepared to alter the normal working of a charging order so that any net funds recovered in the Claims Motion and Preferences Application be paid into court or to a person satisfactory to both client and solicitor. Goldfinger does not complain about how Davis Moldaver handled both proceedings, although following their conclusion he has complained about the overall quantum of fees. From the record before me, no such complaint was made prior to the completion of the trials. Accordingly, the normal course shall prevail, and any net funds attached by the charging order shall be paid to Davis Moldaver.

C. Conclusion on charging order motion

371 By way of summary, I grant the motion by Davis Moldaver LLP for a charging order on the following terms and conditions:

(i) the order is without prejudice to any rights which Goldfinger, 183 and Diagnostic may enjoy to assess the invoices rendered by Davis Moldaver;

(ii) the order is without prejudice to any rights which Goldfinger, 183 and Diagnostic may enjoy to pursue any claims against Davis Moldaver; and,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(iii) upon the payment to them by Goldfinger of the sum of $40,000, Davis Moldaver shall deliver to Goldfinger, or to his direction, those portions of its files dealing with the documentation relating to the following issues in the Claims Motion on which Goldfinger/183 may make further submissions:

a. the securing and adducing of any evidence to support the expenses claimed on the CTC $50K Charge;

b. responding to any additional information Farber provides in respect of the SGG unjust enrichment claim against SGW; and,

c. making submissions on what, if any, limitations period issue exists in respect of Annopol's unsecured claim against SGW and in respect of SGG's unjust enrichment claim against SGW.

I also order that the motion materials for the charging order motion be sealed and they shall not be opened without an order from this Court.

372 There shall be no costs of the motion.

Order accordingly.

Footnotes

1 Goldfinger testified that his loans were made to "the general enterprise of Jack to rehabilitate buildings", and he did not expect specific companies to pay him back specific advances: Transcript of Goldfinger November 14, 2012 cross-examination, Q. 307.

2 In his November 4, 2008 affidavit Goldfinger talked about making a demand on Kimel in 2007 for the repayment of his "shareholder loans" (para. 24).

3 Trial Transcript, October 10, 2012, pages 13 and 14.

4 Goldfinger November 4, 2008 Affidavit, para 6.

5 Farber Factum, Preferences Application, para. 29.

6 Transcript of cross-examination of Morris Goldfinger, April 25, 2012, Q. 100.

7 Transcript of cross-examination of Kimel, November 12, 2012, Q. 189.

8 Trial transcript, October 10, 2012, p. 58.

9 Transcript of the cross-examination of Goldfinger, November 14, 2012, Q. 335; Goldfinger November 4, 2008 Affidavit, para 3.

10 Goldfinger September 27, 2010 affidavit, paras. 96 to 99.

11 2010 SKQB 182 (Sask. Q.B.).

12 See Goldfinger affidavit, July 18, 2012, paras. 23 through 26.

13 October 10, 2012 Trial Transcript, pp. 111-112.

14 Kimel testimony, October 10, 2012 Trial Transcript, p. 112.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

15 Trial Ex. 9.

16 Trial Ex. 11.

17 October 10, 2012 Trial Transcript, p. 116.

18 October 10, 2012 Trial Transcript, p. 117.

19 Transcript of the September 19, 2012 examination of Jack Perelmuter, Q. 210.

20 Perelmuter transcript, Q. 213.

21 Affidavit of Michael Baigel (Farber) sworn June 25, 2010, para. 7.

22 SGW's March 31, 2006 and 2007 unaudited financial statements, in the "liabilities" section of the balance sheet, recorded "mortgages payable" of $1.050 million, which I find referred to the amounts payable under the CTC and Montor mortgages.

23 October 10, 2012 Trial Transcript, p. 122.

24 *Quick Credit v. 1575463 Ontario Inc.*, 2010 ONSC 7227 (Ont. S.C.J.), para. 20; aff'd 2012 ONCA 221 (Ont. C.A.); *Bank of Montreal v. Bonner*, [1988] B.C.J. No. 115 (B.C. S.C.)

25 These were also filed by Farber in its January 18, 2011 Report.

26 Transcript of cross-examination of Martin Cyr, April 27, 2012, Q. 60.

27 October 11, 2012 Trial Transcript, p. 19 and Exhibit 14. Farber, at pp. 10-12 of its October 5, 2012 Answers to Questions, provided a detailed description of the business conducted by Annopol and the properties it had owned.

28 Farber, August 17, 2012 Brief of Documents, Vol. 3, Tab 21H.

29 To complicate matters, in a way which only Kimel seemed capable of doing, the evidence contained an April 14, 2000 Trust Declaration to the effect that the Annopol $750,000 Charge "represents funds totally advanced to Annopol Holdings by Morris Goldfinger and is being held in Trust strictly and solely by Annopol Holdings for Morris Goldfinger". Goldfinger knew nothing about the mortgage until 2007 and in this proceeding he did not assert a claim for himself under that mortgage.

30 This position was repeated in Farber's June 25, 2012 Report.

31 October 11, 2012 Trial Transcript, pp. 36-37.

32 *Ibid.*, p. 38.

33 *Ibid.*, p. 63.

34 As to his plan to protect his family's equity in 105 University, see Kimel's evidence at trial, October 10, 2012, pp. 31 to 33.

35 Farber's January 18, 2011 Report made no mention of any advances by Annopol to SGW at the time of the Annopol $100K Charge.

36 These were also filed by Farber in its January 18, 2011 Report.

37 Farber Brief of Documents, June 25, 2012, Volume 1, Tab 3.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

38 Transcript of the cross-examination of Martin Cyr, April 27, 2012. I appreciate that the cross-examination took place in the context of a motion to remove Farber as trustee by reason of conflicts of interest, but I find it unusual that a trustee would refuse to disclose information to support a filed proof of claim.

39 October 10, 2012 Trial Transcript, pp. 16 and 17.

40 *Ibid.*, pp. 20-22.

41 *Ibid.*, pp. 28-29.

42 *Ibid.*, p. 52.

43 *Ibid.*, pp. 72-73.

44 *Ibid.*, p. 56.

45 *Ibid.*, p. 60

46 *Ibid.*, pp. 74 and 75.

47 *Ibid.*, pp. 98-99.

48 October 11, 2012 Trial Transcript, pp. 9-10

49 See, for example, the Annopol (Kimel) letter to Ronel Srubiski, December 21, 2007, Brief of Exhibits from Cross-examination of Jack Lechcier-Kimel, Tab 16; also, Trial Exs. 14, 15, 16 and 17.

50 Farber Answers to Questions, October 5, 2012, Vol. 3, Tab 20.

51 October 11, 2012 Trial Transcript, pp. 11-12.

52 Goldfinger, Yellow Exhibit Brief, Tab 2.

53 Transcript of Perelmuter examination conducted September 19, 2012, Q. 265.

54 2001 CarswellOnt 568 (Ont. S.C.J.), aff'd 2002 CarswellOnt 424 (Ont. C.A.).

55 Farber Claims Motion Factum, paras. 79 *et seq*.

56 See the cases digested in Houlden, Morawetz and Sarra, *The 2013 Annotated Bankruptcy and Insolvency Act*, G§47. The conflicting interests represented by Farber as a result of it wearing many hats evidently resulted in Farber, as trustee of SGW, failing to put forth arguments dealing with limitation periods, an omission which should not have occurred given the duties of a trustee in bankruptcy.

57 The applicable limitation period is set out in the *Real Property Limitations Act*, R.S.O. 1990, c. L.15.

58 October 11, 2012 Trial Transcript, p. 39.

59 *Ibid*, p. 42.

60 Farber Priorities' Factum, paras. 91 to 95.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

61 *Garland v. Consumers' Gas Co.*, [2004] 1 S.C.R. 629 (S.C.C.), para. 30.

62 *Ibid.*, para. 31.

63 *Ibid.*, paras. 44 to 46.

64 Goldfinger Priorities' Factum, paras. 128 to 130.

65 Farber, Brief of Documents, June 25, 2012, Vol. 1, Tab 9.

66 Farber, Answers to Question, October 5, 2012, p. 13, Items 28 and 30.

67 Farber July 23, 2011 Report, para. 47.

68 October 10, 2012 Trial Transcript, p. 44.

69 See Tab M, Farber January 18, 2011 Report.

70 Farber Factum in the SGW Proceeding, para. 119.

71 2003 CanLII 13384.

72 *Elias Markets Ltd., Re* (2006), 25 C.B.R. (5th) 50 (Ont. C.A.), paras. 51 to 53.

73 Halsbury's Laws of Canada, First Edition, *Guarantee and Indemnity 2010* (Toronto: LexisNexis, 2010), p. 624.

74 *Chisos Investment Co. v. Firm Capital Equities Corp.*, 1998 CarswellOnt 3861 (Ont. Gen. Div. [Commercial List]), para. 15; *Land Titles Act*, R.S.O. 1990, c. L.5, s. 101(4).

75 *SimEx Inc. v. IMAX Corp.* [2005 CarswellOnt 7297 (Ont. C.A.)], 2005 CanLII 46629, para. 49.

76 2011 ONCA 160 (Ont. C.A.), paras. 33, 37 and 44; see also *Soulos v. Korkontzilas*, [1997] 2 S.C.R. 217 (S.C.C.), paras. 34 to 36.

77 Trial Transcript, December 5, 2012: Carl Schwebel, pp. 19, 20; Reuben Rosenblatt, pp. 56, 58, 59, 70.

78 See, *Canrock Ventures LLC v. Ambercore Software Inc.*, [2011] O.J. No. 729 (Ont. S.C.J. [Commercial List]), paras. 28 to 30.

79 Baigel, November 19, 2012 transcript, Q. 478.

80 December 5, 2012 Trial Transcript: Schwebel, pp. 29, 30, 32. See also Rosenblatt, p. 72.

81 December 5, 2012 Trial Transcript: Schwebel, pp. 24

82 Goldfinger September 6, 2011 Affidavit, paras. 117 and 118. Goldfinger deposed that at the time of the settlement he had no reason to believe that the SG Holding Companies were insolvent: Goldfinger September 27, 2010 affidavit, para. 38. December 9 and 10, 2007 emails between Kimel and Goldfinger disclosed that Goldfinger was aware Kimel was borrowing some of the money.

83 Kimel CX November 12, 2012: QQ 237-240, 241-243, 263- 270, 271-274, and Exhibit P.

84 Kimel CX November 12, 2012: QQ. 207-219.

85 *Ibid.*: QQ. 231-2.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

86 October 10, 2012 Trial Transcript, p. 58; Kimel, CX November 12, 2012, QQ. 264-268.

87 Goldfinger September 6, 2011 Affidavit, para. 36.

88 Goldfinger July 20, 2012 Affidavit, para. 15(a).

89 Baigel acknowledged that Goldfinger previously had paid $2.9 million to Annopol: Baigel CX November 19, 2012, Q. 111.

90 John D. McCamus, *The Law of Contracts* (Toronto: Irwin Law, 2005), p. 226.

91 Goldfinger CX, November 14, 2012, QQ. 451-457.

92 Goldfinger CX, November 14, 2012, QQ. 447-450, Exhibit H.

93 2002 CarswellBC 1642 (B.C. S.C.).

94 (1980), 36 C.B.R. (N.S.) 111 (Que. S.C.).

95 2008 SCC 26 (S.C.C.).

96 *Piikani Nation v. Piikani Energy Corp.*, 2013 ABCA 293 (Alta. C.A.), para. 29.

97 2012 ABQB 187 (Alta. Q.B.).

98 *Ibid.*, paras. 129 and 130.

99 2013 ABCA 293 (Alta. C.A.).

100 2002 ABQB 993 (Alta. Q.B.).

101 *Ibid.*, paras. 19 and 23

102 Transcript of the September 19, 2012 examination of Jack Perelmuter, QQ. 198-201.

103 *Ibid.*, Q. 259.

104 Goldfinger July 20, 2012 Affidavit, paras. 18 to 21.

105 Goldfinger September 27, 2010 affidavit, paras. 40 and 41.

106 Farber Factum, February 7, 2013, para. 67.

107 2002 CanLII 20177, paras. 20-22.

108 (1984), 51 C.B.R. (N.S.) 29 (Ont. Bktcy.)

109 [1988] O.J. No. 2569 (Ont. H.C.), pp. 4 and 5.

110 *Conte*, *supra.*, para. 43; *Boudreau v. Marler* [2004 CarswellOnt 1502 (Ont. C.A.)], 2004 CanLII 19333, para. 70.

111 Transcript of the cross-examination of Michael Baigel, November 19, 2012, QQ.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

112 Transcript of cross-examination of Jack Lechcier-Kimel, November 12, 2012, QQ. 100-107.

113 Kimel, November 12, 2012, QQ.

114 *Ibid.*, QQ. 171-175.

115 *Ibid.*, QQ. 178-181.

116 Goldfinger, September 20, 2012, Q. 12, 15.

117 Transcript of cross-examination of Goldfinger, September 20, 2012, Q. 441.

118 December 5, 2012 Trial Transcript, pp. 33, 34.

119 December 5, 2012 transcript, p. 65.

120 *Kisluk v. B.L. Armstrong Co.* (1982), 44 C.B.R. (N.S.) 251 (Ont. S.C.), para. 45.

121 May I note that there was an unhelpful lack of precision by Farber in its factum, failing to indicate clearly whether it was claiming under *APA* s. 4(1), or 4(2), or both.

122 1996 CanLII 8253, para. 57.

123 *Olympia & York Developments Ltd. (Trustee of) v. Olympia & York Realty Corp.* (2003), 68 O.R. (3d) 544 (Ont. C.A.), para. 45.

124 *Ibid.*, para. 46.

125 *BCE Inc., Re*, [2008] 3 S.C.R. 560 (S.C.C.).

126 R.S.O. 1990, c. P.5.

127 *OBCA*, s. 135(1) and (3).

128 Baigel affidavit, August 15, 2012, paras 60-67.

129 *City Peel Taxi v. Hanna*, 2012 ONSC 2450 (Ont. S.C.J.), paras. 129 and 162.

130 Trial Transcript, December 5, 2012, p. 40.

131 *Royal City Chrysler Plymouth Ltd., Re* [1998 CarswellOnt 1041 (Ont. C.A.)], 1998 CanLII 1337.

132 *Kisluk v. B.L. Armstrong Co.* (1982), 44 C.B.R. (N.S.) 251 (Ont. S.C.), para. 45.

133 Goldfinger November 14, 2012 CX, Q. 328.

134 Paragraph II(b) of Farber's Fresh as Amended Notice of Application.

135 Trial Transcript, December 5, 2012, p. 42. See also Goldfinger September 27, 2010 Affidavit, para. 37.

136 Trial Transcript, December 5, 2012, p. 44.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

137 Ex. 11.

138 Farber Compendium, February 11, 2013, Vol. 2, Tab 11.3.E.

139 Kimel, November 12, 2012, QQ. 406-7.

140 *Thomas Gold Pettinghill LLP v. Ani-Wall Concrete Forming Inc.*, 2012 ONSC 2182 (Ont. S.C.J.), para. 82; *General Electric Canada Real Estate Financing Holding Co. v. Liberty Assisted Living Inc.*, 2013 ONCA 119 (Ont. C.A.).

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 22

1977 CarswellSask 5
Supreme Court of Canada

Robinson v. Countrywide Factors Ltd.

1977 CarswellSask 138, 1977 CarswellSask 5, [1977] 1 A.C.W.S. 137, [1977] 2 W.W.R. 111, [1978] 1 S.C.R. 753, 14 N.R. 91, 23 C.B.R. (N.S.) 97, 72 D.L.R. (3d) 500

Robinson v. Countrywide Factors Ltd.

Laskin C.J.C., Martland, Judson, Ritchie, Spence, Pigeon, Dickson, Beetz and de Grandpré JJ.

Judgment: January 25, 1977

Counsel: *D. G. McLeod, Q.C.*, and *G. Morris*, for appellant.
W. N. Lawton, Q.C., for Attorney General of Saskatchewan.
J. Polika, for Attorney General of Ontario.
W. G. Burke-Robertson, Q.C., for Attorney General of British Columbia.
W. Henkel, Q.C., for Attorney General of Alberta.
E. J. Moss, Q.C., and *B. J. Scherman*, for respondent.
T. B. Smith, Q.C., for Attorney General of Canada.

Subject: Corporate and Commercial; Insolvency; Contracts; Torts

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Fraud and Misrepresentation --- Fraudulent preferences — Validity of provincial legislation

Fraudulent preferences — Provincial legislation dealing with insolvency — Validity — The Fraudulent Preferences Act, R.S.S. 1965, c. 397, ss. 3, 4 — Insolvency — Burden of proof on trustee — The Bankruptcy Act, R.S.C. 1970, c. B-3, ss. 50(6), 73.

Section 3 of The Fraudulent Preferences Act of Saskatchewan dealing with transactions taken with the intent to defeat, hinder, delay or prejudice creditors, and s. 4 of the Act, which is concerned with transactions taken with the intent to give one creditor a preference over other creditors, are valid and subsisting provincial legislation available to a trustee in bankruptcy in his attack on certain transactions. The sections are not in conflict with the Bankruptcy Act. Section 73 of the Bankruptcy Act should be confined to providing for the invalidity of transactions within its exact scope; the Parliament of Canada has refrained from completely covering the whole field of transactions avoided by provincial legislation. Section 50(6) of the Bankruptcy Act is an indication that Parliament recognizes that provisions in provincial statutes dealing with preferential transactions are still valid provincial enactments in reference to "property" and "civil rights" and are valuable aids to trustees in bankruptcy in attacking the validity of such transactions and should be

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

available to the trustees in bankruptcy.

Although the burden is on the trustee to prove the insolvency of the debtor at the time of the transaction — as the burden is always upon the plaintiff to prove his case — the trustee may adduce such a prima facie case as will call upon the defendant to adduce evidence to rebut that prima facie evidence. It must be remembered that a trustee is often faced with a situation where he has to go back into the past and establish an insolvency which he alleges existed at some earlier time. The trustee in such a situation must deal with records which are, in many cases, fragmentary and may well be intentionally deceptive. For instance, he has no means of checking the actual stock-in-trade which existed at that time and sometimes can place little dependence upon the evidence of the debtor.

Annotation

In this case, the majority of the Supreme Court of Canada ruled that the provincial legislation dealing with fraudulent preferences is intra vires. In the past, there were a number of obiter dicta, and the opinions varied greatly. It seems that this issue has now been laid at rest.

The judgment of the majority is also very interesting in another respect, namely, it makes the burden of a trustee in proving insolvency somewhat easier. In the words of Spence J., "the trustee may adduce such a prima facie case which will call upon the defendant to adduce evidence to rebut that prima facie evidence."

It has previously been held that, although insolvency need not be proved beyond a reasonable doubt, the court would not presume insolvency — it must be proved as a matter of fact; it must be shown with reasonable certainty that at the date or dates of payment the debtor was an insolvent person as defined in the Bankruptcy Act, R.S.C. 1970, c. B-3.

As Spence J. said, "trustees in many cases must deal with records which are fragmentary and may well be intentionally deceptive. Under such circumstances, it would be very difficult for a trustee to prove that insolvency was a fact in existence some years earlier."

Reference may be had to Houlden and Morawetz, Bankruptcy Law of Canada, p. 148, and 1976 Supplement, pp. 102-103.

Appeal from the majority judgment of the Saskatchewan Court of Appeal, 19 C.B.R. (N.S.) 24, setting aside the judgment of MacPherson J., 16 C.B.R. (N.S.) 120. Appeal allowed and judgment at trial restored.

***Laskin C.J.C.* (dissenting) (*Martland, Dickson* and *De Grandpre JJ.* concurring):**

1 There are two issues in this appeal, which is here by leave of this court. The first is whether a certain transaction and, in particular, a certain debenture granted on a debtor's stock in trade in pursuance of the transaction between the debtor and the respondent creditor was a fraudulent preference that was impeachable under ss. 3 and 4 of The Fraudulent Preferences Act,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

R.S.S. 1965, c. 397. The second is whether, if it was so impeachable, those provisions of the provincial Act were ultra vires as an invasion of exclusive federal power in relation to bankruptcy and insolvency or, alternatively, were inoperative in the face of the preference provisions of the Bankruptcy Act, R.S.C. 1970, c. B-3.

2 The appellant is trustee in bankruptcy of Kozan Furniture (Yorkton) Ltd. pursuant to a receiving order of 19th November 1968. On 19th November 1966 Kozan entered into a transaction with a pressing creditor, the respondent, whereby it sold certain stock in trade to a third person (payment being made to the respondent which reduced Kozan's indebtedness accordingly) and it also agreed to give the respondent a debenture on its stock in trade for its remaining indebtedness. The debenture was executed on or about 20th March 1967 and duly registered. After the receiving order against Kozan was made, proceedings were taken by the appellant trustee in bankruptcy to set aside the transaction of 19th November 1966 as constituting a fraudulent preference under the provincial Fraudulent Preferences Act and to recover the money paid to the respondent and to annul the debenture.

3 MacPherson J. found that Kozan was insolvent at the time of the transaction of 19th November 1966, that there was a concurrent intention of Kozan and the respondent to give and receive a preference and that, consequently, both the payment made to the respondent and the debenture constituted fraudulent preferences under the provincial statute and were hence impeachable [(1971), 16 C.B.R. (N.S.) 120]. On appeal, this judgment was set aside on the view of the majority of the Saskatchewan Court of Appeal that the appellant had failed to prove that Kozan was insolvent on 19th November 1966 [19 C.B.R. (N.S.) 24]. The trial judge was not called upon to deal with any constitutional issue and the majority of the Court of Appeal did not have to do so in view of its finding on insolvency. Hall J.A., who dissented, supported the trial judge's finding of insolvency, and in a one sentence assertion, in reliance upon *Re Panfab Corpn. Ltd.; Duro Lam Ltd. v. Last*, 15 C.B.R. (N.S.) 20, [1971] 2 O.R. 202, 17 D.L.R. (3d) 382, he rejected the contention that The Fraudulent Preferences Act was ultra vires.

4 I would not interfere with the findings of the judge of first instance that Kozan was insolvent at the material time and that Kozan intended to give and the respondent intended to receive a preference. This is the view of my brother Spence who, in exhaustive reasons, also concluded that The Fraudulent Preferences Act as a whole was not ultra vires nor was either s. 3 or s. 4 inoperative in the face of the Bankruptcy Act. I have a different opinion on the constitutional issue in this case, as appears from what now follows. That issue does not invite this court to pronounce on the validity of provincial legislation dealing with fraudulent conveyances or with fraudulent transactions in general. Thus, to take as an example The Fraudulent Conveyances Act, R.S.O. 1970, c. 182, nothing said in these reasons is to be taken as impugning the validity of that or similar enactments. They do not, ex facie, depend on proof of insolvency or on bankruptcy. In so far as any of the case law — some of it canvassed by my brother Spence — relates to such legislation and carries it into a consideration of the validity of provincial preference legislation which depends, as do ss. 3 and 4 of the Saskatchewan Fraudulent Preferences Act, on a condition of insolvency, I find it inapt for the determination of the constitutional question in this appeal.

5 Sections 3 and 4 aforesaid are in the following terms:

> 3. Subject to sections 8, 9, 10 and 11 every gift, conveyance, assignment or transfer, delivery over or payment of goods, chattels or effects or of bills, bonds, notes or securities or of shares, dividends, premiums or bonus in a bank, company or corporation, or of any other property real or personal, made by a person at a time when he is in insolvent circumstances or is unable to pay his debts in full or knows that he is on the eve of insolvency, with intent to defeat, hinder, delay or prejudice his creditors or any one or more of them, is void as against the creditor or creditors injured, delayed or prejudiced.
>
> 4. Subject to sections 8, 9, 10 and 11 every gift, conveyance, assignment or transfer, delivery over or payment of goods, chattels or effects or of bills, bonds, notes or securities or of shares, dividends, premiums or bonus in a bank, company

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> or corporation, or of any other property real or personal, made by a person at a time when he is in insolvent circumstances or is unable to pay his debts in full or knows that he is on the eve of insolvency to or for a creditor, with intent to give that creditor preference over his other creditors or over any one or more of them, is void as against the creditor or creditors injured, delayed, prejudiced or postponed.

6 Sections 8, 9, 10 and 11, to which each of the foregoing provisions is subject, do not affect the constitutional issue, being concerned with bona fide sales or payments to innocent purchasers, valid sales for consideration and protection of security given up by a creditor. The present case does not involve ss. 8 to 11.

7 I approach the question of validity on principle and on authority. So far as principle is concerned, the starting point is in the relevant words of the B.N.A. Act, 1867, namely, s. 91(21), "Bankruptcy and Insolvency", as they relate to s. 92(13), "Property and Civil Rights in the Province". The elucidation of the meaning and scope of s. 91(21), as of the meaning and scope of any other heads of legislative power, can hardly ever be a purely abstract exercise, even where an attempt is made at neutral definition; but I see no reason why judicial pronouncements, especially at the appellate level where they are those of the court, should not be considered as throwing light upon the integrity of the head of power in the scheme of the B.N.A. Act as a whole.

8 Four things stand out. First, s. 91(21) is an exclusive federal power; second, it is a power confided to the Parliament of Canada notwithstanding anything else in the Act; third, it is a power, like the criminal law power, whose ambit did not and does not lie frozen under conceptions held of bankruptcy and insolvency in 1867 (see *A.G.B.C. v. A.G. Can.; Reference re Farmers' Creditors Arrangement Act*, [1937] A.C. 391 at 402-403); and fourth, the term "Insolvency" in s. 91(21) has as much an independent operation in the reservation of an exclusive area of legislative competence to the Parliament of Canada as the term "Bankruptcy" (see *Can. Bankers Assn. v. A.G. Sask.*, 35 C.B.R. 135, [1956] S.C.R. 31, (sub nom. *Re Moratorium Legislation)* [1955] 5 D.L.R. 736, per Rand J. at p. 46).

9 The view taken by the Privy Council and by this court as to the meaning of "insolvency", after as well as before the abolition of Privy Council appeals, has been a uniform one. Lord Thankerton, speaking for the Privy Council in the *Farmers' Creditors Arrangement Act* reference, supra, at p. 402 expressed it as follows:

> In a general sense, insolvency means inability to meet one's debts or obligations; in a technical sense, it means the condition or standard of inability to meet debts or obligations, upon the occurrence of which the statutory law enables a creditor to intervene, with the assistance of a Court, to stop individual action by creditors and to secure administration of the debtor's assets in the general interest of creditors; the law also generally allows the debtor to apply for the same administration.

10 This definition was referred to with approval in the majority judgment of the Supreme Court of Canada delivered by Kerwin C.J.C. in *Reference re Orderly Payment of Debts Act, 1959 (Alta.)*, 1 C.B.R. (N.S.) 207 at 212, [1960] S.C.R. 571, 23 D.L.R. (2d) 449. Earlier in *Reference re Debt Adjustment Act, 1937 (Alta.)*; *A.G. Alta. v. A.G. Can.*, 24 C.B.R. 144 at 148, [1942] S.C.R. 31, [1942] 1 D.L.R. 1, affirmed [1943] 1 W.W.R. 378, 24 C.B.R. 129, [1943] A.C. 356, [1943] 1 All E.R. 240, [1943] 2 D.L.R. 1, Duff C.J.C., speaking for all but one of the members of the court, took as an additional ground for invalidating the challenged provincial legislation in that case that the powers of the provincial statutory tribunal set up under that legislation would normally "come into operation when a state of insolvency exists"; and he continued:

> It is not too much to say that it is for the purpose of dealing with the affairs of debtors who are pressed and unable to pay

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

their debts as they fall due that these powers and duties are created.

11 If it is for Parliament alone to deal with insolvency, indeed to define it where it chooses to do so and to leave it otherwise to judicial definition, there can be no argument about unlawful invasion of provincial power in relation to property and civil rights. A limitation upon such power necessarily inheres in the federal catalogue of powers in s. 91, and it was recognized as early as 1880 in *Cushing v. Dupuy* (1880), 5 App. Cas. 409 at 415, in respect of the federal bankruptcy and insolvency power.

12 I refer to two other propositions before turning to what I consider to be the relevant cases. First, there is the well-recognized proposition that federal abstinence from legislation in relation to an exclusive head of legislative power does not leave that legislative area open to provincial action: see *Union Colliery Co. v. Bryden*, [1899] A.C. 580 at 588. The principle of our Constitution as it relates to legislative power is not one of simple concurrency of authority subject only to a variable doctrine of paramountcy. Exclusiveness is central to the scheme of distribution, save as to a specified number of concurrent powers such as those in s. 95. It is only under the umbrella of the doctrine of exclusiveness that the relative scope of federal and provincial authority is assessed, the assessment being carried forward to determine whether there is preclusion or supersession where both federal and provincial legislation are in competition. This brings me to the second point. I take the same view here that was taken by Duff C.J.C. in the *Debt Adjustment Act* reference, supra, and I adopt his words at p. 148, namely, that although the motives of a provincial legislature may be laudable ones, it is precluded from seeking to realize its object by entering into a field not open to it.

13 *A.G. Ont. v. A.G. Can.*, [1894] A.C. 189, generally known as the *Voluntary Assignments* case, stands as the general support for provincial legislation of the kind or allied to the kind of legislation that is challenged in the present case. It concerned only one section, s. 9, of the Ontario Assignments and Preferences Act, R.S.O. 1887, c. 124, first enacted in 1885 (Can.), c. 26. That section was as follows:

> 9. An assignment for the general benefit of creditors under this Act shall take precedence of all judgments and of all executions not completely executed by payment, subject to the lien, if any, of an execution creditor for his costs, where there is but one execution in the sheriff's hands, or to the lien, if any, of the creditor for his costs who has the first execution in the sheriff's hands.

14 This Act replaced earlier pre-Confederation legislation found in C.S.U.C. 1859, c. 26, under the title "The Relief of Insolvent Debtors Act", which was continued in the post-Confederation legislation of Ontario as An Act respecting the Fraudulent Preference of Creditors by persons in insolvent circumstances, and included in R.S.O. 1877, c. 118. What is significant in this earlier legislation is that (as set out in s. 2 of R.S.O. 1877, c. 118) it dealt with "any person, being at the time in insolvent circumstances or unable to pay his debts in full, or knowing himself to be on the eve of insolvency". The substituted Act of 1885 continued the reference to insolvency in respect of preferences but it also introduced new provisions respecting assignments for the benefit of creditors and these provisions, as was noted in the *Voluntary Assignments* case, were not predicated on insolvency and, indeed, were to a large degree separated from the preference provisions of the Act, as is reflected in s. 3 of R.S.O. 1887, c. 124.

15 Certainly, as the Privy Council noted, the challenged provision, s. 9, had to be taken in the context of the entire Act. There is no doubt, as well, that the issue of validity was recognized as arising at a time when there was no federal bankruptcy or insolvency legislation in force, the only such legislation, the Insolvency Act of 1875, having been repealed in 1880 by 1880 (Can.), c. 1. The majority of the Ontario Court of Appeal, to which the question of the validity of s. 9 had been referred, had found that it was ultra vires as invading exclusive federal power in relation to bankruptcy and insolvency: see (1893), 20

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

O.A.R. 489. The reversal of this judgment by the Privy Council was accompanied by an acknowledgement of the broad scope of federal power under s. 91(21) when affirmatively exercised but it was held that this power was not invaded by an enactment relating to an assignment that was purely voluntary.

16 The explanation for this result is found in two passages of the Privy Council's reasons. First [at p. 198]:

> ... it is to be observed that an assignment for the general benefit of creditors has long been known to the jurisprudence of this country and also of Canada, and has its force and effect at common law quite independently of any system of bankruptcy or insolvency, or any legislation relating thereto.

17 Second [at p. 199]:

> ... the operation of an assignment for the benefit of creditors was precisely the same, whether the assignor was or was not ... insolvent ... The validity of the assignment and its effect would in no way depend on the insolvency of the assignor, and their Lordships think it clear that the 9th section would equally apply whether the assignor was or was not insolvent.

18 What is evident, therefore, from that case is that, unlike the situation here, the operation of the provincial enactment did not depend on insolvency and the Privy Council was willing to treat s. 9 as having an object that was independent of it. This may even be a supportable view today, albeit there is a range of existing federal legislation dealing with bankruptcy and insolvency. I should note, however, that in the majority judgment of this court in *Reference re Orderly Payment of Debts Act, 1959 (Alta.)*, supra, at pp. 212-13, Kerwin C.J.C., referring to the *Voluntary Assignments* reference, said,

> ... it is doubtful whether in view of later pronouncements of the Judicial Committee it would at this date be decided in the same sense, even in the absence of Dominion legislation upon the subject of bankruptcy and insolvency.

19 The later pronouncements of the Privy Council include its judgment in the *Debt Adjustment Act* reference, supra, as well as in the *Farmers' Creditors Arrangement Act* reference, supra. Equally important is the judgment of this court in *Can. Bankers Assn. v. A.G. Sask.*, supra, dealing with the validity of provincial moratorium legislation. It was in line with the decision in the *Debt Adjustment Act* reference in finding an invasion of federal power in relation to bankruptcy and insolvency. I think it enough, for present purposes, to refer to what Locke J., speaking for the majority of the court, said at p. 146:

> Power to declare a moratorium for the relief of the residents of a province generally in some great emergency, such as existed in 1914 and in the days of the lengthy depression in the thirties, is one thing, but power to intervene between insolvent debtors and their creditors, irrespective of the reasons which have rendered the debtor unable to meet his liabilities, is something entirely different.

20 Although judgments of the Privy Council and of this court (and I add to those already cited, *Royal Bank of Can. v. Larue*, [1928] 1 W.W.R. 534, 8 C.B.R. 579, [1928] A.C. 187, (sub nom. *Bélanger v. Royal Bank of Can.)* [1928] 1 D.L.R. 945) have recognized the broad power of Parliament to embrace in its legislation in relation to bankruptcy or insolvency provisions which might otherwise fall within provincial competence, I know of no case in those courts, other than *Ladore v. Bennett*, [1939] 2 W.W.R. 566, 21 C.B.R. 1, [1939] A.C. 468, [1939] 3 All E.R. 98, [1939] 3 D.L.R. 1, where provincial

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

legislation has been sustained, either in the absence of or in the face of federal legislation, when such provincial legislation depends for its operation only upon insolvency. *Ladore v. Bennett* can best be explained as involving municipal re-organization and hence as being concerned with the amalgamation and financial restructuring of units of local government for which the provincial legislature has a direct responsibility, albeit some of the municipalities involved in the legislatively-directed re-organization were insolvent. It is, indeed, a special case of a piece of special legislation enacted in pursuance of the power conferred by s. 92(8) of the B.N.A. Act, and I do not regard it as offering any lead to continuing legislation relating to private debtors and their creditors.

21 It is plain to me that, if provincial legislation avowedly directed to insolvency and to transactions between debtor and creditor consummated in a situation of insolvency can be sustained as validly enacted unless overborne by competent federal legislation, there is a serious breach of the principle of exclusiveness which embraces insolvency under s. 91(21). This court so held in a series of cases where the encroachment on the federal bankruptcy and insolvency power was less obvious than that exhibited here. I refer, of course, to the *Debt Adjustment Act* reference, supra, to the *Can. Bankers Assn.* case, supra, and to the *Orderly Payment of Debts Act, 1959* (*Alta.*) reference, supra. It would be a curious reversal of the proposition enunciated in *Madden v. Nelson and Fort Sheppard Ry. Co.*, [1899] A.C. 626, namely, that you cannot do indirectly what you cannot do directly, to hold that the province can do directly what it cannot do indirectly.

22 The case put forward by the appellant and by the intervening provinces which supported him goes even farther. It is contended that notwithstanding the existence of federal bankruptcy legislation dealing with preferences the challenged provincial legislation can still operate in respect of a particular preference which is given outside of the time limits within which the federal control operates, so long at least as the provincial provision is not more stringent.

23 I do not follow this line of reasoning, especially on the submission of greater or lesser stringency. The relevant federal provision is s. 73 of the Bankruptcy Act which reads as follows:

> 73.(1) Every conveyance or transfer of property or charge thereon made, every payment made, every obligation incurred, and every judicial proceeding taken or suffered by any insolvent person in favour of any creditor or of any person in trust for any creditor with a view to giving such creditor a preference over the other creditors shall, if the person making, incurring, taking, paying or suffering the same becomes bankrupt within three months after the date of making, incurring, taking, paying or suffering the same, be deemed fraudulent and void as against the trustee in the bankruptcy.
>
> (2) Where any such conveyance, transfer, payment, obligation or judicial proceeding has the effect of giving any creditor a preference over other creditors, or over any one or more of them, it shall be presumed *prima facie* to have been made, incurred, taken, paid or suffered with a view to giving such creditor a preference over other creditors, whether or not it was made voluntarily or under pressure and evidence of pressure shall not be receivable or avail to support such transaction.
>
> (3) For the purposes of this section, the expression 'creditor' includes a surety or guarantor for the debt due to such creditor.

24 This provision cannot be taken in isolation. The Bankruptcy Act is a code on the subject of bankruptcy and insolvency, defining what is an act of bankruptcy and who is an insolvent person; prescribing what are vulnerable settlements as well as what are vulnerable preferences; declaring what is comprised in a bankrupt's estate, and providing for priorities in distribution and for rateable distribution. It provides also, as in the present s. 31(1), for the making of an assignment by an insolvent person for the benefit of creditors as well as providing by s. 24(1)(*a*) that it is an act of bankruptcy to make an assignment for the benefit of creditors whether the assignment is or is not authorized by the Bankruptcy Act. In short, apart

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

from the question whether provincial legislation predicated on insolvency is ipso facto invalid, I see no room for any assertion that such provincial legislation can continue to have operative effect in the face of the scope of the Bankruptcy Act embracing both bankruptcy and insolvency in its provisions.

25 It is worth a reminder that there is no common law of bankruptcy and insolvency and hence it cannot be said that there was an existing common law course of decision which was being embraced by provincial legislation. The common law did not distinguish the fraudulent from the insolvent debtor; it was through legislation that such a distinction was made. If a provincial legislature wishes to proscribe fraudulent transactions, it is compelled by the B.N.A. Act to ensure that its legislation dealing with such transactions does not focus on insolvency.

26 Of the many cases cited in argument before this court, I can put to one side *Re Davison*, 5 C.B.R. 860, 52 O.L.R. 244, [1923] 4 D.L.R. 1049, and *Re Panfab Corpn. Ltd.*, supra, both of which were decisions of single judges and dealt largely with the Ontario Fraudulent Conveyances Act which, as I have already said, does not depend for its activation either on insolvency or on bankruptcy nor on any question of preference such as that presented here. Similarly, I put to one side *Allison & Burnham Concrete Ltd. v. Mountain View Construction Ltd.* (1965), 53 W.W.R. 274, 9 C.B.R. (N.S.) 52, 54 D.L.R. (2d) 67, a judgment of Ruttan J. of the British Columbia Supreme Court, in so far as it was concerned with the British Columbia Fraudulent Conveyances Act, R.S.B.C. 1960, c. 155, akin to the Ontario Act of the same name.

27 Chronologically, the first of the cited cases that calls for consideration here is *Hoffar Ltd. v. Can. Credit Men's Trust Assn. Ltd.*, [1929] 1 W.W.R. 557, 10 C.B.R. 369, 40 B.C.R. 454, [1929] 2 D.L.R. 73, leave to appeal refused [1929] S.C.R. 180, [1929] 2 D.L.R. 106. It was a judgment of the British Columbia Court of Appeal involving the question whether s. 3 of the provincial Fraudulent Preferences Act, R.S.B.C. 1924, c. 97 (similar to ss. 3 and 4 of the Saskatchewan Act in the present case), was in conflict with the then preference provision, s. 64, of the federal Bankruptcy Act, R.S.C. 1927, c. 11.

28 It is important to note, as stated by British Columbia chief justice Macdonald, that no argument was raised in the *Hoffar* case as to the validity of either the provincial Fraudulent Preferences Act or the Bankruptcy Act. A second significant aspect of the decision is that the court felt it was immaterial that the federal Act prescribed a 3-month period for invalidation of a transaction while the provincial Act prescribed a 60-day period. In fact, the transaction sought to be impugned was made less than 60 days before an assignment under the Bankruptcy Act, and there was a finding that the debtor was insolvent at the time of the transaction. The judge of first instance found that although the transaction had the effect of giving a preference it was not made with a view thereto. Under the Bankruptcy Act there was a rebuttable presumption in such a case that the transaction was concluded with a view to a preference and it was found that there was rebutting evidence. However the provincial Act made the transaction void irrespective of rebutting evidence, and the judge at first instance applied this Act.

29 The British Columbia Court of Appeal reversed this decision holding that the provincial provisions were inoperative because they were in conflict with the federal Act. A for tiori, the provincial provisions would be inoperative, in my view, if a transaction was made with a view to giving a preference. Leave to appeal was refused by Mignault J. in the Supreme Court of Canada on the ground that the decision sought to be appealed was plainly right, and he added a reference to a passage in the reasons in the *Voluntary Assignments* case where the Privy Council spoke of the preclusion of the provincial legislature from interfering with federal bankruptcy legislation.

30 This preclusive principle of non-interference is as applicable in connection with the federal power in relation to bankruptcy and insolvency as it is in the field of criminal law. In that connection, I point to the words of the late Rand J. in *Johnson v. A.G. Alta.*, 18 C.R. 173 at 183, [1954] S.C.R. 127, 108 C.C.C. 1, [1954] 2 D.L.R. 625, and adapt them here to say

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

that "any local legislation of a supplementary nature that would tend to weaken or confuse [the] enforcement [of the Bankruptcy Act] would be an interference with the exclusive power of Parliament".

31 It is worth adding that in his reasons in the British Columbia Court of Appeal in the *Hoffar* case M. A. Macdonald J.A. indicated that provincial fraudulent conveyances legislation could be invoked where the Bankruptcy Act did not apply on the facts, even if provincial fraudulent preference legislation could not be.

32 The next case for consideration is *Re Pommier*, 11 C.B.R. 449, 65 O.L.R. 415, [1930] 4 D.L.R. 113, a judgment of Fisher J.A. sitting in bankruptcy. I accept one of its premises, namely, that the Bankruptcy Act did not oust all provincial legislation respecting fraudulent transactions, for example, the Ontario Fraudulent Conveyances Act. This was the same point taken in the *Hoffar* case. However, unlike the result in the *Hoffar* case (which was cited but not followed) the court in *Re Pommier* held that in the case of a preferential transaction which took place more than three months before an assignment in bankruptcy (and therefore outside the preference period under the federal Act) resort could be had to the provincial Assignments and Preferences Act, R.S.O. 1927, c. 162, to impeach it. The learned judge invoked a so-called doctrine of overlapping, which he distinguished from a situation of conflict, in holding the provincial Act to be available. In my opinion, he misconceived its purport as it was enunciated in *Grand Trunk Ry. Co. v. A.G. Can.*, [1907] A.C. 65 at 68, 7 C.R.C. 472. The proposition there related to a situation where "the field is clear" to one legis lature or the other. The Privy Council noted that "if the field is not clear, and in such a domain the two legislations meet, then the Dominion legislation must prevail".

33 It is only necessary to add that *Re Pommier* was overruled by the Ontario Court of Appeal in *Re Trenwith*, 15 C.B.R. 372, [1934] O.R. 326, [1934] 3 D.L.R. 195, where Masten J.A. said at p. 376 (after referring to the *Voluntary Assignments* case, to *Royal Bank of Can. v. Larue*, supra, and to the *Hoffar* case):

> ... it seems clear to me that the common field of legislation respecting the distribution of the estates of insolvents having now become occupied by the Dominion *Bankruptcy Act*, the provisions of *The Assignments and Preferences Act* respecting the preference of one creditor over another have been thereby superseded and have ceased to have any operation. If I am right in this conclusion, the effect is to overrule ... *Re Pommier*.

34 Davis J.A., who dissented on other grounds, was also of the opinion that "since the enactment of bankruptcy legislation by the Dominion Parliament, this provincial statute cannot be invoked" (at p. 384).

35 To the same effect was the opinion of this court expressed by Duff C.J.C. in *Re Bozanich; A. H. Boulton Co. v. Trusts & Guarantee Co.*, 23 C.B.R. 234, [1942] S.C.R. 130, [1942] 2 D.L.R. 145, that "the provisions of *The Assignments and Preferences Act*, R.S.O. 1927, ch. 162, in relation to preferences are superseded by sec. 64 of *The Bankruptcy Act*, and that the authority of the Ontario Legislature to enact such legislation is, in consequence of the enactment of sec. 64, suspended in view of the concluding paragraph of sec. 91 of The British North America Act".

36 Three judgments at first instance may be mentioned before I go on to consider the unanimous judgment of the Alberta Appellate Division, sitting as a bench of five, in *A.G. Alta. v. Nash* (1964), 50 W.W.R. 155, 7 C.B.R. (N.S.) 92, (sub nom. *Re McIntosh-Marshall Equipment Ltd.; Nash v. Guelph Engineering Co.)* 48 D.L.R. (2d) 619, affirming 48 W.W.R. 420, 7 C.B.R. (N.S.) 84. The three cases are *Crown Coal Co. Ltd. v. Swanson Lumber Co. Ltd.*, [1935] 3 W.W.R. 245, 17 C.B.R. 115, [1935] 4 D.L.R. 707 (C.A.); *Gard v. Yates*, [1936] 1 W.W.R. 212, 17 C.B.R. 168, 50 B.C.R. 353, [1936] 2 D.L.R. 50, and *Totem Radio Supply Co. Ltd. v. Stone* (1959), 29 W.W.R. 552, 38 C.B.R. 112. All three of these cases concerned issues

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

of alleged conflict between provincial and federal legislation respecting rights of creditors of a person who has made an authorized assignment or was insolvent at a material time. The *Crown Coal Co. Ltd.* case, an Alberta judgment, did not turn on a constitutional issue and, at any rate, it cannot stand in the face of the *Nash* case; I am, similarly, unable to appreciate how either *Gard v. Yates* or the *Totem Supply* case, both British Columbia decisions, can stand against the reasoning in *Nash*, the views expressed in *Re Trenwith* and those expressed by Duff C.J.C. in *Re Bozanich*. The first represents a decision overtaken by later authority and the second cites no authorities at all but on the point of alleged conflict between the respective provincial and federal preference provisions is content to say simply that there is no conflict where the preference is given outside the three-month period fixed by the federal Bankruptcy Act when the provincial Act fixes a larger period for impeachment. Reliance was placed on the then s. 41(6) [of R.S.C. 1952, c. 14], now s. 50(6), of the Bankruptcy Act, to which I will return later in these reasons. I should add that in another later British Columbia case, the *Allison & Burnham Concrete Ltd.* case already mentioned (also a judgment of a single judge), Ruttan J. did canvass later authorities but decided to rest on earlier decisions such as *Gard v. Yates* to justify a construction that avoided any constitutional infirmity in the event that the provincial Act gave a longer impeachment period than the federal Act. In effect, his view was to leave the constitutional issue to a higher court. That is where it now is.

37 *A.G. Alta. v. Nash* came before Milvain J., as he then was, through a proceeding by a trustee in bankruptcy to set aside payments made by the bankrupt company to its creditors within one year prior to bankruptcy but, save as to one payment, beyond the three-month period under the then s. 64 (now s. 73) of the Bankruptcy Act. The trustee relied on s. 4 of the Alberta Fraudulent Preferences Act [R.S.A. 1955, c. 120] which, like the Saskatchewan provisions in issue here, is predicated for its operation on insolvency. It fixes a one-year period within which a transaction having the effect of giving a preference may be impeached as being utterly void. Milvain J. held that the Alberta Act was ultra vires as being in pith and substance insolvency legislation.

38 In the Alberta Appellate Division Johnson J.A., speaking for a unanimous court of five, was content to consider the Alberta Fraudulent Preferences Act, first enacted in 1922, and, in particular, s. 4 (with a 60-day impeachment period, enlarged in 1931 to one year) from the standpoint of its preclusion by the prior enactment of the federal Bankruptcy Act and its preference provisions. After a canvass of the authorities to date, he said this (at pp. 160-61):

> There can, I think, be no doubt that the impugned Act was *ultra vires* of the legislature when it was passed. Whatever can be said for similar legislation that was passed before the *Bankruptcy Act* become (sic) operative, this legislation, viewed in the light of sec. 64, becomes an attempt to cover the same ground that section covers. The enlargement of the time from 60 days to one year must be viewed as an attempt to strengthen the remedy which sec. 64 gives to creditors. Sec. 4 cannot be looked upon as legislation which was intended to deal with contracts and which only incidentally and as part of a larger scheme dealt with matters which were within the scope of one or more of the subjects mentioned in sec. 91. This section is what it purports to be. Legislation intended to prevent a person 'at a time when he is in insolvent circumstances or is unable to pay his debts in full or knows that he is on the eve of insolvency' (4 [*a*]), from disposing of his property in such a manner as to prefer one creditor over another. It is exactly what sec. 64 of the *Bankruptcy Act* was passed to prevent. If it is not in pith and substance insolvency legislation under the earlier cases, it has become so under the enlarged definition [of later cases] and also by virtue of sec. 64 of the *Bankruptcy Act*.
>
> Viewing sec. 64 as being ancillary to bankruptcy and insolvency legislation, there can be no doubt of the conflict between that section and this section of *The Fraudulent Preferences Act*. Sec. 64 fixes three months as the time within which proceedings must be taken to avoid preferential dealings. Transactions beyond that period cannot be attacked under that section and are, therefore, legal. To enlarge that period to one year is to render void payments and transfers of property which were valid under sec. 64. The exclusions from the operation of the two sections, while similar, exhibit a differing approach and there can be little doubt that sec. 64 gives a wider exemption than sec. 7 of *The Fraudulent Preferences Act*.

39 In coming to the conclusion that s. 4 of the Alberta Act was in conflict with the then s. 64 of the federal Act, the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

learned judge in the *Nash* case took into consideration s. 41(6) of the Bankruptcy Act, now s. 50(6), which read as follows:

> 41. ...
>
> (6) The provisions of this Act shall not be deemed to abrogate or supersede the substantive provisions of any other law or statute relating to property and civil rights that are not in conflict ... with this Act, and the trustee is entitled to avail himself of all rights and remedies provided by such law or statute as supplementary to and in addition to the rights and remedies provided by this Act.

40 In my opinion, this provision is not designed to enlarge provincial authority, and Johnson J.A. rightly held that because of conflict it had no application. The provision aforesaid does not provide for the effacement of federal legislation to allow provincial legislation to operate but relates to provincial provisions which satisfy two conditions: first, they must be provisions which are independently valid; and second, they must be provisions which do not conflict with the application and operation of federal provisions. I do not see how provincial legislation whose operation is predicated on insolvency can be anything but insolvency legislation, nor do I see how a provincial statute can validly provide that what a federal statute says is not impeachable can nonetheless be impeached. There is no difference, in my view, between the situation where a province seeks to narrow the period of impeachability of a transaction and the situation where it seeks to enlarge it, especially when in either case it is doing this from the standpoint of insolvency as the triggering factor. This is a different thing from legislation dealing only with fraudulent preferences apart from or unrelated to insolvency. Here, although such legislation may be valid in the absence of federal legislation, there may nonetheless be operative incompatibility in particular cases but no general supersession or preclusion.

41 I wish now to address myself to an issue which, I think, has influenced the approach by single judges to the constitutional question in this case, and wrongly so. That issue is the undesirability of interfering with what appeared to be a practical way of reaching as many alleged preferences in fraud of creditors as possible, by using provincial legislation where federal legislation did not reach far enough, and by using provincial insolvency legislation if nothing else was available. Hence, the approach by way of construction (albeit a dip into a constitutional area was inevitable) avoiding a direct constitutional confrontation. There are cases even in this court and on this very subject which have proceeded on a straight construction basis to examine whether operative effect can be given to provincial legislation in the face of a federal enactment. Two examples are *Traders Finance Corpn. v. Levesque*, 2 C.B.R. (N.S.) 52, [1961] S.C.R. 83, 26 D.L.R. (2d) 384, and *Re Gingras Automobile Ltée.; Produits de Caoutchouc Marquis Inc. v. Trottier*, 4 C.B.R. (N.S.) 123, [1962] S.C.R. 676, 34 D.L.R. (2d) 751. I do not regard either of these cases as requiring a decision on constitutional grounds. The *Traders Finance* case concerned a largely procedural matter, namely, whether the failure of a trustee in bankruptcy to impeach a preference illegal under the Bankruptcy Act precluded a suit by a creditor to that end. The *Trottier* case dealt with the effect of the Bankruptcy Act on the extent of a landlord's claim to rank as a preferred creditor.

42 There are numerous illustrations in other branches of the law where practices carried on for some time without objection on constitutional grounds were brought to an end when the constitutional question was raised directly. Perhaps the most celebrated instance was that considered by the Privy Council in *Nadan v. The King*, [1926] 1 W.W.R. 801, [1926] A.C. 482, 45 C.C.C. 221, [1926] 2 D.L.R. 177, where a federal enactment of 1888, purporting to exclude appeals to the Privy Council in criminal matters, was invalidated almost 40 years later. Equally significant because the issue was well-known to the Ontario Bar, which seems to have agreed to live with it as a matter of convenience, was the constitutional propriety of provincial legislation vesting jurisdiction in the master to try mechanics' lien actions in the county of York. Once the constitutional issue was squarely raised the courts did not back away from it and held that s. 96 of the B.N.A. Act was offended; see *A.G. Ont. v. Victoria Medical Building Ltd.*, [1960] S.C.R. 32, (sub nom. *Display Service Ltd. v. Victoria Medical Building Ltd.)* 21 D.L.R. (2d) 97.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

43 There have been a number of recent cases where this court has proceeded on a construction basis rather than on a constitutional basis in respect of the operation of both federal and provincial legislation although aware that a constitutional question was involved but being unwilling to deal with it unless raised by a party so that necessary notice could be given to the Attorneys General, federal and provincial. One example is *Les Immeubles Fournier Inc. v. Construction St. Hilaire Ltée*, [1975] 2 S.C.R. 2, 52 D.L.R. (3d) 89, involving s. 8 of the Interest Act, R.S.C. 1970, c. I-18. Another is *Can. Labour Relations Bd. v. C.N.R.*, [1974] 4 W.W.R. 661, [1975] 1 S.C.R. 786, 45 D.L.R. (3d) 1, which concerned the scope of s. 53(*g*) of the federal Industrial Relations and Disputes Investigation Act, R.S.C. 1952, c. 152 (now s. 108, Pt. V [reen. 1972, c. 18, s. 1] of the Canada Labour Code, R.S.C. 1970, c. L-1) and whether it embraced (validity not put in issue) a hotel operated by the respondent railway.

44 Finally, on this phase of the case, I refer to *Gingras v. General Motors Products of Can. Ltd.*, [1976] S.C.R. 426, 57 D.L.R. (3d) 705, which involved a question of prescription in respect of an action by a trustee in bankruptcy to set aside an illegal preference under the Bankruptcy Act. No constitutional question was directly involved and the majority judgment held that a certain prescriptive provision of the Civil Code of Quebec did not apply so as to limit the trustee's right of action.

45 I conclude, therefore, as follows. Provincial legislation which purports to provide for impeachment of preferences to creditors given by a person who is then insolvent, where insolvency is the sine qua non of impeachability, is invalid as a direct invasion of exclusive federal power in relation to bankruptcy and insolvency. Hence, ss. 3 and 4 of Saskatchewan Fraudulent Preferences Act are ultra vires. Moreover, in so far as these sections prescribe an impeachment period which enables a creditor to set aside a preference made beyond the period fixed by the Bankruptcy Act and hence not impeachable under that Act, it interferes with the operation of the Bankruptcy Act and is, indeed, repugnant to it. It must be remembered that where, as in the present case, there has been a receiving order, the intrusion of provincial legislation relating to transactions entered into by an insolvent must interfere with the rateable distribution of the bankrupt's property according to the scheme of distribution prescribed by the Bankruptcy Act. Whether that scheme is faulty in the view of a court is immaterial; the correction must come from the responsible legislature. No more under bankruptcy and insolvency law than under the criminal law can a province make unlawful what is lawful under valid federal legislation, or make lawful what is unlawful under valid federal legislation.

46 In the result, I would answer the two questions in issue here in the affirmative. The judgment of the Saskatchewan Court of Appeal should be varied so as to restore the finding of insolvency by the trial judge but the appeal should otherwise be dismissed in view of the affirmative answers aforesaid. Leave is also given for a reference to determine the amount due under the debenture if the parties are unable to agree thereon. The respondent should have its costs in this court but there should be no order as to costs to or against any of the intervenors.

***Spence J. (Judson, Ritche* and *Pigeon JJ.* concurring):**

47 This is an appeal from the judgment of the Court of Appeal for Saskatchewan pronounced on 14th March 1974 [19 C.B.R. (N.S.) 24]. By that judgment the Court of Appeal allowed an appeal from the judgment of MacPherson J., pronounced on 16th June 1971 [16 C.B.R. (N.S.) 120]. By the latter judgment, MacPherson J. had declared that the payment of the sum of $9,152.31 to the respondent was void as a preference under The Fraudulent Preferences Act, R.S.S. 1965, c. 397, and had given judgment in favour of the appellant against the respondent for that amount.

48 The issue determined by MacPherson J., insofar as may be adjudged from a perusal of the reasons for judgment delivered by the learned trial judge, was simply whether the transaction was or was not a preferential one voided by the provisions of that statute.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

49 On the appeal to the Court of Appeal, the present respondent not only dealt with that issue but with the issue of whether the provincial statute was available to the appellant in this court (there respondent) in an attack on the transaction.

50 Maguire J.A., in giving reasons for the majority of the Court of Appeal, held that the transaction was not a preferential one within the meaning of the section in the provincial Fraudulent Preferences Act, and, therefore, was not called upon to determine whether that statute was available in whole or in part to the trustee in bankruptcy. Hall J.A., giving a dissenting judgment, found that the transaction was a preferential one within The Fraudulent Preferences Act and was, therefore, called upon to deal with the issue as to the validity and applicability of the provisions of The Fraudulent Preferences Act. Perhaps realizing that his reasons were dissenting, he did so in a very short paragraph, which I quote [p. 34]:

> The appellant contends that The Fraudulent Preferences Act, is ultra vires of the legislation of the province. For the reasons given in *Re Panfab Corpn. Ltd.; Duro Lam Ltd. v. Last*, 15 C.B.R. (N.S.) 20, [1971] 2 O.R. 202, 17 D.L.R. (3d) 382, with which I agree, this contention must be rejected.

51 Upon the trustee in bankruptcy obtaining leave to appeal to this court, the respondent Countrywide Factors Ltd., in accordance with the rules of this court and in view of the fact that it wished to argue the ultra vires character of the provincial Fraudulent Preferences Act, applied to this court for directions and this court ordered that notice of two questions be served on the Attorney General of Canada and the Attorneys General of the provinces. The two questions were:

> 1. Whether The Fraudulent Preferences Act, R.S.S. 1965, Chapter 397, is *ultra vires* of the Legislature of the Province of Saskatchewan.
>
> 2. Alternatively, whether sections 3 and 4 of The Fraudulent Preferences Act, R.S.S. 1965, Chapter 397, while being within the legislative competence of the Legislature of the Province of Saskatchewan, are in conflict with valid legislation of the Parliament of the Dominion of Canada relating to bankruptcy and insolvency, namely, the Bankruptcy Act, R.S.C. 1970, Chapter B 3.

52 As will be demonstrated hereafter, the transaction attacked by the trustee in bankruptcy occurred on 19th November 1966 or, at any rate, not later than 20th March 1967.

53 Kozan Furniture (Yorkton) Ltd. was the subject of a receiving order in bankruptcy on 19th November 1968. Therefore the Bankruptcy Act provisions as to preferential transactions contained in s. 73 of the Bankruptcy Act, R.S.C. 1970, c. B-3, which provides:

> 73.(1) Every conveyance or transfer of property or charge thereon made, every payment made, every obligation incurred, and every judicial proceeding taken or suffered by any insolvent person in favour of any creditor or of any person in trust for any creditor with a view to giving such creditor a preference over the other creditors shall, if the person making, incurring, taking, paying or suffering the same becomes bankrupt within three months after the date of making, incurring, taking, paying or suffering the same, be deemed fraudulent and void as against the trustee in the bankruptcy.
>
> (2) Where any such conveyance, transfer, payment, obligation or judicial proceeding has the effect of giving any creditor a preference over other creditors, or over any one or more of them, it shall be presumed *prima facie* to have

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> been made, incurred, taken, paid or suffered with a view to giving such creditor a preference over other creditors, whether or not it was made voluntarily or under pressure and evidence of pressure shall not be receivable or avail to support such transaction.
>
> (3) For the purposes of this section, the expression 'creditor' includes a surety or guarantor for the debt due to such creditor,

has no application nor has s. 5 of The Fraudulent Preferences Act. In the Bankruptcy Act the interval between the transaction and the declaration of bankruptcy is limited to three months, and in The Fraudulent Preferences Act, s. 5 only applies if the attack is made within 60 days after the transaction. Therefore, in order to succeed, the appellant must have available to him the provisions of ss. 3 and 4 of the said Fraudulent Preferences Act. It is the submission of the respondent that either of those sections, or indeed the whole statute, is ultra vires of the province of Saskatchewan or that ss. 3 and 4, while being within the legislative competence of the legislature of the province, are in conflict with the legislation of the Parliament of Canada relating to bankruptcy and insolvency. That problem is one which has plagued the courts from 1894 on.

54 The Bankruptcy Act was enacted only in the year 1919, but in *A.G. Ont. v. A.G. Can.*, [1894] A.C. 189, the Judicial Committee dealt with the problem of whether s. 9 of an Ontario statute, the then counterpart of the present Ontario Assignments and Preferences Act, R.S.O. 1970, c. 34, was intra vires of the province of Ontario. It is to be remembered that s. 91(21) of the B.N.A. Act, 1867, granted exclusive legislative jurisdiction to the Parliament of Canada on subjects entitled "Bankruptcy and Insolvency". Section 9 of the Ontario statute, R.S.O. 1887, c. 124, read as follows:

> 9. An assignment for the general benefit of creditors under this Act shall take precedence of all judgments and of all executions not completely executed by payment, subject to the lien, if any, of an execution creditor for his costs, where there is but one execution in the sheriff's hands, or to the lien, if any, of the creditor for his costs who has the first execution in the sheriff's hands.

55 The Judicial Committee held that such a provision was within the constitutional powers of the province as granted in s. 92(13) of the B.N.A. Act, i.e., "Property and Civil Rights in the Province". The Lord Chancellor said at pp. 198-99:

> But it is argued that inasmuch as this assignment contemplates the insolvency of the debtor, and would only be made if he were insolvent, such a provision purports to deal with insolvency, and therefore is a matter exclusively within the jurisdiction of the Dominion Parliament. Now it is to be observed that an assignment for the general benefit of creditors has long been known to the jurisprudence of this country and also of Canada, and has its force and effect at common law quite independently of any system of bankruptcy or insolvency, or any legislation relating thereto. So far from being regarded as an essential part of the bankruptcy law, such an assignment was made an act of bankruptcy on which an adjudication might be founded, and by the law of the Province of Canada which prevailed at the time when the Dominion Act was passed, it was one of the grounds for an adjudication of insolvency.
>
> It is to be observed that the word 'bankruptcy' was apparently not used in Canadian legislation, but the insolvency law of the Province of Canada was precisely analogous to what was known in England as the bankruptcy law.
>
> Moreover, the operation of an assignment for the benefit of creditors was precisely the same, whether the assignor was or was not in fact insolvent. It was open to any debtor who might deem his solvency doubtful, and who desired in that case that his creditors should be equitably dealt with, to make an assignment for their benefit. The validity of the assignment and its effect would in no way depend on the insolvency of the assignor, and their Lordships think it clear that the 9th section would equally apply whether the assignor was or was not insolvent.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

56 And at pp. 200-201 continued:

> It is not necessary in their Lordships' opinion, nor would it be expedient to attempt to define, what is covered by the words 'bankruptcy' and 'insolvency' in sect. 91 of the British North America Act. But it will be seen that it is a feature common to all the systems of bankruptcy and insolvency to which reference has been made, that the enactments are designed to secure that in the case of an insolvent person his assets shall be rateably distributed amongst his creditors whether he is willing that they shall be so distributed or not. Although provision may be made for a voluntary assignment as an alternative, it is only as an alternative. In reply to a question put by their Lordships the learned counsel for the respondent were unable to point to any scheme of bankruptcy or insolvency legislation which did not involve some power of compulsion by process of law to secure to the creditors the distribution amongst them of the insolvent debtor's estate.
>
> In their Lordships' opinion these considerations must be borne in mind when interpreting the words 'bankruptcy' and 'insolvency' in the British North America Act. It appears to their Lordships that such provisions as are found in the enactment in question, relating as they do to assignments purely voluntary, do not infringe on the exclusive legislative power conferred upon the Dominion Parliament. They would observe that a system of bankruptcy legislation may frequently require various ancillary provisions for the purpose of preventing the scheme of the Act from being defeated. It may be necessary for this purpose to deal with the effect of executions and other matters which would otherwise be within the legislative competence of the provincial legislature. Their Lordships do not doubt that it would be open to the Dominion Parliament to deal with such matters as part of a bankruptcy law, and the provincial legislature would doubtless be then precluded from interfering with this legislation inasmuch as such interference would affect the bankruptcy law of the Dominion Parliament. But it does not follow that such subjects, as might properly be treated as ancillary to such a law and therefore within the powers of the Dominion Parliament, are excluded from the legislative authority of the provincial legislature when there is no bankruptcy or insolvency legislation of the Dominion Parliament in existence.

57 It will be seen, therefore, that the Judicial Committee in this decision only determined that a system providing for voluntary assisgnments enacted in a province prior to the enactment of any federal Bankruptcy Act was intra vires, but acknowledged that a subsequently enacted Bankruptcy Act by the federal Parliament might well overcome the provisions of the provincial statute. It would seem that the decision is quite silent as to the effect of provisions in a provincial Assignments and Preferences Act other than one permitting a voluntary assignment of debts except that one might well argue that by implication provisions in the provincial statute dealing with fraudulent preferences would be equally within the purview of the province under "property" and "civil rights" unless and until overcome by federal legislation ancillary to its power in bankruptcy and insolvency.

58 In 1922 Orde J. gave a decision in *Re Davison*, 5 C.B.R. 860, 52 O.L.R. 244, [1923] 4 D.L.R. 1049, in a matter where a mortgage was being attacked by a trustee in bankruptcy as void under The Fraudulent Conveyances Act, R.S.O. 1914, c. 105, and also The Assignments and Preferences Act, R.S.O. 1914, c. 134. The mortgagee submitted that if the transaction could not be avoided under s. 31 [now s. 73] of the Bankruptcy Act, 1919 (Can.), c. 36, it could not be set aside at all. In other words, that the provincial statutes aforesaid were no longer applicable in the province when bankruptcy occurred, having been superseded by the provisions of the Bankruptcy Act. At p. 861 the learned justice said:

> This is a startling suggestion, and, if sound, would turn back the clock for three centuries and enable a debtor to commit a deliberate fraud upon his creditors, and by holding off his bankruptcy for three months to validate the transaction. There is nothing in sec. 31 or in any other part of *The Bankruptcy Act* which either expressly or impliedly abrogates the existing law of each province as to the invalidity of fraudulent transactions. On the contrary, in the enumeration of the different kinds of acts of bankruptcy in sec. 3(*b*), it is clearly intended to include cases of fraudulent conveyances which are fraudulent quite independently of *The Bankruptcy Act*, those which are fraudulent under the Act being mentioned in par. (c). Rule 120 clearly contemplates other laws than *The Bankruptcy Act* itself, under which a transaction may be declared invalid, though, if the effect of the Act is as Mr. White contends, the Rules cannot nullify that effect.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

59 Orde J. was the first judge dealing with bankruptcy matters in Ontario after the enactment of the statute. The report books for the years following the enactment of the statute are filled with his wise decisions in reference to bankruptcy and, in my view, he firmly established the course of bankruptcy law in Ontario and largely affected the course of the law throughout Canada in the early years of bankruptcy administration. I am of the view that his observation, which I have cited, is a very sound one and is still applicable today. I might even go further: It is not only possible for a debtor to hold off his bankruptcy for three months in order to validate the transaction but it is quite possible for a creditor, improperly and fraudulently preferred, to support a debtor and enable him to postpone the date of his eventual declaration of bankruptcy beyond the three months.

60 The view expressed by Orde J. seems to have prevailed for a considerable length of time.

61 In *Hoffar Ltd. v. Can. Credit Men's Trust Assn. Ltd.*, [1929] 1 W.W.R. 557, 10 C.B.R. 369, 40 B.C.R. 454, [1929] 2 D.L.R. 73, leave to appeal refused [1929] S.C.R. 180, [1929] 2 D.L.R. 106, the Court of Appeal for British Columbia had considered a situation where a transfer had been made by a debtor less than 60 days before the debtor's assignment under the provisions of the Bankruptcy Act. The transaction was attacked on two grounds: firstly, that it was avoided by the provisions of s. 64 [now s. 73] of the Bankruptcy Act, R.S.C. 1927, c. 11, and, secondly, that it was utterly void as against the trustee under the provisions of s. 3(2) of The Fraudulent Preferences Act of British Columbia [R.S.B.C. 1924, c. 97]. It was found at trial and not contested on appeal that s. 64 of the Bankruptcy Act could not apply because it had not been proved that the transaction was made with a view to prefer one creditor over another and, in the Court of Appeal, it was also held that s. 3 of the provincial statute had been rendered inoperative by the enactment of s. 64 of the Bankruptcy Act. M. A. Macdonald J.A. said [at p. 561]:

> The Dominion statute adds however subsec. (2) quoted *ante*, stating when the view or intent to prefer shall be presumed. If it has the effect of giving a preference it is *prima facie* proof that it was made with that intent. That is a presumption and evidence may be adduced to rebut it. That right is given by the Dominion Act on a state of facts common to both Acts. The provincial statute denies that right. Given the insolvency as in the Dominion Act and the intent as in the Dominion Act ("with a view of") the transfer is utterly void under sec. 3(1) without any right to offer evidence to rebut it. And under sec. 3, subsec. (2), if action is taken within 60 days or if an assignment follows within 60 days the transfer is void.
>
> The provincial Act is not dealing with a new situation; the variation in words and figures does not affect the subject-matter. But the result is different. Under the provincial Act the transfer is void; under the Dominion Act it is deemed void with however the right to rebut. If this is given by Dominion legislation a provincial Act destroying it is *ultra vires* to the extent of the conflict. Under the Dominion Act the assignor has the benefit of that right. Under the provincial Act invalidity is an irrebuttable presumption. That is the conflict.

62 M.A. Macdonald J.A. added the very important comment [p. 562]:

> This is not to say that the trustee cannot resort to a provincial Act to impeach a transaction. Provincial legislation respecting fraudulent conveyances may be resorted to. The *Bankruptcy Act* does not abrogate provincial Acts simply because they deal with preferential transactions. But obviously both Parliaments cannot enact that one result shall follow in one case and a different result in the other. Counsel for respondent submitted that the section in the provincial Act deals with a topic not dealt with by the Dominion Act. I cannot agree. He also urged that there is no conflict where the Dominion Act voids a transaction on one ground and a provincial Act avoids it on other and additional grounds; in other words, the Dominion Act does not say that transactions of another kind shall be lawful. That is not this case. We are

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> dealing with legislative results following the same transaction and the results differ. That result in case of conflict must be determined by the Dominion Act. The test is, can both sections be enforced?

63 So, in *Hoffar*, the Court of Appeal for British Columbia acknowledged that, of course, valid federal legislation on the subject of bankruptcy and insolvency would overcome provincial legislation on the subject of property and civil rights but only to the extent of the conflict. In that case, the court found a conflict but foresaw cases where there would be no conflict and where, therefore, the provincial legislation would still be in full force and effect. Leave to appeal to this court in the *Hoffar* case was refused by Mignault J.

64 In *Re Pommier*, 11 C.B.R. 449, 65 O.L.R. 415, [1930] 4 D.L.R. 113, Fisher J.A. considered an application to set aside as preferential a transaction between the bankrupt and the creditor which took place more than three months before the making of the authorized assignment and which, therefore, was not within the prohibition in s. 64 [now s. 73] of the Bankruptcy Act. At pp. 116-17 the learned justice said:

> After careful consideration of the provisions of the Bankruptcy Act, the Assignments and Preferences Act and the decisions to which I shall make reference, I am unable to give effect to Mr. Hellmuth's contentions.
>
> I frankly admit that conflict is to be found when sec. 64 is read in connection with sec. 5 of the Assignments and Preferences Act and the following sections, except possibly sec. 12, and that, the Bankruptcy Act, being Dominion legislation, as to this conflict the Dominion Act prevails; but, in my opinion, sec. 64 does not attempt to interfere directly with provincial legislation dealing with the same subject-matter, because it is quite clear that s-ss. (3) and (4) of s. 4 of the Assignments and Preferences Act cover transactions not covered by the Bankruptcy Act, and in those respects are not in conflict with the Bankruptcy Act, and that these subsections are still operative; but, even if it could be said that these subsections do deal with the same subject-matter, it is not one of conflict but of 'overlapping'.

65 And at p. 119 said:

> It appears to me, and I am of opinion, that the combined effect of Rule 142, s. 64, and the other sections of the Acts to which I have referred, is to give to a trustee in bankruptcy, without special enabling words, power to impeach all fraudulent or preferential transactions which may by the Bankruptcy Act or provincial law be avoided; that neither the Assignments and Preferences Act nor the Fraudulent Conveyances Act has been abrogated, and that these Acts, apart from the conflicting sections mentioned, are still running concurrently with the provisions of the Bankruptcy Act and may be resorted to by a trustee under that Act, if it is found that relief cannot be obtained thereunder, or, to adopt the words of Macdonald, J.A., in the *Hoffar* case, unless on the same state of facts we find a different result arising, resort may be had to the provisions of whichever legislation fits the case.

66 So, therefore, another most eminent and experienced judge in bankruptcy matters came to the like conclusion that the provincial statute, insofar as it was not overcome by the provisions of the Bankruptcy Act, was still available to the trustee in bankruptcy.

67 However, the Court of Appeal for Ontario in *Re Trenwith*, 15 C.B.R. 372, [1934] O.R. 326, [1934] 3 D.L.R. 195, again considered a transaction allegedly preferential which had occurred much more than three months prior to the petition which resulted in the receiving order. Kerwin J., as he then was, had at trial set aside the impugned transaction using the provisions of The Assignments and Preferences Act, being of the opinion that he was so required by the decision in *Re Pommier*, supra.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

But upon appeal Masten J.A. said at p. 376:

> The question is, therefore, open for adjudication by this Court, and on a consideration of the cases of *A.G. Ont. v. A.G. Can.* [supra, at p. 200]; *Royal Bank of Can. v. Larue*, [1928] 1 W.W.R. 534, 8 C.B.R. 579, [1928] A.C. 187, (sub nom. *Bélanger v. Royal Bank of Can.)* [1928] 1 D.L.R. 945 , and *Hoffar Ltd. v. Can. Credit Men's Trust Assn. Ltd.* [supra] it seems clear to me that the common field of legislation respecting the distribution of the estates of insolvents having now become occupied by the Dominion *Bankruptcy Act*, the provisions of *The Assignments and Preferences Act* respecting the preference of one creditor over another have been thereby superseded and have ceased to have any operation. If I am right in this conclusion, the effect is to overrule the view expressed by Fisher, J.A., in *Re Pommier* [supra].

68 The Court of Appeal for Ontario, therefore, came to exactly the opposite conclusion, not to the actual decision in *Hoffar* but to the reservation made by M.A. Macdonald J.A., which I have cited above, and to a conclusion opposite to that reached by Fisher J.A. in *Re Pommier*. The conclusion, however, may well be considered obiter because Masten J.A. follows the statement which I have quoted above with a holding that, although the transaction could not be attacked under either s. 64 of the then Bankruptcy Act or under The Assignments and Preferences Act of the province, it could be attacked as a settlement under the then s. 60 [now s. 69] of the Bankruptcy Act.

69 The statement which I have quoted above, however, is plainly that by enacting the then s. 64 of the Bankruptcy Act the federal Parliament, enacting valid legislation on the subject of bankruptcy and insolvency, has covered the field and therefore cannot be reconciled with decisions to which I have referred which reduce the deleterious effect of the federal legislation to points of actual conflict only. The decision, however, has some support in this court and in the Courts of Appeal of the provinces. In *Re Bozanich; A. H. Boulton Co. v. Trusts & Guarantee Co.*, 23 C.B.R. 234, [1942] S.C.R. 130, [1942] 2 D.L.R. 145, this court considered whether a chattel mortgage was or was not a settlement within the meaning of the then s. 60 of the Bankruptcy Act and held it was not such a settlement. There seems to have been no allegation whatsoever that the transaction could be subject to attack under the provisions of the Ontario Assignments and Preferences Act or the Ontario Fraudulent Conveyances Act, but Duff C.J.C. said at p. 136:

> I may add that, in my opinion, the provisions of R.S.O. 1927, Chap. 162, in relation to preferences are superseded by section 64 of the *Bankruptcy Act*, and that the authority of the Ontario Legislature to enact such legislation is, in con sequence of the enactment of section 64, suspended in virtue of the concluding paragraph of section 91.

70 The statement is, of course, plainly obiter and it is not reflected in the reasons for judgment of Rinfret J., who came to the same result as did the chief justice.

71 In 1949, the Parliament of Canada enacted the Bankruptcy Act, 1949 Can., c. 14 (2nd Sess.) [in particular, s. 41(6)], which now appears as s. 50(6) of the statute and which provides:

> (6) The provisions of this Act shall not be deemed to abrogate or supersede the substantive provisions of any other law or statute relating to property and civil rights that are not in conflict with this Act, and the trustee is entitled to avail himself of all rights and remedies provided by such law or statute as supplementary to and in addition to the rights and remedies provided by this Act.

72 In *Totem Radio Supply Co. v. Stone* (1959), 29 W.W.R. 552, 38 C.B.R. 112 (B.C.), Whittaker J., sitting in single judge court, held that The Fraudulent Preferences Act, R.S.B.C. 1948, c. 132, was not in conflict with s. 64 [now s. 73] of the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Bankruptcy Act and at p. 553 said:

> Prior to 1949 there were conflicting decisions as to whether or not the dominion legislation entirely superseded provincial Acts dealing with preferences, but this matter is now resolved by sec. 41(6) of the *Bankruptcy Act* of 1949.

73 Other cases in the various provincial courts went either way but the next case which I shall consider is *A.G. Alta. v. Nash* (1964), 50 W.W.R. 155, 7 C.B.R. (N.S.) 92, (sub nom. *Re McIntosh-Marshall Equipment Ltd.; Nash v. Guelph Engineering Co.)* 48 D.L.R. (2d) 619. There the Appellate Division of the Supreme Court of Alberta held, confirming Milvain J. [48 W.W.R. 420, 7 C.B.R. (N.S.) 84], that The Fraudulent Preferences Act of Alberta, R.S.A. 1955, c. 120, was ultra vires. Johnson J.A. said at pp. 160-61:

> There can, I think, be no doubt that the impugned Act was *ultra vires* of the legislature when it was passed. Whatever can be said for similar legislation that was passed before the *Bankruptcy Act* became operative, this legislation, viewed in the light of s. 64, becomes an attempt to cover the same ground that section covers. The enlargement of the time from 60 days to one year must be viewed as an attempt to strengthen the remedy which sec. 64 gives to creditors. Sec. 4 cannot be looked upon as legislation which was intended to deal with contracts and which only incidentally and as part of a larger scheme dealt with matters which were within the scope of one or more of the subjects mentioned in sec. 91. This section is what it purports to be. Legislation intended to prevent a person 'at a time when he is in insolvent circumstances or is unable to pay his debts in full or knows that he is on the eve of insolvency' (4 [*a*]), from disposing of his property in such a manner as to prefer one creditor over another. It is exactly what sec. 64 of the *Bankruptcy Act* was passed to prevent. If it is not in pith and substance insolvency legislation under the earlier cases, it has become so under the enlarged definition and also by virtue of sec. 64 of the *Bankruptcy Act*.

74 Johnson J.A. cited s. 41(6) [now s. 50(6)] of the Bankruptcy Act, R.S.C. 1952, c. 14, and then continued [at p. 163]:

> Whittaker, J. of the British Columbia supreme court considered this amendment in *Totem Radio Supply Co. v. Stone* [supra] and as he could find no conflict between sec. 64 of the *Bankruptcy Act* and the section of the *Fraudulent Preferences Act*, RSBC, 1948, ch. 132 (similar to our Act), set aside a mortgage which had been given more than three months before the company became bankrupt. With respect, I must disagree with his conclusion. Having concluded, as previously stated, that there is a conflict between the two sections, it would follow that the section in the provincial Act is unaffected by the amendment.
>
> The court of appeal of Ontario again considered the *Assignments and Preferences Act*, RSO, 1960, ch. 25, in *Re Shelly Films Ltd.; Clarkson Co. v. Overland Finance Corpn.*, 4 C.B.R. (N.S.) 186, [1963] 1 O.R. 431, 37 D.L.R. (2d) 419, reversing 3 C.B.R. (N.S.) 94, [1961] O.W.N. 371 (C.A.), and held that sec. 12(1) of that Act was abrogated by sec. 64 of the *Bankruptcy Act*. Because no mention was made of the amendment to the *Bankruptcy Act* in that case, we are asked to assume that it had been overlooked and was not considered by that court. Judicial comity would make one hesitate to impute to the court of another province such an oversight. The case does point out the conflicts in the two Acts and it is much more reasonable to assume that the amendment was in fact considered by the court.
>
> It may be that certain sections of the *Fraudulent Preferences Act* are continued effective by the amendment to sec. 41 of the *Bankruptcy Act*, but because of the conflict between the section we are considering and sec. 64, sec. 4 is not one of them.

75 It would seem that Johnson J.A.'s judgment, although he commences with the statement that the Act is ultra vires, ends with the conclusion that only the section under attack in that particular decision was ultra vires. The particular section was s. 4, which avoided preferential transactions where an action had been brought within one year thereafter. The statute under

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

consideration in this appeal, the Saskatchewan Fraudulent Preferences Act, in ss. 3 and 4 makes no reference whatsoever to any time limit. The section which does make such reference and which creates a presumption is s. 5 and it is not advanced by the trustee.

76 In *Re Panfab Corpn.*, supra, Houlden J. considered an appeal from a registrar to whom an issue had been directed as to the validity of a security given by an individual to a corporation and held that s. 64A [en. 1966-67, c. 32, s. 11; now s. 74] did not apply. He continued at p. 24:

> The next issue is whether the transaction, not being a fraudulent preference because it does not come within s. 64A, can be attacked as a fraudulent conveyance. Counsel for the appellants gave notice to the Attorney General for Canada and the Attorney General for Ontario pursuant to s. 33 of The Judicature Act, R.S.O. 1960, c. 197, that he proposed to argue that The Fraudulent Conveyances Act, R.S.O. 1960, c. 154, was ultra vires of the legislature of the Province of Ontario, or ineffective in that it is legislation relating to either bankruptcy or insolvency which by s. 91, para. 21 of the B.N.A. Act, 1867, is under the exclusive legislative authority of the Parliament of Canada.

77 And at p. 25 he expressed the view that The Fraudulent Conveyances Act in Ontario was not in pith and substance bankruptcy legislation but was valid legislation as in reference to property and civil rights within s. 92(13) of the B.N.A. Act. He continued [p. 25]:

> The Fraudulent Conveyances Act is used constantly to attack transactions which have no connection with bankruptcy. It is an important part of the weapons available to creditors in recovering assets that have been fraudulently transferred by debtors. In my opinion, there is no conflict between the provisions of The Fraudulent Conveyances Act and the Bankruptcy Act. Section 41(6) of the Bankruptcy Act recognizes that provincial legislation such as The Fraudulent Conveyances Act exists and provides that the trustee is entitled to make use of such legislation in addition to the rights and remedies provided by the Bankruptcy Act.

78 Houlden J.'s decision is obiter, however, in that he found that the transaction was not within The Fraudulent Conveyances Act because it was bona fide. It is to be noted also that Houlden J.'s concern was with The Fraudulent Conveyances Act while this appeal is concerned with the exact provisions of ss. 3 and 4 of The Fraudulent Preferences Act of Saskatchewan. Perhaps it should also be noted that Houlden J., in the *Panfab* case, had inclined to the opposite conclusion in reference to this problem which he found, in his comment reported in (1960), 38 C.B.R. 114, to be one of great importance, and where he found the decision in *Re Trenwith* had been a block to trustees. Houlden J. does not mention *Re Trenwith* in his reasons for judgment in *Panfab*. It is to be remembered that *Re Panfab Corpn.* was not appealed to the Court of Appeal and we, therefore, have not an opportunity to determine whether that court had recanted from its view taken 35 years before in *Re Trenwith.*

79 In *Traders Finance Corpn. Ltd. v. Levesque*, 2 C.B.R. (N.S.) 52, [1961] S.C.R. 83, 26 D.L.R. (2d) 384, the court considered a transaction, allegedly preferential, occurring within three months before the declaration of bankruptcy. The attack upon the transaction, however, was not made until more than a year after the bankruptcy when the creditor — the trustee having refused to take the action — obtained the leave of the court to proceed under the provisions of s. 16 of the Bankruptcy Act [now s. 20]. The provisions of art. 1040 of the Civil Code purported to place a limitation period of one year upon such attack. This court, confirming the Court of Appeal of Quebec, by a majority judgment held that art. 1040 of the Civil Code would not apply because the action was taken within a year of the creditor obtaining knowledge of the payment as the said article provides. Locke J. did consider art. 1040 of the Civil Code and held that it had no application whatever to proceedings under the provisions of the Bankruptcy Act, saying at pp. 58-59:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> It may be said that provisions similar to those contained in the articles of the Civil Code to which I have referred are to be found in statutes of most of the provinces of Canada. They are to be found in British Columbia in the Fraudulent Preferences Act, R.S.B.C. 1948, c. 132, in Alberta in the Fraudulent Preferences Act, R.S.A. 1955, c. 120, in Saskatchewan in the Fraudulent Preferences Act, R.S.S. 1953, c. 362, in Manitoba in the Assignments Act, R.S.M. 1954, c. 11, and in Ontario in the Assignments and Preferences Act, R.S.O. 1950, c. 26. All of these statutes deal with the rights of creditors to set aside conveyances made by persons in insolvent circumstances, which have the effect of giving a creditor a preference over the others and all of them provide that, in the event of action being brought within a certain period of the date of the conveyance, it is to be held null and void. The remedies thus given are quite distinct from those given to the trustee in bankruptcy under s. 64 of the Bankruptcy Act. The right to enforce such claims by creditors does not depend upon the fact that the person making the transfer has been declared bankrupt and these rights may be enforced under the provincial statutes unless bankruptcy has intervened. This has been held in a number of cases in various provinces, which are to be found collected in the 3rd edition of Bradford and Greenberg on the Bankruptcy Act, at p. 158 *et seq.* In Quebec the limitation provided by art. 1040 only refers to proceedings under the articles mentioned.

80 One might infer from Locke J.'s words that once bankruptcy has intervened then the provincial statutes have no application even to a transaction occurring before the period covered by the present s. 73. I am not of the view that that is a proper implication from Locke J.'s words. I am assisted in coming to that conclusion by the decision of this court in *Gingras v. General Motors Products of Can. Ltd.*, [1976] 1 S.C.R. 426, 57 D.L.R. (3d) 705. There, the Court of Appeal of Quebec had confirmed a decision of the Superior Court which had dismissed a "motion to cancel preferential payments" instituted by the trustee in bankruptcy. The trustee had in such motion attacked a transaction which had occurred less than three months before the declaration of the bankruptcy but had not instituted the action within one year of his appointment as provided in art. 1040 of the Civil Code.

81 The defendant filed an exception relying on the said art. 1040 of the Civil Code and such exception was successful in both courts below. However, this court by a majority judgment held that the trustee, in taking action under s. 73 of the Bankruptcy Act to attack a transaction as a preference occurring within three months before the bankruptcy, was not affected by art. 1040 of the Civil Code and was controlled alone by the provisions of the Bankruptcy Act. de Grandpré J., dissenting, was of the opinion that in proceeding in the Superior Court the trustee was governed by the procedural provisions of the Civil Code and that therefore art. 1040 would apply to bar the action.

82 It is noted that Pigeon J., giving reasons concurred in by Martland and Dickson JJ., said at p. 437:

> I would therefore allow the appeal and dismiss the exception to dismiss submitted by respondent. This does not mean that the latter will not be entitled to rely on Art. 1040 in answer to a claim based on the goods taken back, if the trustee should contend that his petition allows him to go beyond the three months preceding the bankruptcy, and base a claim not only on the *Bankruptcy Act* but also on Arts. 1032 to 1040 *C.C.*

83 In my view, Pigeon J., therefore, expressed the view that in the attack upon transactions not within the three-month period provided by s. 73 of the Bankruptcy Act the trustee was free to use the provisions of the Civil Code as to preferential transactions.

84 de Grandpré J., in his dissenting reasons, said at p. 443:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> In my view, the *Bankruptcy Act* overrides the Paulian action only to the limited extent that it deals with acts in defraud of the debtor; all aspects of fraudulent action falling outside the provisions of the *Bankruptcy Act* may be considered in the light of the principles of the *Civil Code*.

85 Again, a plain statement that any reference to transactions outside of the narrow limits of the provisions of what is now s. 73 of the Bankruptcy Act, the Civil Code remained in full force and available to the trustee in bankruptcy.

86 I have dealt with what, in my view, are the main cases upon the subject in Canada. Upon considering them all, as well as the decision of the Judicial Committee in *A.G. Ont. v. A.G. Can.*, supra, I have come to the conclusion that the better view is to confine the effect of what is now s. 73 of the Bankruptcy Act to providing for the invalidity of transactions within its exact scope. To that extent, the Parliament of Canada, by valid legislation upon "bankruptcy" and "insolvency", has covered the field but has refrained from completely covering the whole field of transactions avoided by provincial legislation. I am of the opinion that the enactment in 1949 of the provisions now found in s. 50(6) of the Bankruptcy Act was a plain indication that Parliament recognized that provisions in provincial statutes dealing with preferential transactions were still valid provincial enactments in reference to "property" and "civil rights" and were valuable aids to trustees in bankruptcy in attacking the validity of such transactions and should be available to the said trustees in bankruptcy.

87 I am assisted in coming to this conclusion by the view which I believe was behind the Lord Chancellor's reasons in *A.G. Ont. v. A.G. Can.* that the words "bankruptcy" and "insolvency" in s. 91(21) of the B.N.A. Act were aimed at legislative schemes which had the purpose of governing the distribution of a debtor's property amongst his creditors. There may well be (and there are) provisions in such legislative schemes, i.e., the Bankruptcy Act, dealing with "property" and "civil rights". Such provisions are properly ancillary to the bankruptcy and insolvency legislation and, to the extent to which they go, overcome existing valid provincial legislation and bar future provincial legislation contra thereto but do not purport to extend beyond that point to invalidate other valid provincial legislation upon "property" and "civil rights".

88 I have, therefore, come to the conclusion that the provisions of ss. 3 and 4 of The Fraudulent Preferences Act of Saskatchewan are valid and subsisting provincial legislation available to the trustee in his attack upon the transactions with which this appeal is concerned. In my view, s. 3 of that statute, dealing with transactions taken with the intent to defeat, hinder, delay or prejudice creditors, is not as relevant as s. 4 which provides:

> 4. Subject to sections 8, 9, 10 and 11 every gift, conveyance, assignment or transfer, delivery over or payment of goods, chattels or effects or of bills, bonds, notes or securities or of shares, dividends, premiums or bonus in a bank, company or corporation, or of any other property real or personal, made by a person at a time when he is in insolvent circumstances or is unable to pay his debts in full or knows that he is on the eve of insolvency to or for a creditor, with intent to give that creditor preference over his other creditors or over any one or more of them, is void as against the creditor or creditors injured, delayed, prejudiced or postponed,

and is concerned with transactions taken with the intent to give one creditor preference over other creditors.

89 In order to determine whether that section applies to avoid the transaction in question in this appeal, a detailed analysis of the circumstances is necessary.

90 Kozan Furniture (Yorkton) Ltd. had carried on business for a period of years in Saskatchewan. Part of that business

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

was the sale of floor coverings, paints, draperies, interior decorating material, etc. The supplier of those items was Kennedy Flooring Limited of Winnipeg, a wholly-owned subsidiary of Gaultco Limited of Winnipeg. Another wholly-owned subsidiary of the said Gaultco was Countrywide Factors Limited. By some mysterious and unspecified arrangement, Countrywide Factors Limited became the accounting firm and the billing agent for Kennedy Flooring.

91 The three corporations, Gaultco Limited, Kennedy Flooring Limited and Countrywide Factors Limited, were all controlled by the same officers and we are not concerned with the arrangements between the three companies.

92 As early as 1965 Countrywide Factors Limited was unsatisfied with the payments being received from Kozan Furniture (Yorkton) Limited on its open account and placed Kozan Furniture (Yorkton) Limited on a "C.O.D." basis. The learned trial judge found — and it was confirmed by the majority on appeal — that by the spring of 1966 Kozan Furniture (Yorkton) Limited was not paying the accounts as they became due. One Tony Ollinger was the manager of the floor covering department in Kozan Furniture (Yorkton) Limited and he arranged with Kozan Furniture (Yorkton) Limited and its controlling shareholder, George E. Kozan, to purchase the floor covering inventory for the sum of $10,300. Of course, it was of crucial interest to Ollinger that he should continue to have Kennedy Flooring Limited supply him with stock. On 19th November 1966 two officers of Countrywide Factors went from Winnipeg to Yorkton, Saskatchewan, and conferred with George E. Kozan and Tony Ollinger. The two officers were Mr. David Albert Bowles, a director of Countrywide and also its solicitor, and Mr. Philip Douglas Medhurst, its credit manager. As a result of that conference, a document was drawn up and executed which read as follows:

> I, Tony Ollinger, agree to pay Countrywide Factors Ltd. $10,300.00 (more or less) representing sale of inventory of floor coverings, paint & Drapery as determined by stocktaking of Sept. 21/66; payment as follows:
>
> (a) Before Nov. 26/66 ...... $7,000.00
>
> (b) Before Jan. 31/67, the balance & int. at 7%
>
> (If substantially paid — say within $300.00 — this will be adequate compliance & any unpaid balance will be paid by the last day of Feb. 1967.)
>
> Countrywide will agree to the sale of said inventory on such compliance & will reduce the account of Kozan Furniture (Yorkton) Ltd. now at $25,000.00 (more or less) by the amount of said inventory price.
>
> George Kozan guarantees repayment of the account of Kozan Furniture (Yorkton) Ltd. as set out in his letter of Oct. 1/66 & attached. He & Kozan Furniture (Yorkton) Ltd. will give a debenture on the stock in the form attached, an assignment of book debts in Countrywide's form & a collateral mortgage on 76 and 80 Circlebrook Drive.

Kozan Furniture (Yorkton) Ltd. Per: 'George E. Kozan' 'Tony Ollinger'	Countrywide Factors Ltd. Per: 'D. A. Bowles'

93 At the same time and place George E. Kozan executed a personal guarantee of the debt to Countrywide and, in accordance with the agreement set out above, in February of 1967 Kozan Furniture (Yorkton) Limited granted to Countrywide Factors Limited a debenture in the sum of $35,512 covering all of its remaining assets. The floor coverings, which under the transaction had been transferred from Kozan Furniture (Yorkton) Limited to Tony and Rudolph Ollinger,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

were conveyed by a bill of sale which was, however, executed only on 15th February 1967. Again a mysterious company appears. That transfer was not made by Kozan Furniture (Yorkton) Limited, the owner of the inventory, but purportedly by a corporation entitled Kozan Interiors Limited and purportedly for a consideration of $10,300. The actual inventory of the material covered in the bill of sale had only amounted to $9,152.31 and that was the exact amount of the money paid by Ollinger to Countrywide under the provisions of the agreement of 19th November 1966 which I have set out in full above.

94 Kozan Interiors Limited was unknown to Kennedy Flooring Limited and, in fact, the learned trial judge refers to that corporation in the words [p. 122], "... if ever incorporated, which is unlikely, never carried on business and never owned the assets which were the subject of Ex. D 22" (the bill of sale of 17th February 1967). George E. Kozan attempted to explain the interjection of this corporate name. The learned trial judge referred to that explanation in the following words [p. 122]:

> Mr. Kozan weakly suggested that he made the mistake when he instructed Mr. Wentzell, the solicitor who drew Ex. D 22. I suppose it is the type of error made by a businessman who is in the throes of insolvency.

95 Another light may be thrown on the topic by a document produced at trial and marked as Ex. P10, which reads as follows:

> IN THE MATTER OF A CERTAIN SALE MADE UNDER THE BULK SALES ACT FOR THE PROVINCE OF SASKATCHEWAN.
>
> BETWEEN:
>
> Kozan Interiors Ltd.,
> of Yorkton, in the Province
> of Saskatchewan,
> -- and --
> Anthony Ollinger and Rudolf Ollinger
> both of Yorkton, in the Province of
> Saskatchewan,
>
> KNOW ALL MEN BY THESE PRESENTS that Country Wide Factors Ltd., the undersigned does for the purpose of Section 6 of the Bulk Sales Act for the Province of Saskatchewan, HEREBY RENOUNCE AND WAIVE any right which the said Country Wide Factors Ltd., has under the said Act against Anthony Ollinger and Rudolph Ollinger and against any right or claim to any of the goods, draperies, paints, floorings and materials covered in the sale agreement dated the 7th day of February, A.D. 1967.
>
> IN WITNESS WHEREOF Country Wide Factors Ltd., has hereunto set their hands and affixed their corporate seal on its behalf this 13th day of April A.D. 1967.
>
> Country Wide Factors Ltd.
>
> ____________________
>
> ____________________
>
> Secty-Treasurer.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

96 Certainly the transaction between Kozan Furniture (Yorkton) Limited and Ollinger, whereby the title to the floor coverings was transferred from one to the other but the sale price was paid to Countrywide Factors, was one within the provisions of The Bulk Sales Act, R.S.S. 1965, c. 389, but if the vendor had, in truth, been Kozan Interiors Limited, then that company had no creditors and The Bulk Sales Act provisions would not have applied. It is, I think, significant in dealing with the bona fides of the transaction. After that transfer of the inventory of floor coverings, etc., Kozan Furniture (Yorkton) Limited was said to have paid to Countrywide Factors the following sums:

1966, November $1,000.00

1967, February 1,000.00

March 6,000.00

April 2,152.31

June 1,000.00

September 500.00

97 As a matter of fact, the payments in March, April and June were payments by Ollinger totalling $9,152.31, the amount of the inventory and the amount which he had agreed to pay to Countrywide Factors by the agreement of 9th November 1966.

98 Kozan Furniture (Yorkton) Limited continued doing business, after a fashion, until 19th November 1968, when a receiving order in bankruptcy was made out against the company.

99 On 10th July 1969 the trustee in bankruptcy moved for an order that the proceeds of the sale be declared a fraudulent preference contra to the provisions of ss. 3 to 6 of The Fraudulent Preferences Act and for an order directing the respondent to pay the sum of $10,300 to the said trustee. MacPherson J. directed a trial of that issue and then himself conducted the trial. MacPherson J., in written and detailed reasons, found that the transaction was a preference and directed that the trustee recover from Countrywide the sum of $9,152.31 and that the debenture given by Kozan Furniture (Yorkton) Limited to Countrywide Factors Limited be declared void. The majority of the Court of Appeal — Maguire J.A. giving reasons which were concurred in by Woods J.A. — reversed that judgment, holding that the trustee had failed to establish that Kozan Furniture (Yorkton) Limited, on 19th November 1966, the date of the agreements aforesaid, or in March 1967, the date when the payments under that agreement to Countrywide Factors Limited commenced, was insolvent, unable to pay its debts in full or on the eve of bankruptcy. Hall J.A. dissented, being of the opinion that Kozan Furniture (Yorkton) Limited was, on either of those dates and throughout, insolvent. Hall J.A. expressed the view that The Fraudulent Preferences Act was intra vires and applicable.

100 It would appear, from a perusal of the reasons given by Maguire J.A. for the majority, that he was of the opinion that in order to bring himself within the benefit of the section the trustee had to prove that the debtor was not only in insolvent circumstances but was also unable to pay his debts in full and knew that he was on the eve of insolvency. A reading of the section would seem to make it quite clear that those three are alternatives and not conjunctives and that all the trustee had to prove was that the debtor was insolvent or that he was unable to meet his debts in full or that he knew he was on the eve of insolvency. I am not concerned particularly with the last-named alternative as that is quite subjective and I do not find it necessary to pierce the mind of George E. Kozan.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

101 I am in agreement with the view expressed by Hall J.A. that although the burden is on the trustee to prove the insolvency of the debtor at the time of the transaction — as the burden is always upon the plaintiff to prove his case — the trustee may adduce such a prima facie case which will call upon the defendant to adduce evidence to rebut that prima facie evidence. It must be remembered that a trustee is often faced with a situation, which faced this trustee when he was not appointed until November 1968, where he had to go back into the past and establish an insolvency which he alleged had existed in November 1966. The trustee in such a situation must deal with records which are, in many cases, fragmentary and may well be intentionally deceptive. He has no means of checking the actual stock in trade which existed at that date and sometimes can place little dependence upon the evidence of the debtor. In the particular case I am of the opinion, as were Hall J.A. and MacPherson J., that the trustee as plaintiff (here appellant) had certainly shown such a prima facie case.

102 Maguire J.A., giving reasons for the majority of the Court of Appeal, said [at p. 25]: "It is established that Kozan as early at least as spring of 1966 was not paying all accounts as they became due."

103 In *Ladore v. Bennett*, [1939] 2 W.W.R. 566, 21 C.B.R. 1, [1939] A.C. 468, [1939] 3 All E.R. 98, [1939] 3 D.L.R. 1, Lord Atkin said at p. 571:

> Insolvency is the inability to pay debts in the ordinary course as they become due; and there appears to be no doubt that this was the condition of these corporations.

104 I am of the opinion that the statement by Maguire J.A. which I have quoted above would have been sufficient to have disposed of the issue and justify a holding that the debtor was in insolvent circumstances within the words of s. 4 of The Fraudulent Preferences Act at the time of the transaction. However, there is no need to put the decision on that single ground for I have come to the conclusion that the debtor was unable to pay his debts in full at the date of the transaction.

105 The Court of Appeal, as I have said, seemed to be of the opinion that the difficulty facing the trustee was that he could not prove that the debtor was unable to pay his debts in full or, to use the words appearing in *Walter v. Adolph Lumber Co.* (1915), 8 W.W.R. 351 at 355, 23 D.L.R. 326 (Alta.), that "[he] had not the means of paying [his creditors] in full out of the assets realized upon a sale for cash or its equivalent", because the trustee could not prove the extent of the inventory possessed by the debtor on 19th November 1966. It is true that the debtor had no inventory which could be produced and to which a dollars-and-cents value could be attached. Mr. Medhurst, credit manager of the respondent, however, had given some evidence where he, in a very casual manner, estimated the value of that inventory at that time at about $75,000, admitting however that he was no expert on furniture valuations. Since Mr. Medhurst was anxious to uphold the transaction and, therefore, to see that the debtor had assets sufficient to cover his liabilities, he certainly would not have underestimated the value of the inventory. Therefore, even if we take that valuation of $75,000, we have this situation (and I am quoting here figures adopted by Maguire J.A. and appearing in his majority reasons for the Court of Appeal at p. 28):

Trade accounts and liability to bank	$111,199.16	
Shareholders loan	22,702.62	

Total liabilities		$133,901.78
Accounts receivable, subject to some deductions for disputed items	$ 44,099.62	
Delivery truck -- ... [subsequently sold by trustee]	1,000.00	

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Total of those assets	$ 45,099.62

106 Even adopting those figures, the other assets in inventory, that is, stock in trade and store fixtures, would have had to amount to $88,802.16; yet, two full years later, those remaining assets were sold for only $31,200, which sum was subject to a landlord's lien for $3,200, leaving a net amount in the trustee's hands of only $28,000 not $88,000. In addition, the accounts receivable shown in Maguire J.A.'s figures at $44,099.62 were reduced in December 1966 on the instructions of the debtor's auditor to $23,598.51 so that to establish that the debtor could have paid all his debts by realization of his assets would have required an increase in the value of the stock in trade and fixtures of another $20,600, requiring the valuation of that stock in trade and fixtures at over $100,000, an amount for which there has been no scintilla of evidence.

107 I agree with Hall J.A. when he said [at p. 31]: "There was, in my opinion, evidence from which the trial Judge could infer the value of the stock-in-trade was nowhere near $100,000."

108 Under the circumstances, I am of the opinion that the trustee had produced a prima facie case to show that the debtor was unable to pay his debts in full by realization of his assets in November 1966. As MacPherson J. remarked [at p. 126]:

> Two years is a long time to continue in a state of insolvency, that is true, but the evidence indicates that that is what happened. There was no time in that period when it was not insolvent. Perhaps its affairs were worse, perhaps better from time to time, but there was a continued state of insolvency.

109 For these reasons, I am of the opinion that the appeal should be allowed, the judgment of the Court of Appeal of Saskatchewan quashed and the judgment at trial restored. As I have already said, the questions upon which leave was given to the various intervenors should be answered as follows:

110 Q. 1: No.

111 Q. 2: Sections 3 and 4 of The Fraudulent Preferences Act are not in conflict with the provisions of the Bankruptcy Act.

112 The appellant should have his costs against the respondent in the Court of Appeal and in this court. There will be no costs to intervenors.

***Beetz J.*:**

113 I have had the advantage of reading the opinions of the chief justice and of Spence J. I agree with Spence J. To his

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

reasons for judgment I would, however, like to add some of my own.

114 The power to repress fraud by avoiding fraudulent conveyances and preferences is an indisputable part of provincial jurisdiction over property and civil rights. The risk of fraud is increased when a debtor finds himself in a situation of impending or actual insolvency and, in my view, provincial laws can, without undergoing a change in nature, focus upon that situation as upon a proper occasion to attain their object. Given their purpose, they do not cease to be laws in relation to property and civil rights simply because they are timely and effective or because Parliament could enact similar laws in relation to bankruptcy and insolvency.

115 Insolvency has been defined by Lord Thankerton in *A.G. B.C. v. A.G. Can.; Reference re Farmers' Creditors Arrangement Act*, [1937] A.C. 391 at 402:

> In a general sense, insolvency means inability to meet one's debts or obligations; in a technical sense, it means the conditio or standard of inability to meet debts or obligations, upon the occurrence of which the statutory law enables a creditor to intervene, with the assistance of a Court, to stop individual action by creditors and to secure administration of the debtor's assets in the general interest of creditors; the law also generally allows the debtor to apply for the same administration.

116 The primary meaning of "insolvency" in s. 91(21) of the Constitution is insolvency in the technical sense, not in the general sense. This Lord Thankerton made clear just a few lines after the passage quoted above: with respect to the jurisdiction of Parliament under s. 91(21) he referred to "the statutory conditions of insolvency which enabled a creditor or the debtor to invoke the aid of the bankruptcy laws".

117 There is no common law of bankruptcy and insolvency in the technical sense, but the disruptions resulting from insolvency in the general sense had of necessity to be taken into account by general legal systems such as the common law and the civil law. Insolvency lies at the core of those parts of the common law and of the civil law which relate to such matters as mortgage, pledge, pawning, suretyship and the securing of debts generally which are implicitly or explicitly predicated on the risk of insolvency and which produce their full effect when the risk has been converted into reality; so it is with the rules which determine the rank of privileges and hypothecs or which ordain that an insolvent or bankrupt debtor shall lose the benefit of the term (art. 1092 of the Quebec Civil Code). Some of the most fundamental principles of the civil law are expressed in arts. 1980, 1981 and 1982 of the Quebec Civil Code:

> Art. 1980. Whoever incurs a personal obligation, renders liable for its fulfilment all his property, moveable and immoveable, present and future, except such property as is specially declared to be exempt from seizure.
>
> Art. 1981. The property of a debtor is the common pledge of his creditors, and where they claim together they share its price rateably, unless there are amongst them legal causes of preference.
>
> Art. 1982. The legal causes of preference are privileges and hypothecs.

118 Although not expressly referred to, insolvency forms the web of these articles; there would be little need for them, particularly the last two, were it not for insolvency. But I cannot be persuaded that they are not laws relating to property and civil rights.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

119 When the exclusive power to make laws in relation to bankruptcy and insolvency was bestowed upon Parliament, it was not intended to remove from the general legal systems which regulated property and civil rights a cardinal concept essential to the coherence of those systems. The main purpose was to give to Parliament exclusive jurisdiction over the establishment by statute of a particular system regulating the distribution of a debtor's assets. However, given the nature of general legal systems, the primary jurisdiction of Parliament cannot easily be exercised together with its incidental powers without some degree of overlap in which case federal law prevails. On the other hand, provincial jurisdiction over property and civil rights should not be measured by the ultimate reach of federal power over bankruptcy and insolvency any more than provincial competence in relation to the administration of justice can be determined by every conceivable and potential use of the criminal law power. This, I believe, is the general import of the *Voluntary Assignments* case, *A.G. Ont. v. A.G. Can.*, [1894] A.C. 189. The Judicial Committee declared that the validity of the provision it had to consider and of the assignments made under the authority of that provision did not depend on the insolvency of the assignor: an assignment was also open "to any debtor who might deem his insolvency doubtful" [p. 199]. All that one can say is that legislation of the type considered in the *Voluntary Assignments* case presents little interest for prosperous persons; it is of concern chiefly to debtors in strained circumstances whose solvency is, at best, uncertain. It should be noted that the impugned voluntary assignments enactment did not only deal with assignments: it also provided that an assignment for the general benefit of creditors should take *precedence* of all judgment and of all executions not completely executed by payment.

120 I am reinforced in those views by a consideration of the Civil Code of Lower Canada, 1866, in light of An Act respect ing Insolvency, c. 17 of the Statutes of the Province of Canada, 1864. Both were enacted at a time when Confederation was being discussed. The French title of The Insolvent Act of 1864, was "l'Acte concernant la Faillite, 1864", the word "faillite" being the one now currently used to translate the word "bankruptcy". In spite of its English title, the Act was in fact a bankruptcy Act. It applied to all persons in Upper Canada and to traders only in Lower Canada and it contained detailed provisions relating to fraudulent conveyances and preferences. Nevertheless, the Civil Code comprised a section of nine articles (arts. 1032 to 1040 inclusive) entitled "Of the avoidance of contracts and payments made in fraud of creditors", applicable to traders and to non-traders alike except where The Insolvent Act was to prevail. The legislative history of those articles was set forth by Pigeon J. in *Gingras v. General Motors Products of Can. Ltd.*, [1976] 1 S.C.R. 426, 57 D.L.R. (3d) 705. Some have been amended. It will suffice to quote a few of them as they then read:

> 1034. A gratuitous contract is deemed to be made with intent to defraud, if the debtor be insolvent at the time of making it.
>
> 1035. An onerous contract made by an insolvent debtor with a person who knows him to be insolvent is deemed to be made with intent to defraud.
>
> 1036. Every payment by an insolvent debtor to a creditor knowing his insolvency, is deemed to be made with intent to defraud, and the creditor may be compelled to restore the amount or thing received or the value thereof, for the benefit of the creditors according to their respective rights.
>
> 1037. Further provisions concerning the presumption of fraud and the nullity of acts done in contemplation of insolvency are contained in The Insolvent Act of 1864.

121 Article 17.23 of the Code defines "bankruptcy" ("faillite") as meaning "the condition of a trader who has discontinued his payments"; insolvency was left undefined, the word being clearly used by the Code in the general sense. Even though arts. 1034, 1035 and 1036 are predicated on insolvency, the commissioners appointed for codifying the laws of Lower Canada in civil matters would have been astonished had they been told that those articles formed no part of the civil law: except perhaps for art. 1036, which appears to be an improvement of relatively modern origin (although it was not considered new law), such provisions were derived from a division of Roman law called Paulian law and, from time immemorial, had constituted a pivot of the civil law system. Other provisions of the Code are of the same nature and also depend on insolvency, such as art. 803 (revocation of a gift made by an insolvent debtor), and art. 2023 (hypothec consented to by an insolvent debtor). Other provisions still, although not expressly predicated on insolvency, are related to insolvency and to the protection of creditors, for instance, art. 655 (the creditors of an heir who renounces a succession to their prejudice

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

can have the renunciation rescinded and accept the succession in his stead).

122 The constitutional validity of such provisions is not in issue: they antedate Confederation and were continued by s. 129 of the Constitution. The only issue which could arise with respect to them is whether they are in conflict with federal law. But the content and integrity of the Civil Code are indicative of the extent of provincial jurisdiction over property and civil rights: *Citizens Insur. Co. of Can. v. Parsons* (1881), 7 App. Cas. 96 at 110-11. The fact that there existed a statutory scheme of bankruptcy and insolvency to which the Code explicitly referred as to a distinct and specific body of law, without curtailing for that reason its own normal ambit, illustrates how the respective domains of property and civil rights and of bankruptcy and insolvency were viewed during the very period when the federal union was being discussed; it also reveals how it was intended that the distribution of powers should operate with respect to those domains.

123 In *Reference re Debt Adjustment Act, 1937 (Alta.); A.G. Alta. v. A.G. Can.*, [1943] 1 W.W.R. 378, 24 C.B.R. 129, [1943] A.C. 356, [1943] 1 All E.R. 240, [1943] 2 D.L.R. 1, in *Can. Bankers Assn. v. A.G. Sask.*, 35 C.B.R. 135, [1956] S.C.R. 31, (sub nom. *Re Moratorium Legislation)* [1955] 5 D.L.R. 736, and in *Reference re Orderly Payment of Debts Act, 1959 (Alta.)*, 1 C.B.R. (N.S.) 207, [1960] S.C.R. 571, 23 D.L.R. 449, the various provincial laws found ultra vires were predicated upon insolvency. But they went further and set up elaborate statutory schemes involving one or more of the following features: the denial of creditors' access to courts or the restriction of their right to enforce their claims, the establishment of administrative boards, mediation, composition, arrangements, moratoriums, consolidation orders, staying of proceedings and the relief of debtors from liability to pay their debts. No such features are to be found in the presently impugned Saskatchewan statute where all that is at stake is the avoidance of fraudulent acts for the better enforcement of civil obli gations. Some doubt was expressed in the *Orderly Payment of Debts Act* reference at pp. 576-77 as to whether the *Voluntary Assignments* case would have been decided in the same way at a later date even in the absence of federal legislation on the subject of bankruptcy and insolvency. However, even if this doubt was not expressed in an obiter dictum, I would regard it as questioning not the general principles enunciated in the *Voluntary Assignments* case, but their application in that particular instance. Accordingly, I do not think that those previous decisions of the Judicial Committee and of this court preclude my abiding by my conclusions: laws provincial in their purpose, object and nature as those under attack cannot be rendered ultra vires because of virtual federal paramountcy; they can only become inoperative in case of actual repugnancy with valid federal laws.

124 On this latter point, I believe the test of repugnancy to be applied in this case should not differ from the one which was admitted in *Provincial Secretary of P.E.I. v. Egan*, [1941] S.C.R. 396, 76 C.C.C. 227, [1941] 3 D.L.R. 305; *O'Grady v. Sparling*, 33 W.W.R. 360, 33 C.R. 293, [1960] S.C.R. 804, 128 C.C.C. 1, 25 D.L.R. (2d) 145, and *Ross v. Registrar of Motor Vehicles* (1973), 23 C.R.N.S. 319; provincial law gives way to federal law in case of operational conflict. Even if the test be one of conflict of legislative policies entailing no operational inconsistency and depending solely "upon the intention of the paramount legislature" as was said by Dixon J. in a passage of *Ex parte McLean* (1930), 43 C.L.R. 472 at 483, quoted by Pigeon J. in the *Ross* case (at p. 326), I am of the view that s. 50(6) of the Bankruptcy Act provides a clear indication that Parliament, far from intending to depart from the rule of operational conflict, did in fact aim at the highest possible degree of legal integration of federal and provincial laws. Attacks upon transactions within the three-month period provided by s. 73 of the Bankruptcy Act constitute a minimum but the trustee in bankruptcy is entitled to avail himself of all other rights and remedies provided by provincial law "as supplementary to and in addition to the rights and remedies provided by" the Bankruptcy Act.

125 I would dispose of this appeal as is proposed by Spence J.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 23

1979 CarswellOnt 195
Ontario Supreme Court, In Bankruptcy

Garrett, Re

1979 CarswellOnt 195, 30 C.B.R. (N.S.) 150

RE GARRETT

Steele J.

Heard: May 24, 1979
Judgment: June 6, 1979

Counsel: *H. R. Poultney, Q.C.*, for applicants.
H. Cartwright, Q.C., for respondent, Kenneth Garrett.

Subject: Corporate and Commercial; Insolvency; Contracts; Torts

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy --- Avoidance of transactions prior to bankruptcy — Fraudulent and illegal transactions — General

Bankruptcy --- Avoidance of transactions prior to bankruptcy — Practice and procedure

Fraud and Misrepresentation --- Fraudulent conveyances — Practice and procedure — Burden of proof — Transactions between near relatives — Corroboration

Fraudulent conveyances — Transfer of property — Near relatives — Necessity for corroboration — Affidavit sworn before agent or employee of solicitor acting for party — The Bankruptcy Act, ss. 73, 74, 157(9) — Bankruptcy R. 21.

Under the provisions of s. 157(9) of the Bankruptcy Act, the court has power to permit the affidavits which do not comply with Bankruptcy R. 21 to be considered as being sufficient, provided that no substantial injustice would be caused thereby.

Where transactions for the transfer of land take place between near relatives under suspicious circumstances which have the effect of defeating the claims of creditors, the persons upholding the transaction must furnish corroborative evidence to support the transaction. Where the transfer of property in effect deprived the bankrupt of all his property with the necessary consequence that there was nothing left for his creditors, the necessary inference that should be drawn is that the transfer is fraudulent.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

In order for the principle set out in *Mulcahy v. Archibald* (1898), 28 S.C.R. 523, to apply, there must be a pre-existing debt that would justify the transaction and the making of the transfer as security therefor or payment therefor.

In addition to the provisions of ss. 73 and 74 of the Bankruptcy Act the provisions of the Fraudulent Conveyances Act and the Assignments and Preferences Act are available to a creditor on an application to set aside the preference or conveyance that has been established.

Table of Authorities

Cases considered:

Bank of N.S. v. Zgurski (1970), 14 C.B.R. (N.S.) 185, 72 W.W.R. 464 (Alta.) — *applied*

Re Dougmor Realty Holdings Ltd; Fisher v. Wilgorn Invts. Ltd., [1967] 1 O.R. 66, 10 C.B.R. (N.S.) 141, 59 D.L.R. (2d) 432, reversed [1968] 1 O.R. 61, 11 C.B.R (N.S.) 153, 65 D.L.R. (2d) 419 (C.A.) — *applied*

Mulcahy v. Archibald (1898), 28 S.C.R. 523 — *distinguished*

Robinson v. Countrywide Factors Ltd., [1977] 2 W.W.R. 111, 23 C.B.R. (N.S.) 97, 72 D.L.R. (3d) 500, (sub nom. *Kozan Furniture (Yorkton) Ltd. v. Countrywide Factors Ltd.)* 14 N.R. 91 — *applied*

Statutes considered:

Bankruptcy Act, R.S.C. 1970, c. B-3, ss. 73, 74, 157(9).

Assignments and Preferences Act, R.S.O. 1970, c. 34.

Fraudulent Conveyances Act, R.S.O. 1970, c. 182.

Mortgages Act, R.S.C. 1970, c. 279.

Rules considered:

Bankruptcy R. 21.

Application to have conveyance by bankrupt set aside.

***Steele J.*:**

1 On opening, counsel for the applicant moved that affidavits flied on behalf of the respondent should not be considered on the grounds that they were sworn before the solicitor acting for the party on whose behalf the affidavits were to be used,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

contrary to R. 21. It was discovered that the affidavit filed on behalf of the applicant was also sworn before an agent or employee of the solicitor acting for him. Both parties consented to the application proceeding as if the affidavits were sufficient. I am of the opinion that under the provisions of s. 157(9) of the Bankruptcy Act, R.S.C. 1970, c. B-3, the court has power to permit the affidavits to be considered as being sufficient even if there was no consent. No substantial injustice would be caused by proceeding, and I ruled that the affidavits were sufficient.

2 This application is for a declaration that a conveyance by the bankrupt to her father-in-law, Kenneth Garrett, of parts of lots 8 and 9, concession 2, in the township of Loughborough, is null and void pursuant to the provisions of the Fraudulent Conveyances Act, R.S.O. 1970, c. 182, and the Assignments and Preferences Act, R.S.O. 1970, c. 34. I am of the opinion that, in addition to the provisions of ss. 73 and 74 of the Bankruptcy Act, the provisions of the Fraudulent Conveyances Act and the Assignments and Preferences Act are available to a creditor on an application to set aside a preference or conveyance that has been established: *Robinson v. Countrywide Factors Ltd.*, [1977] 2 W.W.R. 111, 23 C.B.R. (N.S.) 97, 72 D.L.R. (3d) 500, (sub nom. *Kozan Furniture (Yorkton) Ltd. v. Coutrywide Factors Ltd.)* 14 N.R. 91.

3 In the present case, the provisions of ss. 73 and 74 of the Bankruptcy Act do not apply because the conveyance in question took place more than 12 months prior to the petition for a receiving order. However, s. 75 of the Bankruptcy Act applies to protect a conveyance if adequate valuable consideration has been given and if the conveyance took place in good faith before the date of the bankruptcy and the transferee was not, at the time of the conveyance, in receipt of any notice of any act of bankruptcy committed by the bankrupt. For reasons that I will state later, I find that the transaction took place before the date of bankruptcy but that there was not adequate valuable consideration for the transfer in question, that the transferee was not acting in good faith, and that he had notice of an act of bankruptcy committed by the bankrupt, namely, the bankrupt's failure to meet her obligations as they generally fell due. Based on his own affidavit, he had this notice as early as 1973. I therefore find that the conveyance in question is not a conveyance protected by s. 75, and I turn to the application to set aside the conveyance under the Fraudulent Conveyances Act.

4 There is conflicting evidence in the affidavit material filed upon which there has been no cross-examination. Where there is conflict, I prefer the evidence contained in the registrar's abstract and the certified copies of the various documents attached to the affidavit of the applicant, H. Robert Sheppard.

5 On or about 9th April 1973 the bankrupt purchased approximately 100 acres of land comprising parts of lots 8 and 9 at a price of $21,500. The deed was not registered until 16th April 1974. The funds for this purchase came from a bank loan secured by a note signed by the bankrupt and her father, Clifton Silver (hereinafter referred to as "Silver"). Subsequently, Silver repaid the bank, and the bankrupt gave him a mortgage for $22,500 to secure the money that he had advanced to her. The mortgage expressly provided that there would be no interest and that the whole principal sum would become due on 2nd August 1975. It also provided that the mortgagee would give partial discharges covering any part of the property that might be sold, upon payment of a pro rata portion of the sum received from the sale from the land sold.

6 In June 1975 the bankrupt sold a parcel of land to McGinnis for a sale price of $13,200. Silver gave a partial discharge of mortgage covering this land. Although the actual partial discharge of mortgage was not produced, the consideration shown in the abstract is $1. Silver also received a mortgage from McGinnis in the amount of $10,700. This mortgage also was not produced, but there is nothing that indicates that it was other than a normal mortgage for valuable consideration between McGinnis and Silver. Although it was argued otherwise, there is nothing in the material filed that sheds any further light on this transaction.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

7 In December 1975 a solicitor, acting on behalf of Silver, wrote the bankrupt, stating that the full amount of the mortgage was still owing and demanding payment thereof and threatening foreclosure proceedings in the event of non-payment. While the evidence is somewhat unsatisfactory I can only conclude that Silver received no payment from the bankrupt as consideration for the partial discharge of mortgage granted in June 1975 and that as of December 1975 the full amount of the mortgage was still owing.

8 In January 1976 the bankrupt sold an additional parcel of land to Fraser for $9,400, and in March 1976 she sold an additional parcel of land to White for $8,500. On 16th March 1976 Silver gave a partial discharge of mortgage covering these two parcels of land in which he states that he received $11,879.96 on account of the mortgage. This partial discharge of mortgage was given notwithstanding that the demand had been for the full amount in December 1975. I therefore find that after this payment there was outstanding and owing on the Silver mortgage an amount of $10,620.04.

9 The bankrupt and her husband took an action against the applicant, Robert Sheppard, and in May 1976, at the conclusion of the trial, the action was dismissed with costs being awarded to Mr. Sheppard. These costs were not then determined but subsequently, on taxation on 24th November 1977, they were fixed at $5,499.

10 By deed dated 3rd December 1976 and registered on 21st January 1977, the bankrupt conveyed the lands in question to the respondent, Kenneth Garrett. The affidavit of land transfer tax, sworn to by the bankrupt, provides that the total consideration was $22,500, stated to be paid by the debt of $22,500 owing by the bankrupt to her father-in-law being discharged by the transfer. The affidavit also indicates that there was a balance of existing encumbrances owing at the date of transfer of $22,500. According to the registered title at that time, this affidavit is obviously incorrect because, first, there was no interest of Kenneth Garrett shown in the lands by way of mortgage and, secondly, there was no amount of $22,500 owing as an existing encumbrance because of the payment of $11,879.96 that had been made in March 1976.

11 In September 1977 Kenneth Garrett conveyed the lands in question to himself, his wife and his son, and the affidavit of land transfer tax attached to that conveyance sworn to by the respondent shows that there was $15,000 paid in cash as consideration. He subsequently brought an unopposed application for partition and sale, and on 8th December 1977 a partition order was issued dividing the lands among Kenneth Garrett, his wife and his son. On 7th April 1978, the bankrupt was so declared. On 1st May 1978 a discharge of the Silver mortgage was registered. This discharge was dated and the affidavits attached thereto were sworn on 1st December 1976. It was signed by Silver and, therefore, there are no records in the Registry Office of any assignment of the mortgage from Silver to Kenneth Garrett.

12 On 20th April 1978 the respondent, Garrett, and his son conveyed a part of the land to Selle for a consideration of $12,400.

13 While full descriptions of all the individul conveyances to the bona fide purchasers, such as White, McGinnis and Selle, were not before me because reference was made to reference plans, it is obvious that, at the time that the bankrupt conveyed all of her remaining interest in the lands to Kenneth Garrett, there was a very substantial acreage and frontage still held by her. Based on the sale prices to the bona fide purchasers, it is also obvious that the price of $15,000 stated in the conveyance from Kenneth Garrett to himself, his wife and his son, was totally inadequate.

14 The affidavit of Kenneth Garrett filed stated that he took over the mortgage from Silver on or about 24th March 1976,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

upon payment to him of $11,879.96, and that the face value of the mortgage was $22,500. The amount paid, according to the affidavit, is exactly the same as the amount that was stated to have been paid to Silver at the time that he gave his partial discharge of mortgage, relating to the White and Fraser sales. It is therefore doubtful that this amount was for the balance owing on the mortgage, but it would appear more accurately to reflect that Kenneth Garrett in fact paid the amount for the partial discharge of mortgage rather than the bankrupt, thus allowing the bankrupt to keep the total sale price on the White and Fraser sales. If Kenneth Garrett's statement is accurate, then it would be more logical that he would have taken an assignment of the total mortgage from Silver at that time, of which there is no evidence, and in fact there is the contradictory evidence that indicates that Silver gave a partial discharge of mortgage in consideration of this exact payment and that the discharge of the total mortgage was not signed by Silver until 1st December 1976. It is obvious that in both March and December 1976 there was a large acreage and frontage of lands still held by the bankrupt and that the value thereof was substantially in excess of $22,500 and much in excess of any lesser amount. I find that the respondent not only knew of the insolvency of the bankrupt at the time of the conveyance to him, but that he also knew that the lands were worth far more than any amount owing on the mortgage or the total amount of $39,264.96 set out in his affidavit as being the amount of advances by him to the bankrupt and her husband.

15 One additional fact should be noted, and that is that the respondent concedes that at the present time the bankrupt and her husband are living on a part of the lands in question in a residence that he has erected for their use.

16 In the affidavit filed by the respondent he states that his son and his family have been substantially dependent upon him from 1973 until the present time and sets out a statement of sums advanced to the bankrupt and his son. He states that when Silver threatened to foreclose the mortgage he offered to take it over and pay him off, that he did pay him the sum of $11,879.96 as stated, that at that time the bankrupt and his son were substantially indebted to him, and that he took the mortgage as security for this debt. He further states that it later became apparent that "my daughter-in-law could not pay this mortgage". He then makes the somewhat conflicting statement that it later became apparent that the bankrupt could not pay this mortgage so that it was agreed between the bankrupt and himself that she would deed the land to him and that, in fact, she executed a deed to him in the month of November 1976. He explains that the stated consideration in the deed was $22,500, which was the face amount of the mortgage, but that actually his daughter-in-law was indebted to him for considerably more than that at the time and that upon paying off the Silver mortgage he took a discharge of the mortgage rather than an assignment since his daughter-in-law was prepared at that time to deed the land to him in satisfaction or partial satisfaction of the above-described debt. I find the statements in the respondent's affidavit to be conflicting, contradictory and confusing with respect to the consideration and with respect to the time at which various matters are alleged to have taken place.

17 On the evidence, I am not satisfied that there was any intention on the part of Kenneth Garrett that he should ever be repaid the advances that he made to the bankrupt and her husband. He deposes that they were dependent upon him. This does not mean that he loaned money to them with the intention that they would repay.

18 I am of the opinion that, where a transaction such as this has taken place between near relatives under suspicious circumstances and has the effect of defeating the claims of creditors, the persons upholding the transaction must furnish corroborative evidence to support the transaction: *Bank of N.S. v. Zgurski* (1970), 14 C.B.R. (N.S.) 185, 72 W.W.R. 464 (Alta.). This transfer in effect deprived the bankrupt of all her property with the necessary consequence that there was nothing left for her creditors, and the necessary inference that should be drawn is that the transfer was fraudulent. In addition, I am satisfied in this case that the debtor was insolvent at the time of the transfer. While the facts of the *Bank of N.S. v. Zgurski* case are not similar to the present case, I am satisfied that the respondent was aware of the insolvency of the bankrupt and was aware that the value of the property that he was acquiring was far in excess of any loans or advances that he had made to the bankrupt. In addition, after the transfer, he continued to make advances to the bankrupt and her husband to provide for their accommodation and also subsequently erected a dwelling, on the very land in question, for their use. The principles stated in *Re Dougmor Realty Holdings Ltd.; Fisher v. Wilgorn Invts. Ltd.*, [1967] 1 O.R. 66, 10 C.B.R. (N.S .) 141, 59 D.L.R.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(2d) 432, reversed on other grounds [1968] 1 O.R. 61, 11 C.B.R. (N.S.) 153, 65 D.L.R. (2d) 419 (C.A.), are also applicable. I am satisfied that the transaction in question defeated the creditors and that, although it was voluntary, it involved a substantial asset. There was not adequate consideration, nor was this a bona fide transaction because of the knowledge of both the grantor and grantee. I am satisfied that the grantee, namely, the respondent herein, participated in the fraudulent intent to defeat the creditors of the bankrupt.

19 There is no corroborative evidence which, if available, could easily have been provided. It was not, and this reinforces my belief that the transaction was not a bona fide transaction. The suspicious circumstances of the transfer of the property at or about the time of the taxation of the costs of one of the applicants together with the close relationship between the parties make a prima facie case that the conveyance was fraudulent.

20 The respondent raised the defence that he took an assignment of the mortgage and therefore, under the principle set out in *Mulcahy v. Archibald* (1898), 28 S.C.R. 523, he is protected because he is taking and assuming the responsibility of a pre-existing debt regardless of intent.

21 Even if I accept that the respondent paid an amount to Silver in consideration for the assignment of the mortgage, which I have found he did not, the question is: Was there a pre-existing debt from the bankrupt to the transferee? There is no evidence as to how much of the alleged advances made to the bankrupt and her husband was properly attributable to the bankrupt as opposed to her husband, and I am also satisfied that there was no intention that these advances be repaid. I am therefore of the opinion that there was no pre-existing debt that justified the transaction and the making of the transfer as security therefor or payment therefor.

22 In addition, the respondent submited that, because he paid off the mortgage held by Silver, he stands in the shoes of Silver and, under the provisions of the Mortgages Act, R.S.O. 1970, c. 279, had valid security for the amount of $22,500 against the lands, that this was the consideration set out in the conveyance, and that therefore it was a valid transaction. In view of the conflicting evidence and my finding that the respondent paid the amount for the partial discharge of mortgage only, I find that he did not take an assignment of the mortgage and that he did not pay off the mortgage, and therefore he does not stand in the shoes of Silver. For this reason the principles set out in the Mortgages Act are inapplicable.

23 For the above reasons a declaration will issue that the conveyance from the bankrupt to Kenneth Garrett registered as instrument 286257 is null and void pursuant to the provisions of the Fraudulent Conveyances Act; and that the trustee in bankruptcy of the estate of Marie Marion Garrett is the owner of all of the lands covered thereby other than the lands conveyed to Wayne Douglas Selle and Constance Madeline Selle by instrument registered as No. 305751; and that Kenneth Garrett and Wayne Garrett hold the proceeds of the sale to Selle as trustees for the trustee in bankruptcy.

24 The applicants are entitled to their costs against the estate of the bankrupt.

Application granted.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 24

Case Name:
Oliver v. McLaughlin

**Oliver v.
McLaughlin et ux.**

[1893] O.J. No. 11

24 O.R. 41

Ontario High Court of Justice
Queen's Bench Division

Armour C.J. and Falconbridge J.

June 26, 1893.

Fraudulent Conveyance -- Action to Set Aside -- Plaintiff not an Execution Creditor -- Appropriate Relief -- Demurrer to Relief Prayed -- Rule 384 -- 13 Eliz. ch. 5 -- Status of Plaintiff -- Claim upon Implied Contract to pay Mortgage -- Proof of Contract -- Voluntary Conveyance -- Fraudulent Intent.

1. Where a creditor brings his action to set aside as fraudulent a conveyance made by his debtor of his property, without first obtaining judgment and execution, be must sue on behalf of all the creditors of the debtor, and in such action his relief will be confined to setting aside the conveyance, leaving him to resort to some independent proceeding to obtain execution against the property comprised in such conveyance.
2. A demurrer to the relief prayed in respect of the cause of action, and not to the cause of action itself, will not now be allowed. Rule 384 referred to.
3. The protection of 13 Eliz. ch. 5 is not confined to creditors only, but extends to creditors and others who have lawful actions; and in this case, where, before the impeached conveyance was made, all the moneys secured by a mortgage, subject to which the plaintiff had conveyed the mortgaged lands to the fraudulent grantor, had fallen due, the plaintiff had at the time of the making of the conveyance a lawful action upon the implied contract of his vendee to pay the moneys secured by the mortgage; and this implied contract was sufficiently proved against the fraudulent grantee by proof of the mortgage and of the conveyance by the plaintiff to the fraudulent grantor subject to the mortgage.

4. Where a conveyance is voluntary, it is only necessary to shew fraudulent intent on the part of the grantor.

---

1 THE plaintiff by his statement of claim alleged: (1) That by deed under the Act respecting Short Forms of Conveyances, dated the 21st February, 1889, he conveyed to the male defendant certain lands in the town of Essex, subject to a mortgage made by the plaintiff to one Brodie for $500 and interest thereon, due and payable on the 3rd October, 1891, which mortgage the male defendant agreed to assume and pay off and to indemnify the plaintiff against all liability thereon, but the male defendant did not do so; and on the 27th October, 1892, the plaintiff obtained in this Division of the High Court a judgment for $653 and costs against the male defendant, which still remained due and unpaid. (2) That on the 21st February, 1889, and up to the time of the conveyance thereinafter mentioned, the male defendant was seized in fee of certain lands in [24 OR Page42] the township of Colchester North which were available for the payment of the debts of the male defendant, and he had no other property available for the payment thereof. (3) That by a conveyance dated the 30th October, 1891, and registered on the 9th November, 1891, the male defendant granted and conveyed to the female defendant these last mentioned lands. (4) That the female defendant was the wife of the male defendant. (5) That no consideration was given or paid by the female defendant to the male defendant for the conveyance, but it was made voluntarily for the purpose of fraudulently protecting the lands from the claim of the plaintiff and the other creditors of the male defendant, and would have the effect of preventing the plaintiff and the other creditors of the male defendant from realizing their claims against him, and was so made with the full intent on the part of the defendants to defraud the plaintiff and the other creditors, and to defeat, delay, and hinder them from obtaining payment of their claims.

2 And the plaintiff claimed: (1) That the conveyance from the male to the female defendant might be set aside and declared null and void as against the plaintiff and the other creditors of the male defendant. (2) That the land therein described might be sold and the proceeds applied in payment of the amounts justly due to the plaintiff and the other creditors of the male defendant. (3) And such further relief as to the Court might seem meet.

3 The male defendant by his statement of defence: (1) Denied the allegations in the statement of claim. (2) Specially denied that the alleged conveyance was made for the purpose of fraudulently protecting the lands from the claims of the plaintiff or others. (3) Denied that he ever made any conveyance or the conveyance mentioned with the intent of defrauding the plaintiff or others, or of defeating, delaying, or hindering him or them, and denied that the conveyance in question had such effect. (4) Alleged that at the date of the alleged conveyance he owned other lands than those mentioned in such conveyance [24 OR Page43] free of incumbrances, and other real and personal property sufficient to satisfy all claims against him, and still owned a great part thereof. (5) Alleged that the plaintiff was not, at the date of such conveyance, a creditor of his, and had no legal claim whatever against him. (6) Denied that such conveyance was a voluntary conveyance, and said that, if made, it was made for good and valuable consideration. (7) Alleged that the plaintiff induced him to purchase the lands in the town of Essex by fraudulent misrepresentations as to the value thereof made for the purpose of inducing him to purchase the same, and that he had in consequence of such misrepresentations suffered great loss and damage, and he claimed the same from the plaintiff and the right to set off the same against the alleged judgment. (8) Claimed the right at the trial to still further demur to other portions of the statement of claim.

4 The male defendant also demurred to so much of the statement of claim as claimed that the lands should be sold and the proceeds applied in payment of the amounts justly due to the plaintiff and other creditors, on the ground that the plaintiff had not alleged such facts as shewed that he or any other creditors on behalf of whom he sued had any lien, either legal or equitable, upon the lands, and upon other grounds sufficient in law.

5 The female defendant also delivered a statement of defence, in which she repeated most of the allegations made by her co-defendant, and also alleged that, at the date of the conveyance to her, she had no knowledge that her co-defendant was indebted to the plaintiff in any sum whatever, or that he was bound to indemnify him as alleged. She also demurred on the same grounds as her co-defendant.

6 The plaintiff joined issue upon these defences, and, in reply to the 7th paragraph of the defence of the male defendant, said that the matter therein alleged was pleaded by that defendant in his defence in a former action in this Court wherein this plaintiff was plaintiff and that defendant was defendant, and wherein judgment was given for [24 OR Page44] the plaintiff, which action was that referred to in the 1st paragraph of the statement of claim, and the matter thereof was res judicata and the male defendant was estopped from pleading the same.

7 The action was tried at the Spring Sittings, 1893, of this Court at Sandwich by STREET, J.

8 It appeared that the plaintiff, on the 3rd October, 1888, by indenture of mortgage of that date conveyed the lands in the town of Essex to one Brodie, for securing the sum of $500, payable on the 3rd October, 1891, with interest thereon annually at the rate of eight per centum per annum. That on the 21st February, 1889, the plaintiff by indenture of bargain and sale of that date, for the consideration of $500, conveyed the said lands to the male defendant subject to the said mortgage. That thereafter the male defendant paid some money on account of the interest payable by the said mortgage. That the principal, with some arrears of interest, having fallen due upon the said mortgage, and the plaintiff, being pressed by Brodie for payment, had several conversations with the male defendant in which he urged him to pay off the mortgage, and on the 19th October, 1891, the plaintiff's solicitors, by the plaintiff's instructions, wrote to the male defendant that they were instructed by the plaintiff to take proceedings to compel him to pay the mortgage. That on the 30th day of October, 1891, the plaintiff was served with a writ of summons by Brodie to recover the amount due upon the said mortgage by virtue of the covenant therein, and on that day wrote two letters to the male defendant, one of which he sent by post and one by special messenger, informing him that he had been served with the said writ, and urging to come and settle the mortgage at once. That by indenture of bargain and sale dated the 30th day of October, 1891, and registered on the 9th day of November, 1891, the male defendant, for the expressed consideration of $500, conveyed to the female defendant the north-west quarter of lot 24 on the south [24 OR Page45] side of the Malden Road, in the township of Colchester North, said to be worth $2,500, or $2,600. That Brodie obtained judgment against the plaintiff on his covenant contained in the mortgage for the amount of the principal money and interest due thereon. That on the 4th day of March, 1892, the plaintiff brought an action against the male defendant to compel payment by him of the said mortgage money, and judgment was recovered therein on the 11th day of November, 1892, by the plaintiff against the male defendant for the sum of $653, and costs to be taxed. That this action was commenced on the 11th day of February, 1892. That the female defendant was not aware that the conveyance of the

said land had been made to her till, as she said, it was given to her by her husband after it was registered.

9 The learned Judge held on the evidence there was no consideration for the conveyance from the husband to the wife, that it was a voluntary conveyance, and was fraudulent and void as against creditors; and gave judgment declaring that the said conveyance was voluntary and was fraudulent and void as against the plaintiff and the other creditors of the defendant Thomas McLaughlin, and should be set aside; and ordered and adjudged accordingly, with full costs of the action, including the costs of the demurrer; with reference to the Deputy Clerk of the Crown at Sandwich to take the usual accounts and make the usual inquiries, and if the amount found due to the plaintiff and the other creditors and costs of suit should not be paid within one year from the report, the property in question should be sold to realize the same, with the costs of sale.

10 At the Easter Sittings of the Divisional Court, 1893, the defendants moved to reverse and set aside the said judgment and to enter judgment for the defendants, dismissing the plaintiff's action with costs and allowing the demurrer of the defendants with costs, upon the ground that the said judgment was contrary to law, evidence, and the weight of evidence, and that, upon the facts given in evidence [24 OR Page46] upon the trial, the judgment should have been in favour of the defendants, and more particularly upon the following grounds:

> 1. That the plaintiff was a creditor of the defendant Thomas McLaughlin by reason only of a judgment by consent obtained nearly a year subsequent to the execution and delivery of the impeached conveyance, and the plaintiff was therefore in the position of a subsequent creditor, and, there being no sufficient evidence of any intent to defeat his claim nor any pre-existing debts unpaid, was not in a position to maintain this action.
>
> 2. That if there was a pre-existing liability on the part of the defendant Thomas McLaughlin to the plaintiff, it was by reason only of an alleged right to indemnity in respect of moneys secured by mortgage, and it was not shewn in evidence by how much, if at all, the amount secured exceeded the value of the security, and the plaintiff was not therefore at the date of the impeached conveyance a creditor of the defendant within the meaning of this Act.
>
> 3. That as against the defendant Hannah Caroline McLaughlin the plaintiff did not prove himself a creditor of Thomas McLaughlin, inasmuch as Hannah Caroline McLaughlin was a stranger to the action by which the plaintiff recovered judgment against the defendant Thomas McLaughlin, and the exemplification of judgment and pleadings in the said action could not be used against the defendant Hannah Caroline McLaughlin as evidence of a debt.
>
> 4. That the plaintiff was not necessarily delayed, hindered, or defeated in obtaining payment of his debt, if any, by the impeached conveyance, because the defendant Thomas McLaughlin had at the time this conveyance was executed other property more than sufficient to pay all liabilities, including the plaintiff's;

and because default had been made in respect of the mortgage more than a year prior to the execution of the conveyance attacked, and more than two years before the said judgment was obtained, [24 OR Page47] and no effort was made during that time to enforce performance of the obligation, if any, to pay the mortgage money.

5. That valuable consideration had been given and was proved for this conveyance from the defendant Thomas McLaughlin to Hannah Caroline McLaughlin, and no fraud was shewn on the part of either of the defendants, and certainly none on the part of the defendant Hannah Caroline McLaughlin.

6. The plaintiff did not allege nor prove that he or any other creditor was an execution creditor of the defendant Thomas McLaughlin, and there was no evidence of actual fraud, and the plaintiff was therefore not in a position to maintain this action.

7. The judgment was in any case wrong in directing a sale of the said land without regard to the right of the defendant Hannah Caroline McLaughlin to dower therein, as if the conveyance is set aside she is entitled to obtain dower in the said lands in priority to any claim of the plaintiff thereto.

8. And on the argument of this motion the defendants will contend that, no actual fraud having been shewn, the defendant Thomas McLaughlin was not a proper party to the action, and that the action should, therefore, have been dismissed as against him with costs. And also that the plaintiff not having alleged in his statement of claim that he was an execution creditor of the defendant Thomas McLaughlin, the demurrer of the defendants to so much of the plaintiff's statement of claim as asked for equitable execution should have been allowed with costs; and the defendants will ask upon the foregoing, among other grounds, and upon the evidence, that the plaintiff's action be dismissed with costs, and the judgment, in so far as it directs a sale of the property described in the impeached conveyance, be varied by refusing the prayer for equitable execution; or for such other judgment as to the Court may seem right; and for payment by the plaintiff to the defendants of the costs of the action, including the costs of the motion. [24 OR Page48]

11 The motion was argued before ARMOUR, C.J., and FALCONBRIDGE, J., on the 25th of May, 1893.

12 Aylesworth, Q.C., for the defendants. The judgment of the trial Judge sets aside the conveyance. He inferred that there was an actual intent to defraud. I submit that was not a proper inference to draw from the evidence. No intention existed to defeat this claim. The male defendant considered the plaintiff's threat was not serious. He was not under any contract to pay off the mortgage; he had merely bought the plaintiff's equity of redemption. Even if it was a voluntary conveyance, he was in a position to make a voluntary settlement at the time he conveyed to his wife. At this time the plaintiff was not in a position to set the conveyance aside. His claim was not a debt; it was merely a right to sue to compel the male defendant to discharge the mortgage debt. The plaintiff is in fact a subsequent creditor and has no status: Masuret v. Mitchell, 26 Gr. 435; Clark v. Hamilton Provident and Loan Society, 9 O. R. 177. The plaintiff did not shew that the land was insufficient to pay the mortgage. No attempt was made to sell the land. The case is within the principle of Ex p. Mercer, 17 Q. B. D. 290; Real Estate Loan Co. v. Yorkville and Vaughan Road Co., 9 O. R. 464; Cameron v. Cusack, 17 A. R. 489; Darling v. Price, 27 Gr. 331; Struthers v. Glennie, 14 O. R. 726. If the conveyance was not a purely voluntary one, the intent of the wife must be shewn. She had no knowledge of this claim of the plaintiff; the most that can be said is that she knew her husband had bought a mortgaged property. The decree goes too far at any rate, for when the plaintiff began this action he was not an execution creditor, and he cannot, therefore, have equitable execution: McCall v. McDonald, 13 S. C. R. 247; Longeway v. Mitchell, 17 Gr. 190. Finally, if the judgment stands, the wife's rights as dowress should be preserved.

13 W. H. Blake, for the plaintiff. The form of the decree is right; a simple contract creditor can bring the action, as decided in Longeway v. Mitchell, 17 Gr. 190. As to the [24 OR Page49] facts, the findings of the learned Judge should stand. He heard the evidence of the defendants, and did not believe it. As to the status of the plaintiff, I refer to Allen v. Furness, 20 A. R. 34; Boyd v. Robinson, 20 O. R. 404; May on Fraudulent Conveyances, 2nd ed., p. 166.

14 Aylesworth, in reply.

15 June 26, 1893. The judgment of the Court was delivered by ARMOUR C.J. (after setting out the facts):-- It seems to be well settled that where a creditor brings his action to set aside a fraudulent conveyance made by his debtor of his property without first obtaining judgment and execution against his debtor, he must sue on behalf of all the creditors of his debtor, and in such case his relief in such action will be confined to setting aside the fraudulent conveyance, leaving him to take some independent proceedings if he wishes to have execution against the property so fraudulently conveyed: Reese River Silver Mining Co. v. Atwell, L. R. 7 Eq. 347; Longeway v. Mitchell, 17 Gr. 190; McCall v. McDonald, 13 S. C. R. 247.

16 The plaintiff in this case brought his action to set aside as fraudulent the conveyance of the land made by the male defendant to the female defendant without first obtaining judgment and execution against the male defendant, and rightly brought it on behalf of all the creditors of the male defendant; but the only relief he can obtain is the setting aside the said conveyance, and he must resort to the judgment he has since obtained, and to execution to be issued thereon, to realize out of the said land his judgment debt and costs.

17 The judgment, therefore, of my learned brother must be varied by confining it to the setting aside the fraudulent conveyance of the land made by the male to the female defendant.

18 The demurrer in this case would have been successful [24 OR Page50] under the system of special pleading which flourished in the Court of Chancery before the Judicature Act came into force: Abbott v. Canada Central R. W. Co., 24 Gr. 579.

19 But since the Judicature Act came into force, such a demurrer is no longer allowable, for it is not a demurrer to the cause of action, but only to the relief prayed in respect of the cause of action, and the demurrer in this case was therefore properly overruled: Con. Rule 384.

20 The protection of the statute 13 Eliz. ch. 5 is not confined to creditors only, but extends to creditors and others who have lawful actions, etc.

21 And upon the conveyance by the plaintiff to the male defendant of the land subject to the mortgage to Brodie there arose in favour of the plaintiff an implied contract on the part of the male defendant to pay the moneys secured by the said mortgage as they respectively fell due: Beatty v. Fitzsimmons, 23 O. R. 245.

22 And all the moneys secured by the said mortgage having fallen due before the making of the conveyance by the male to the female defendant, the plaintiff had at the time of the making thereof a lawful action against the male defendant upon his said implied contract, and was by reason thereof entitled to maintain this action to set aside the said conveyance, as devised and contrived to delay, hinder, and defraud him of his said lawful action.

23 This implied contract was sufficiently proved against the female defendant by the proof made at the trial of the mortgage to Brodie and the conveyance by the plaintiff of the land so mortgaged to the male defendant, subject to the said mortgage.

24 If it was necessary for the plaintiff, in the circumstances of this case, to shew that the land mortgaged to Brodie was insufficient in value to satisfy the said mortgage, it was, in our opinion, abundantly shewn out of the mouth of the male defendant.

25 That the conveyance from the male to the female defendant was devised and contrived by the male defendant with the intent of defrauding the plaintiff of his lawful action, there can, upon the evidence, be no doubt. [24 OR Page51]

26 Nor can there, upon the evidence, be any doubt that it was a voluntary conveyance, and that the pretended consideration was trumped up after the making of the conveyance in the vain effort to support it.

27 The learned Judge has found that it was entirely voluntary and was made by the male defendant for the purpose of defrauding the plaintiff.

28 It is only where a conveyance is made upon good consideration that it is necessary under the statute in order to set it aside to shew the fraudulent intent, of both parties to it. But where a conveyance is voluntary, it is only necessary to shew the fraudulent intent of the maker of it.

29 The judgment will, therefore, be that the conveyance from the male to the female defendant is fraudulent and void as against the plaintiff and the other creditors of the male defendant, and that, as against the plaintiff and such other creditors, it be set aside with costs, including the costs of the demurrer, and that this motion be dismissed with costs.

qp/s/qlkam/qlcla

Tab 25

Case Name:
Oliver v. McLaughlin

Oliver v.
McLaughlin et ux.

[1893] O.J. No. 11

24 O.R. 41

Ontario High Court of Justice
Queen's Bench Division

Armour C.J. and Falconbridge J.

June 26, 1893.

Fraudulent Conveyance -- Action to Set Aside -- Plaintiff not an Execution Creditor -- Appropriate Relief -- Demurrer to Relief Prayed -- Rule 384 -- 13 Eliz. ch. 5 -- Status of Plaintiff -- Claim upon Implied Contract to pay Mortgage -- Proof of Contract -- Voluntary Conveyance -- Fraudulent Intent.

1. Where a creditor brings his action to set aside as fraudulent a conveyance made by his debtor of his property, without first obtaining judgment and execution, be must sue on behalf of all the creditors of the debtor, and in such action his relief will be confined to setting aside the conveyance, leaving him to resort to some independent proceeding to obtain execution against the property comprised in such conveyance.
2. A demurrer to the relief prayed in respect of the cause of action, and not to the cause of action itself, will not now be allowed. Rule 384 referred to.
3. The protection of 13 Eliz. ch. 5 is not confined to creditors only, but extends to creditors and others who have lawful actions; and in this case, where, before the impeached conveyance was made, all the moneys secured by a mortgage, subject to which the plaintiff had conveyed the mortgaged lands to the fraudulent grantor, had fallen due, the plaintiff had at the time of the making of the conveyance a lawful action upon the implied contract of his vendee to pay the moneys secured by the mortgage; and this implied contract was sufficiently proved against the fraudulent grantee by proof of the mortgage and of the conveyance by the plaintiff to the fraudulent grantor subject to the mortgage.

4. Where a conveyance is voluntary, it is only necessary to shew fraudulent intent on the part of the grantor.

---

1 THE plaintiff by his statement of claim alleged: (1) That by deed under the Act respecting Short Forms of Conveyances, dated the 21st February, 1889, he conveyed to the male defendant certain lands in the town of Essex, subject to a mortgage made by the plaintiff to one Brodie for $500 and interest thereon, due and payable on the 3rd October, 1891, which mortgage the male defendant agreed to assume and pay off and to indemnify the plaintiff against all liability thereon, but the male defendant did not do so; and on the 27th October, 1892, the plaintiff obtained in this Division of the High Court a judgment for $653 and costs against the male defendant, which still remained due and unpaid. (2) That on the 21st February, 1889, and up to the time of the conveyance thereinafter mentioned, the male defendant was seized in fee of certain lands in [24 OR Page42] the township of Colchester North which were available for the payment of the debts of the male defendant, and he had no other property available for the payment thereof. (3) That by a conveyance dated the 30th October, 1891, and registered on the 9th November, 1891, the male defendant granted and conveyed to the female defendant these last mentioned lands. (4) That the female defendant was the wife of the male defendant. (5) That no consideration was given or paid by the female defendant to the male defendant for the conveyance, but it was made voluntarily for the purpose of fraudulently protecting the lands from the claim of the plaintiff and the other creditors of the male defendant, and would have the effect of preventing the plaintiff and the other creditors of the male defendant from realizing their claims against him, and was so made with the full intent on the part of the defendants to defraud the plaintiff and the other creditors, and to defeat, delay, and hinder them from obtaining payment of their claims.

2 And the plaintiff claimed: (1) That the conveyance from the male to the female defendant might be set aside and declared null and void as against the plaintiff and the other creditors of the male defendant. (2) That the land therein described might be sold and the proceeds applied in payment of the amounts justly due to the plaintiff and the other creditors of the male defendant. (3) And such further relief as to the Court might seem meet.

3 The male defendant by his statement of defence: (1) Denied the allegations in the statement of claim. (2) Specially denied that the alleged conveyance was made for the purpose of fraudulently protecting the lands from the claims of the plaintiff or others. (3) Denied that he ever made any conveyance or the conveyance mentioned with the intent of defrauding the plaintiff or others, or of defeating, delaying, or hindering him or them, and denied that the conveyance in question had such effect. (4) Alleged that at the date of the alleged conveyance he owned other lands than those mentioned in such conveyance [24 OR Page43] free of incumbrances, and other real and personal property sufficient to satisfy all claims against him, and still owned a great part thereof. (5) Alleged that the plaintiff was not, at the date of such conveyance, a creditor of his, and had no legal claim whatever against him. (6) Denied that such conveyance was a voluntary conveyance, and said that, if made, it was made for good and valuable consideration. (7) Alleged that the plaintiff induced him to purchase the lands in the town of Essex by fraudulent misrepresentations as to the value thereof made for the purpose of inducing him to purchase the same, and that he had in consequence of such misrepresentations suffered great loss and damage, and he claimed the same from the plaintiff and the right to set off the same against the alleged judgment. (8) Claimed the right at the trial to still further demur to other portions of the statement of claim.

4 The male defendant also demurred to so much of the statement of claim as claimed that the lands should be sold and the proceeds applied in payment of the amounts justly due to the plaintiff and other creditors, on the ground that the plaintiff had not alleged such facts as shewed that he or any other creditors on behalf of whom he sued had any lien, either legal or equitable, upon the lands, and upon other grounds sufficient in law.

5 The female defendant also delivered a statement of defence, in which she repeated most of the allegations made by her co-defendant, and also alleged that, at the date of the conveyance to her, she had no knowledge that her co-defendant was indebted to the plaintiff in any sum whatever, or that he was bound to indemnify him as alleged. She also demurred on the same grounds as her co-defendant.

6 The plaintiff joined issue upon these defences, and, in reply to the 7th paragraph of the defence of the male defendant, said that the matter therein alleged was pleaded by that defendant in his defence in a former action in this Court wherein this plaintiff was plaintiff and that defendant was defendant, and wherein judgment was given for [24 OR Page44] the plaintiff, which action was that referred to in the 1st paragraph of the statement of claim, and the matter thereof was res judicata and the male defendant was estopped from pleading the same.

7 The action was tried at the Spring Sittings, 1893, of this Court at Sandwich by STREET, J.

8 It appeared that the plaintiff, on the 3rd October, 1888, by indenture of mortgage of that date conveyed the lands in the town of Essex to one Brodie, for securing the sum of $500, payable on the 3rd October, 1891, with interest thereon annually at the rate of eight per centum per annum. That on the 21st February, 1889, the plaintiff by indenture of bargain and sale of that date, for the consideration of $500, conveyed the said lands to the male defendant subject to the said mortgage. That thereafter the male defendant paid some money on account of the interest payable by the said mortgage. That the principal, with some arrears of interest, having fallen due upon the said mortgage, and the plaintiff, being pressed by Brodie for payment, had several conversations with the male defendant in which he urged him to pay off the mortgage, and on the 19th October, 1891, the plaintiff's solicitors, by the plaintiff's instructions, wrote to the male defendant that they were instructed by the plaintiff to take proceedings to compel him to pay the mortgage. That on the 30th day of October, 1891, the plaintiff was served with a writ of summons by Brodie to recover the amount due upon the said mortgage by virtue of the covenant therein, and on that day wrote two letters to the male defendant, one of which he sent by post and one by special messenger, informing him that he had been served with the said writ, and urging to come and settle the mortgage at once. That by indenture of bargain and sale dated the 30th day of October, 1891, and registered on the 9th day of November, 1891, the male defendant, for the expressed consideration of $500, conveyed to the female defendant the north-west quarter of lot 24 on the south [24 OR Page45] side of the Malden Road, in the township of Colchester North, said to be worth $2,500, or $2,600. That Brodie obtained judgment against the plaintiff on his covenant contained in the mortgage for the amount of the principal money and interest due thereon. That on the 4th day of March, 1892, the plaintiff brought an action against the male defendant to compel payment by him of the said mortgage money, and judgment was recovered therein on the 11th day of November, 1892, by the plaintiff against the male defendant for the sum of $653, and costs to be taxed. That this action was commenced on the 11th day of February, 1892. That the female defendant was not aware that the conveyance of the said land had been made to her till, as she said, it was given to her by her husband after it was registered.

9 The learned Judge held on the evidence there was no consideration for the conveyance from the husband to the wife, that it was a voluntary conveyance, and was fraudulent and void as against creditors; and gave judgment declaring that the said conveyance was voluntary and was fraudulent and void as against the plaintiff and the other creditors of the defendant Thomas McLaughlin, and should be set aside; and ordered and adjudged accordingly, with full costs of the action, including the costs of the demurrer; with reference to the Deputy Clerk of the Crown at Sandwich to take the usual accounts and make the usual inquiries, and if the amount found due to the plaintiff and the other creditors and costs of suit should not be paid within one year from the report, the property in question should be sold to realize the same, with the costs of sale.

10 At the Easter Sittings of the Divisional Court, 1893, the defendants moved to reverse and set aside the said judgment and to enter judgment for the defendants, dismissing the plaintiff's action with costs and allowing the demurrer of the defendants with costs, upon the ground that the said judgment was contrary to law, evidence, and the weight of evidence, and that, upon the facts given in evidence [24 OR Page46] upon the trial, the judgment should have been in favour of the defendants, and more particularly upon the following grounds:

> 1. That the plaintiff was a creditor of the defendant Thomas McLaughlin by reason only of a judgment by consent obtained nearly a year subsequent to the execution and delivery of the impeached conveyance, and the plaintiff was therefore in the position of a subsequent creditor, and, there being no sufficient evidence of any intent to defeat his claim nor any pre-existing debts unpaid, was not in a position to maintain this action.
>
> 2. That if there was a pre-existing liability on the part of the defendant Thomas McLaughlin to the plaintiff, it was by reason only of an alleged right to indemnity in respect of moneys secured by mortgage, and it was not shewn in evidence by how much, if at all, the amount secured exceeded the value of the security, and the plaintiff was not therefore at the date of the impeached conveyance a creditor of the defendant within the meaning of this Act.
>
> 3. That as against the defendant Hannah Caroline McLaughlin the plaintiff did not prove himself a creditor of Thomas McLaughlin, inasmuch as Hannah Caroline McLaughlin was a stranger to the action by which the plaintiff recovered judgment against the defendant Thomas McLaughlin, and the exemplification of judgment and pleadings in the said action could not be used against the defendant Hannah Caroline McLaughlin as evidence of a debt.
>
> 4. That the plaintiff was not necessarily delayed, hindered, or defeated in obtaining payment of his debt, if any, by the impeached conveyance, because the defendant Thomas McLaughlin had at the time this conveyance was executed other property more than sufficient to pay all liabilities, including the plaintiff's;

and because default had been made in respect of the mortgage more than a year prior to the execution of the conveyance attacked, and more than two years before the said judgment was obtained, [24 OR Page47] and no effort was made during that time to enforce performance of the obligation, if any, to pay the mortgage money.

5. That valuable consideration had been given and was proved for this conveyance from the defendant Thomas McLaughlin to Hannah Caroline McLaughlin, and no fraud was shewn on the part of either of the defendants, and certainly none on the part of the defendant Hannah Caroline McLaughlin.

6. The plaintiff did not allege nor prove that he or any other creditor was an execution creditor of the defendant Thomas McLaughlin, and there was no evidence of actual fraud, and the plaintiff was therefore not in a position to maintain this action.

7. The judgment was in any case wrong in directing a sale of the said land without regard to the right of the defendant Hannah Caroline McLaughlin to dower therein, as if the conveyance is set aside she is entitled to obtain dower in the said lands in priority to any claim of the plaintiff thereto.

8. And on the argument of this motion the defendants will contend that, no actual fraud having been shewn, the defendant Thomas McLaughlin was not a proper party to the action, and that the action should, therefore, have been dismissed as against him with costs. And also that the plaintiff not having alleged in his statement of claim that he was an execution creditor of the defendant Thomas McLaughlin, the demurrer of the defendants to so much of the plaintiff's statement of claim as asked for equitable execution should have been allowed with costs; and the defendants will ask upon the foregoing, among other grounds, and upon the evidence, that the plaintiff's action be dismissed with costs, and the judgment, in so far as it directs a sale of the property described in the impeached conveyance, be varied by refusing the prayer for equitable execution; or for such other judgment as to the Court may seem right; and for payment by the plaintiff to the defendants of the costs of the action, including the costs of the motion. [24 OR Page48]

11 The motion was argued before ARMOUR, C.J., and FALCONBRIDGE, J., on the 25th of May, 1893.

12 Aylesworth, Q.C., for the defendants. The judgment of the trial Judge sets aside the conveyance. He inferred that there was an actual intent to defraud. I submit that was not a proper inference to draw from the evidence. No intention existed to defeat this claim. The male defendant considered the plaintiff's threat was not serious. He was not under any contract to pay off the mortgage; he had merely bought the plaintiff's equity of redemption. Even if it was a voluntary conveyance, he was in a position to make a voluntary settlement at the time he conveyed to his wife. At this time the plaintiff was not in a position to set the conveyance aside. His claim was not a debt; it was merely a right to sue to compel the male defendant to discharge the mortgage debt. The plaintiff is in fact a subsequent creditor and has no status: Masuret v. Mitchell, 26 Gr. 435; Clark v. Hamilton Provident and Loan Society, 9 O. R. 177. The plaintiff did not shew that the land was insufficient to pay the mortgage. No attempt was made to sell the land. The case is within the principle of Ex p. Mercer, 17 Q. B. D. 290; Real Estate Loan Co. v. Yorkville and Vaughan Road Co., 9 O. R. 464; Cameron v. Cusack, 17 A. R. 489; Darling v. Price, 27 Gr. 331; Struthers v. Glennie, 14 O. R. 726. If the conveyance was not a purely voluntary one, the intent of the wife must be shewn. She had no knowledge of this claim of the plaintiff; the most that can be said is that she knew her husband had bought a mortgaged property. The decree goes too far at any rate, for when the plaintiff began this action he was not an execution creditor, and he cannot, therefore, have equitable execution: McCall v. McDonald, 13 S. C. R. 247; Longeway v. Mitchell, 17 Gr. 190. Finally, if the judgment stands, the wife's rights as dowress should be preserved.

13 W. H. Blake, for the plaintiff. The form of the decree is right; a simple contract creditor can bring the action, as decided in Longeway v. Mitchell, 17 Gr. 190. As to the [24 OR Page49] facts, the findings of the learned Judge should stand. He heard the evidence of the defendants, and did not believe it. As to the status of the plaintiff, I refer to Allen v. Furness, 20 A. R. 34; Boyd v. Robinson, 20 O. R. 404; May on Fraudulent Conveyances, 2nd ed., p. 166.

14 Aylesworth, in reply.

15 June 26, 1893. The judgment of the Court was delivered by ARMOUR C.J. (after setting out the facts):-- It seems to be well settled that where a creditor brings his action to set aside a fraudulent conveyance made by his debtor of his property without first obtaining judgment and execution against his debtor, he must sue on behalf of all the creditors of his debtor, and in such case his relief in such action will be confined to setting aside the fraudulent conveyance, leaving him to take some independent proceedings if he wishes to have execution against the property so fraudulently conveyed: Reese River Silver Mining Co. v. Atwell, L. R. 7 Eq. 347; Longeway v. Mitchell, 17 Gr. 190; McCall v. McDonald, 13 S. C. R. 247.

16 The plaintiff in this case brought his action to set aside as fraudulent the conveyance of the land made by the male defendant to the female defendant without first obtaining judgment and execution against the male defendant, and rightly brought it on behalf of all the creditors of the male defendant; but the only relief he can obtain is the setting aside the said conveyance, and he must resort to the judgment he has since obtained, and to execution to be issued thereon, to realize out of the said land his judgment debt and costs.

17 The judgment, therefore, of my learned brother must be varied by confining it to the setting aside the fraudulent conveyance of the land made by the male to the female defendant.

18 The demurrer in this case would have been successful [24 OR Page50] under the system of special pleading which flourished in the Court of Chancery before the Judicature Act came into force: Abbott v. Canada Central R. W. Co., 24 Gr. 579.

19 But since the Judicature Act came into force, such a demurrer is no longer allowable, for it is not a demurrer to the cause of action, but only to the relief prayed in respect of the cause of action, and the demurrer in this case was therefore properly overruled: Con. Rule 384.

20 The protection of the statute 13 Eliz. ch. 5 is not confined to creditors only, but extends to creditors and others who have lawful actions, etc.

21 And upon the conveyance by the plaintiff to the male defendant of the land subject to the mortgage to Brodie there arose in favour of the plaintiff an implied contract on the part of the male defendant to pay the moneys secured by the said mortgage as they respectively fell due: Beatty v. Fitzsimmons, 23 O. R. 245.

22 And all the moneys secured by the said mortgage having fallen due before the making of the conveyance by the male to the female defendant, the plaintiff had at the time of the making thereof a lawful action against the male defendant upon his said implied contract, and was by reason thereof entitled to maintain this action to set aside the said conveyance, as devised and contrived to delay, hinder, and defraud him of his said lawful action.

23 This implied contract was sufficiently proved against the female defendant by the proof made at the trial of the mortgage to Brodie and the conveyance by the plaintiff of the land so mortgaged to the male defendant, subject to the said mortgage.

24 If it was necessary for the plaintiff, in the circumstances of this case, to shew that the land mortgaged to Brodie was insufficient in value to satisfy the said mortgage, it was, in our opinion, abundantly shewn out of the mouth of the male defendant.

25 That the conveyance from the male to the female defendant was devised and contrived by the male defendant with the intent of defrauding the plaintiff of his lawful action, there can, upon the evidence, be no doubt. [24 OR Page51]

26 Nor can there, upon the evidence, be any doubt that it was a voluntary conveyance, and that the pretended consideration was trumped up after the making of the conveyance in the vain effort to support it.

27 The learned Judge has found that it was entirely voluntary and was made by the male defendant for the purpose of defrauding the plaintiff.

28 It is only where a conveyance is made upon good consideration that it is necessary under the statute in order to set it aside to shew the fraudulent intent, of both parties to it. But where a conveyance is voluntary, it is only necessary to shew the fraudulent intent of the maker of it.

29 The judgment will, therefore, be that the conveyance from the male to the female defendant is fraudulent and void as against the plaintiff and the other creditors of the male defendant, and that, as against the plaintiff and such other creditors, it be set aside with costs, including the costs of the demurrer, and that this motion be dismissed with costs.

qp/s/qlkam/qlcla

---- End of Request ----
Download Request: Current Document: 1
Time Of Request: Thursday, May 29, 2014 12:18:49

Tab 26

2009 CarswellOnt 2906
Ontario Superior Court of Justice

Bank of Montreal v. Peninsula Broilers Ltd.

2009 CarswellOnt 2906, [2009] O.J. No. 2129, 177 A.C.W.S. (3d) 405

BANK OF MONTREAL (Plaintiff) and PENINSULA BROILERS LIMITED and MARK LOUIS FIORENTINO also known as MARK LOUIS FOREN (Defendants)

J.W. Quinn J.

Heard: March 9, 2009; April 17, 2009
Judgment: May 21, 2009
Docket: St. Catharines 50188/08

Counsel: Sean N. Zeitz for Plaintiff / Moving Party
Bryan B. Skolnik for Defendants / Responding Party

Subject: Contracts; Corporate and Commercial; Torts; Property

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Debtors and creditors --- Fraudulent conveyances — Practice and procedure — Summary proceedings — By motion

Plaintiff bank made loan to borrower guaranteed by personal and corporate defendants — Plaintiff relied on personal defendant's personal financial statements listing mobile home valued at $200,000 as asset — Corporate defendant pledged $104,000 in securities to plaintiff in December, 2004 — Plaintiff advised borrower of concerns over its financial performance in July, 2005 — One week later, personal defendant transferred mobile home to corporate defendant — Bill of sale falsely stated that consideration of $104,000 was paid — Borrower defaulted on loan in August, 2007 and plaintiff seized pledged securities — Plaintiff brought action for declaration that conveyance of mobile home was fraudulent — Plaintiff brought motion for summary judgment — Motion dismissed — There was triable issue as to fraudulent intent — Personal defendant could have believed borrower was solvent at time of transfer — Plaintiff could renew motion to argue transfer be set aside on basis of false bill of sale.

Table of Authorities

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Cases considered by *J.W. Quinn J.*:

Aguonie v. Galion Solid Waste Material Inc. (1998), 38 O.R. (3d) 161, 107 O.A.C. 114, 1998 CarswellOnt 417, 17 C.P.C. (4th) 219, 156 D.L.R. (4th) 222 (Ont. C.A.) — followed

Atlantic Acceptance Corp. v. Distributors Acceptance Corp. (1963), [1963] 2 O.R. 18, 38 D.L.R. (2d) 307, 1963 CarswellOnt 80 (Ont. H.C.) — considered

CIT Financial Ltd. v. Zaidi (2006), 2006 CarswellOnt 1680, 24 R.F.L. (6th) 78, 19 C.B.R. (5th) 204 (Ont. S.C.J.) — followed

Commerce Capital Mortgage Corp. v. Jemmett (1981), 37 C.B.R. (N.S.) 59, 1981 CarswellOnt 147 (Ont. H.C.) — considered

Continental Insurance Co. v. Dalton Cartage Co. (1982), 25 C.P.C. 72, [1982] 1 S.C.R. 164, 131 D.L.R. (3d) 559, (sub nom. *Dalton Cartage Ltd. v. Continental Insurance Co.)* 40 N.R. 135, [1982] I.L.R. 1-1487, 1982 CarswellOnt 372, 1982 CarswellOnt 719 (S.C.C.) — followed

Crombie v. Young (1894), 26 O.R. 194 (Ont. C.A.) — referred to

Dwyer v. Fox (1996), 43 Alta. L.R. (3d) 63, 190 A.R. 114, 1996 CarswellAlta 727 (Alta. Q.B.) — considered

Fancy, Re (1984), 46 O.R. (2d) 153, 51 C.B.R. (N.S.) 29, 8 D.L.R. (4th) 418, 1984 CarswellOnt 137 (Ont. Bktcy.) — considered

FL Receivables Trust 2002-A (Administrator of) v. Cobrand Foods Ltd. (2007), 2007 ONCA 425, 2007 CarswellOnt 3697, 85 O.R. (3d) 561, 46 C.P.C. (6th) 23 (Ont. C.A.) — considered

Freeman v. Pope (1870), 5 Ch. App. 538 (Eng. Ch. Div.) — referred to

Guarantee Co. of North America v. Gordon Capital Corp. (1998), [1998] I.L.R. I-3555, 108 O.A.C. 46, 157 D.L.R. (4th) 643, 1998 CarswellOnt 1203, 38 O.R. (3d) 563, 3 C.C.L.I. (3d) 202 (Ont. C.A.) — referred to

Guarantee Co. of North America v. Gordon Capital Corp. (1999), [2000] I.L.R. I-3741, 126 O.A.C. 1, 247 N.R. 97, 49 B.L.R. (2d) 68, [1999] 3 S.C.R. 423, 15 C.C.L.I. (3d) 1, 178 D.L.R. (4th) 1, 1999 CarswellOnt 3171, 1999 CarswellOnt 3172, 39 C.P.C. (4th) 100 (S.C.C.) — followed

Hercules Management Ltd. v. Ernst & Young (1997), 31 B.L.R. (2d) 147, [1997] 2 S.C.R. 165, 1997 CarswellMan 198, 211 N.R. 352, 1997 CarswellMan 199, 115 Man. R. (2d) 241, 139 W.A.C. 241, (sub nom. *Hercules Managements Ltd. v. Ernst & Young)* 146 D.L.R. (4th) 577, 35 C.C.L.T. (2d) 115, [1997] 8 W.W.R. 80 (S.C.C.) — followed

Hi-Tech Group Inc. v. Sears Canada Inc. (2001), 52 O.R. (3d) 97, 4 C.P.C. (5th) 35, 2001 CarswellOnt 9, 11 B.L.R. (3d) 197 (Ont. C.A.) — followed

Hickerson v. Parrington (1891), 18 O.A.R. 635 (Ont. C.A.) — considered

Irving Ungerman Ltd. v. Galanis (1991), 4 O.R. (3d) 545, (sub nom. *Ungerman (Irving) Ltd. v. Galanis)* 50 O.A.C. 176, 1 C.P.C. (3d) 248, 20 R.P.R. (2d) 49 (note), 83 D.L.R. (4th) 734, 1991 CarswellOnt 370 (Ont. C.A.) — referred to

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Keystone Industries (1970) Ltd. v. Craleeco Ltd. (1997), 1997 CarswellOnt 5330 (Ont. Gen. Div.) — considered

Keystone Industries (1970) Ltd. v. Craleeco Ltd. (1999), 1999 CarswellOnt 2325 (Ont. C.A.) — referred to

Nuove Ceramiche Ricchetti S.p.A. v. Mastrogiovanni (1988), 76 C.B.R. (N.S.) 310, 1988 CarswellOnt 184 (Ont. H.C.) — considered

Oliver v. McLaughlin (1893), 24 O.R. 41 (Ont. C.A.) — considered

Park v. Bhandari (2007), 2007 CarswellOnt 3604 (Ont. S.C.J.) — considered

Park v. Bhandari (2008), 2008 ONCA 884, 2008 CarswellOnt 7820 (Ont. C.A.) — referred to

Petrone v. Jones (1995), 1995 CarswellOnt 312, 33 C.B.R. (3d) 17 (Ont. Gen. Div.) — considered

Pizza Pizza Ltd. v. Gillespie (1990), 1990 CarswellOnt 408, 75 O.R. (2d) 225, 33 C.P.R. (3d) 515, 45 C.P.C. (2d) 168 (Ont. S.C.J.) — considered

Rozin v. Ilitchev (2003), 66 O.R. (3d) 410, 175 O.A.C. 4, 2003 CarswellOnt 3052 (Ont. C.A.) — considered

Solomon v. Solomon (1977), 79 D.L.R. (3d) 264, 24 C.B.R. (N.S.) 258, 16 O.R. (2d) 769, 1977 CarswellOnt 96 (Ont. S.C.) — followed

Sun Life Assurance Co. of Canada v. Elliott (1900), 31 S.C.R. 91, 1900 CarswellBC 17 (S.C.C.) — considered

Transamerica Occidental Life Insurance Co. v. Toronto Dominion Bank (1999), 1999 CarswellOnt 911, 28 E.T.R. (2d) 113, 173 D.L.R. (4th) 468, 118 O.A.C. 149, 44 O.R. (3d) 97 (Ont. C.A.) — considered

392278 Ontario Ltd. v. Miletich Estate (2001), 38 R.P.R. (3d) 239, 2001 CarswellOnt 345 (Ont. S.C.J.) — considered

1061590 Ontario Ltd. v. Ontario Jockey Club (1995), 43 R.P.R. (2d) 161, 16 C.E.L.R. (N.S.) 1, 77 O.A.C. 196, 1995 CarswellOnt 63, 21 O.R. (3d) 547 (Ont. C.A.) — considered

Statutes considered:

Fraudulent Conveyances Act, R.S.O. 1990, c. F.29
Generally — referred to

s. 1 "conveyance" — considered

s. 2 — considered

s. 3 — considered

Rules considered:

Rules of Civil Procedure, R.R.O. 1990, Reg. 194
R. 20 — pursuant to

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

R. 20.04 — considered

R. 20.04(1) — considered

R. 20.04(2)(a) — considered

R. 20.06(1) — considered

R. 26.02(b) — considered

MOTION by plaintiff for summary judgment in action for declaration of fraudulent conveyance.

J.W. Quinn J.:

I Introduction

1 The plaintiff ("Bank") has brought an action seeking a declaration that the sale of a certain mobile home by the defendant, Mark Louis Fiorentino ("Mark"), to the defendant, Peninsula Broilers Limited ("corporate defendant"), is fraudulent, null and void and ineffective as against the Bank, pursuant to the *Fraudulent Conveyances Act*, R.S.O. 1990, c. F.29.

2 The Bank now moves for summary judgment under rule 20 of the *Rules of Civil Procedure*, R.R.O. 1990, Reg. 194, contending that there is no genuine issue for trial.

II Overview

3 Peninsula Food & Poultry Distributors Ltd. ("Borrower") operated as a wholesaler of food and poultry products in the Niagara Falls area, targeting the hospitality industry. In 2002, the Bank made available to the Borrower a demand operating loan with a limit of $250,000 ("loan"). I gather that this was in the nature of a line of credit.

4 In consideration for the loan, Mark provided his personal guarantee, as did the corporate defendant.

5 Mark is the sole officer, director and shareholder of the Borrower.

6 Mark's father, Peter Louis Fiorentino ("father") and mother, are the only shareholders of the corporate defendant.

7 The loan fell into arrears. The Bank sued and obtained default judgment against the Borrower and Mark.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

8 In the course of examining Mark in aid of execution, the Bank learned that a mobile home, listed as an asset in personal financial statements prepared by Mark for the Bank, actually had been sold by him to the corporate defendant. The Bank alleges that the sale of the mobile home is a fraudulent conveyance.

9 The central issue both in the action and in the motion is whether the sale or transfer of the mobile home was for good consideration.

III The Evidence

Mark provides first personal financial statement

10 On June 5, 2002, Mark provided a personal financial statement for the Bank in which he showed, as an asset, beach-front property at Sherkston, Ontario (a mobile-home enclave on the shore of Lake Erie), with an estimated value of $200,000. This property, in fact, proved to be a 1989 Chariot Eagle, 38' × 12' mobile home, serial number 9185 ("mobile home").

Borrower's account transferred to special Bank management unit

11 In the years following the loan, the Borrower was in a state of near-constant financial stress.

12 In October of 2003, because the Borrower "continued to experience excesses, it was transferred to [the Bank's] SAMU [Special Accounts Management Unit]."

Mark provides second personal financial statement

13 On December 13, 2003, Mark provided a second personal financial statement for the Bank, again disclosing the same mobile home as an asset.[1]

Bank expresses concern with Borrower's financial performance

14 By letter dated December 1, 2004, the Bank wrote to the Borrower:

> We confirm our advice that the Bank is still concerned with the Borrower's financial performance.

Accordingly, in order "to continue to provide financing" the Bank requested a number of additional security documents[2] and it reduced the operating loan ceiling from $250,000 to $175,000.[3]

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

15 Both the Borrower and the corporate defendant signed an acknowledgement of these new "terms and conditions," as did Mark and the father in their personal capacities. All signatures were witnessed on December 10, 2004 by Daniel J. McDonald, a lawyer practicing in the City of Niagara Falls.

Certificate of Independent Legal Advice

16 Also, on December 10, 2004, Mr. McDonald signed a Bank certificate of independent legal advice certifying that the corporate defendant:

> . . . has consulted me as to the nature and effect of signing or endorsing the following documents:
>
> • guarantee for indebtedness of an incorporated company for $104,000;
>
> • pledge of instrument and assignment of proceeds for $54,000;
>
> • pledge of instrument and assignment of proceeds for $50,000;[4]
>
> which have been executed for the purposes of securing the debts of [the Borrower] to Bank of Montreal up to the amount of $104,000 . . .

These are the same documents that were set out in the Bank's letter of December 1st.[5]

17 Thus, in December of 2004, the corporate defendant granted a guarantee of the Borrower's obligations to the Bank and pledged $104,000 in securities to back up that guarantee.

Bank memorandum

18 On June 30, 2005, the Bank created a memorandum outlining the account history of the Borrower. It stated that, "although the [Borrower]'s cash flow has improved from previous years, it is still tight with occasional excesses." Additional security and further monitoring were recommended.

Borrower defaults on loan

19 In July of 2005, the Borrower on the loan.[6]

Bank again expresses concern with Borrower's financial performance

20 By letter dated July 7, 2005, the Bank wrote to the Borrower, saying, in part:

> We confirm our advice that the Bank is still concerned with the [Borrower]'s financial performance. Such concerns include but are not limited to tight cash flow and high leverage. However, the Bank is prepared to renew the credit

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> facility with the following terms and conditions . . .

One of the "terms and conditions" was an immediate and permanent reduction of the loan limit to $175,000. The balance owing on the loan at that time was $75,000, which was converted to a non-revolving demand loan to be retired over a period of 36 months by way of monthly principal payments. However, the Borrower was at liberty to draw on the available $100,000 loan limit.

21 The Borrower, the corporate defendant, Mark and the father acknowledged their agreement to the new terms and conditions. Their signatures, dated July 13, 2005, again were witnessed by Mr. McDonald.

Mark sells mobile home

22 On that same date, Mark sold the mobile home to the corporate defendant. The bill of sale evidencing the transaction was prepared by Mr. McDonald's office and it includes this passage regarding the consideration that allegedly passed (emphasis added):

> NOW THEREFORE THIS INDENTURE WITNESSETH, that in pursuance of the said Agreement, and *in consideration of the sum of one hundred and four thousand ($104,000) dollars of lawful money of Canada, paid by the [corporate defendant] to [Mark]* at or before the sealing and delivery of this Indenture (the receipt of which is hereby acknowledged), [Mark] does bargain, sell, assign, transfer and set over unto the [corporate defendant], ALL THOSE goods, namely:
>
> 1989 Chariot Eagle 38' × 12' Mobile Home Serial No. 9185

23 This sale occurred seven months after the corporate defendant gave its guarantee of the Borrower's obligations to the Bank and pledged $104,000 as security (the Borrower being, as I have mentioned, Mark's company).

McDonald's reporting letter re sale of mobile home

24 By letter dated July 13, 2005, Mr. McDonald wrote to Mark, confirming that the sale of the mobile home was prompted by the continued uncertain financial performance of the Borrower (emphasis added):

> Re: [Borrower's] guarantee to Bank of Montreal Further to you (sic) office attendance of this date and the execution and delivery of the Bill of Sale to [the corporate defendant] with respect to your 1989 Chariot Eagle Mobile Home located at Sherkston, Ontario. I wish to confirm the terms of your arrangement with your father and [the corporate defendant] concerning this transaction.
>
> As you are aware [the corporate defendant] delivered a guarantee to the Bank of Montreal in the amount of $104,000.00 in December 2004 to guarantee the debts of your company, [the Borrower]. In addition at that time it pledged to the bank certain securities having a value of $104,000.00 in support of the guarantee.
>
> *In view of the continued uncertain financial performance of [the Borrower] and the real possibility that the bank would seize the security pledged by [the corporate defendant] you agreed to transfer ownership of the mobile home to the [the corporate defendant] at this time.*

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

25 The letter goes on to state the legal effect of the transfer (emphasis added):

> As I advised, the legal effect of this transaction is that [the corporate defendant] is now the legal owner of the mobile home notwithstanding that *you will be permitted to use and occupy it and that you will continue to be responsible for all expenses in connection with same.*[7] In addition I confirm that it was agreed that *a notice of change in ownership would not be sent to Sherkston Resorts Inc. because* of their policy of charging a substantial fee when ownership of a mobile home is transferred.

26 The letter also speaks of a re-transfer of the mobile home:

> In addition it is intended that ownership will be retransferred to you if [the corporate defendant] is relieved from its guarantee and the pledged security returned to it.
>
> In the event however that the bank calls upon [the corporate defendant] to honour its guarantee and the pledged securities are retained by the bank ownership of the mobile home will remain with [the corporate defendant].

Mark provides a third personal financial statement

27 In a third personal financial statement required by, and provided to, the Bank, dated January 20, 2007, Mark continued to list, as an asset, a 100% unencumbered interest in the mobile home (which he still valued at $200,000).

Borrower again defaults, Bank makes demand and realizes on its security

28 In August of 2007, the Borrower defaulted on the loan. Also in that month, the Bank, through its solicitors, made a written demand upon the Borrower and upon Mark (in accordance with his personal guarantee).

29 Thereafter, the Bank seized the securities pledged by the corporate defendant and called upon the father's personal guarantee, thereby reducing the indebtedness of the Borrower by $107,000, from $139,000 to $32,000.

Related Action

30 The Bank brought an action ("related action") against the Borrower and Mark for the balance owing on the loan. The statement of claim was issued on October 25, 2007.

Default Judgment in Related Action

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

31 On December 17, 2007, the Bank obtained default judgment in the related action for the sum of $46,253.77.

Mark examined in aid of execution in related action

32 In April of 2008, Mark was examined in aid of execution in the related action. I will review his evidence under seven headings:

1. value of the mobile home

33 Mark was asked about the value of the mobile home:

> Q.43 . . . in July 2002, did you own a [mobile home] at Sherkston . . . free and clear, worth approximately $200,000?
>
> A. Yes, I don't know if it was worth $200,000 . . . That's just ball-parking it.
>
> Q.44 Okay. Did you tell the Bank that it was worth $200,000?
>
> A. I can't remember. I don't, I can't remember. I don't have the paper.

2. consideration for the sale of mobile home

34 Mark admitted that no money changed hands when the mobile home was sold:

> Q.103 Okay. And did [the corporate defendant] pay $104,000 to you for this?
>
> A. Did [it] pay for - no, no, no, no, no.
>
> . . . . .
>
> Q.157 Okay. When you transferred the mobile home on July 15, 2005 to [the corporate defendant], what did you get?
>
> A. . . . I just had to secure the hundred and seventy-five [thousand] and I could do it with the motor home which I did, and what I got was the bank off my back for that hundred and seventy-five thousand.
>
> Q.161 Okay. Could you just clarify what you mean by getting the bank off your back?
>
> A. Well they were either going to pull the loan, take the inventory, if I didn't come up with the $175,000 and that's the only way that I could have come up with it was through my father putting up his collateral, his cash.

3. the timing of the sale

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

35 With the corporate defendant having pledged its securities to the Bank in December of 2004, Mark was asked about the seven-month delay before the mobile home was transferred to the corporate defendant:

> Q.164 . . .
>
> A. Because I was still trying to get financing, so I can pay off that one hundred and seventy-five and not have to do it . . . But I didn't get the financing so I had to put up something, I had to give my father something . . . my accountant was telling me, you've got to give him something . . . [and] was advising my father . . . you've got to get something . . .

36 He was questioned further about the timing of, and reason for, the sale:

> Q.115
>
> . . . . .
>
> A. When the bank started wanting security for the two fifty, down to the one seventy-five, my accountant. . . and my father's accountant . . . mentioned to me that . . . my father . . . should get some security, you know, from all the money that he's putting in. And then when the Bank want this hundred seventy-five thousand, that's when everything started hitting the fan and I said, 'Here, take the motor home for the security of the one-seventy-five.'
>
> . . . . .
>
> A. . . . My accountant said, you know, your father has a lot of money invested, you're going to have to give him some kind of security. This happened, you know, just prior to July of 2005 that he was mentioning it to me . . .
>
> . . . . .
>
> Q.133. No, so this was - so [the corporate defendant] did not, in fact, pay $104,000 but you transferred title
>
> A. Yes.
>
> Q.134 . . . in return for the guarantee on your loan from the bank?
>
> A. Yeah, 'cause he guaranteed - he lost the $175,000.[8]

37 I also note that the father gave this evidence when he was cross-examined on his affidavit filed on the motion:

> Q.37 . . . Now why was the transfer [of the mobile home] completed approximately six months after your pledge [of securities] was made? The pledge was made in December 2004 and then the transfer takes place approximately six months later on July 13, 2005.
>
> A. I don't know. I imagine that's when the bank required the money.
>
> . . . . .
>
> Q.42 Wouldn't you agree that when the pledge was given to the [Borrower] in December 2004, you would have asked for the mobile home to be transferred at that time?
>
> A. I can't remember . . .

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

4. Mark has no further assets

38 Mark was asked whether the sale of the mobile home "was effectively a transfer of substantially all of your assets":

> Q.171 . . .
>
> A. Yes, that was pretty much it.

39 I take his answer (which uses "was" instead of "is") to be referring to the point in time when the mobile home was sold[9] and not to some other date, such as that of his examination in aid of execution.

5. his personal financial statements

40 In his cross-examination, Mark exhibits a nonchalance towards his personal financial statements provided to the Bank:

> Q.23 Okay. Now in Mr. Schu's[10] affidavit, he stated that the Bank relied on your personal financial statement when it decided to accept your guarantee.
>
> A. No, I didn't believe that.
>
> Q.24 Okay. Would you agree that in 2002 and in 2003 and then again in 2007, you provided personal financial statements to the Bank?
>
> A. At the beginning I provided one and I believe, there was another one that was sent, I think via fax, I believe, and it was the same statement, all I did was pull it out of the file and fax it over. It was, that's all I did. I was too busy to be doing anything other than what I was geared to do that day. I'd get on the phone if him or her called and said she needed this, I just dug through, if it was there, it was sent.
>
> Q.25 Okay. Would you agree that there was three financial statements?
>
> A. I don't know. I know, I'll say two for sure. They were exactly the same.
>
> Q.26 So what I'm suggesting to you sir, is that there were three separate time periods in which you sent a personal financial statement to the Bank, and I suggest to you that it was sent in 2002, another statement in 2003 and then another statement in 2007, do you agree?
>
> A. I can't remember. I know there was two different times, the same one was sent.
>
> Q.27 When you say 'the same one' - do you mean you took the same document - and just signed it - dated it and sent it off?
>
> A. Yes.
>
> . . . . .
>
> Q.31 Did you review the statement to ensure that it was accurate?

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

A. No, sir . . . I never even looked at it. I just, I'm too busy, too much stuff on my plate.

. . . . .

Q.107 . . . the information that's listed here [in Mark's personal financial statement dated January 20, 2007] was identical as the first statement in 2002 . . .?

A. It should be, yes.

. . . . .

Q.109 Now on the third page of the statement dated January 20, 2007, you disclose an interest in [the mobile home at] Sherkston . . .

A. Yes.

Q.110 As at January 20, 2007, did you in fact enjoy an ownership interest in that [mobile home]?

A. No.

. . . . .

Q.113 Why did you include it in the statement if you didn't own it?

A. It's the same statement. I just sent the same statement.

6. financial difficulties of the Borrower

41 Mark was questioned about the financial difficulties of the Borrower at the time the Bank created its memorandum of June 30, 2005:

Q.74 Okay. And would you agree that at that time, about June 30, 2005, the [Borrower] was experiencing financial difficulty?

A. I just can't place the date with what was happening . . . there was always a strain because our accounts receivable were a little high . . . So I don't know if we were anymore tight with money that date or the date prior.

42 Mark was asked about the Bank's letter of July 7, 2005:

Q.87 . . . would you agree . . . that you were aware, at least when you got this letter, that the Bank was concerned with the performance of the [Borrower]?

A. Yeah, the bank was. I thought everything was just fine. I thought they were a little scared that they had so much

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> money out with no security whatsoever on it.[11]

7. other questionable conduct by Mark

43 Mark did not inform Sherkston Resorts Inc. about the sale of the mobile home:

> Q.177 Okay. Why didn't you disclose [the sale] to Sherkston?
>
> A. Sherkston . . . wants a piece of everything that they can get their hands on. If I would have told them that I was selling this motor home to my father, they'd want their commission[12] which runs 25 to 30% . . . And then if everything worked out okay and I wanted my motor home back . . . I'd have to give [Sherkston] another 25% to get it back in my name . . .

44 Also, in his three personal financial statements Mark included a 1947 Cadillac as an asset. However, it actually was owned by the father who said so in his cross-examination:

> Q.73 [Mark's personal financial statements refer to] a Jag and then Cad, which I assume is a Cadillac . . . a 1947 vehicle . . . the Jag is a 2004 vehicle, are those your vehicles, sir?
>
> A. The 1947 Cadillac is.

Mark an officer of corporate defendant

45 On May 8, 2008, the Bank learned (through a Corporation Profile Report from the Ministry of Consumer and Business Services) that Mark was actually an officer and director of the corporate defendant.[13] The sale of the mobile home, therefore, was from a son to his father's company, and from an officer of a company to that company.

Within Action Commenced

46 The statement of claim in the within action was issued on May 13, 2008. Among other relief, the Bank seeks, as I indicated at the outset, a declaration that the transfer of the mobile home is fraudulent, null and void and ineffective as against the Bank. The court is asked to set aside the sale as being a fraudulent conveyance.

Interlocutory Injunction Granted

47 On May 15, 2008, Ramsay J. granted an interlocutory injunction, enjoining the corporate defendant and Mark from selling, transferring or encumbering the mobile home until the trial or other disposition of the action.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Statement of Defence

48 A statement of defence was served in June of 2008. It pleads that the transfer of ownership of the mobile home was a *bona fide* transaction for valid consideration:

> 6. In July 2005 the [Borrower]'s indebtedness to the [Bank] by way of its . . . [loan] was reduced to $175,000 as a result of, inter alia, a pledge of certain securities from the [corporate defendant] and the personal guarantee of . . . [the father].
>
> 7. The mobile home was transferred from . . . [Mark] to the [corporate defendant] on or about July 13, 2005. The consideration paid for the mobile home was $104,000. This amount represented the [corporate defendant]'s risk/exposure to the [Bank] by way of its pledge of the securities to the [Bank].
>
> 8. The [Borrower] encountered financial difficulties in the summer of 2007. At that time, the [Bank] realized on its security by seizing the securities and calling upon [the father]'s personal guarantee. As a result, the [Borrower]'s indebtedness was reduced to approximately $32,000 as of August 2007.
>
> 9. In light of matters referred to in paragraphs 6 through 8 herein, the [corporate defendant] satisfied in excess of $107,000 of the [Borrower]'s debt to the [Bank]. The defendants state and the fact is that [the $107,000] represents good, valuable and just consideration for the mobile home.

Statement of Claim Amended

49 The statement of clam was amended on August 20, 2008, pursuant to Rule 26.02(b) of the *Rules of Civil Procedure*. The amendments read as follows (I have omitted the underlining):

> 7. . . . In fact, this was the third personal financial statement that [Mark] delivered to the Bank wherein he disclosed that he owned the mobile home.
>
> 8. . . . [Mark] first provided a personal financial statement to the Bank dated June 5, 2002 followed by an additional personal financial statement dated December 13, 2003. These statements were required by the [Bank] as part of its ongoing monitoring of the [Borrower] and to evaluate the strength of the Bank's security which included . . . [Mark]'s personal guarantee.
>
> 9. . . . [Mark] disclosed and represented to the [Bank] that he owned the mobile home on all three of the personal financial statements.
>
> 10. . . . The [Bank] continued to rely on the representations contained in . . . [Mark]'s personal financial statements including his ownership interest in the mobile home between on or about June 5, 2002 through to and including Judgment against the [Borrower] . . .

50 The defendants have not delivered an amended statement of defence. Therefore, they are deemed to have admitted that the Bank relied on the representations described in paragraph 10 of the amended statement of claim.

evidence of Mr. McDonald

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

51 In 2009, Mr. McDonald was cross-examined on the affidavit he delivered in support of the defendants and in opposition to the summary judgment motion. He was questioned about consultations with Mark regarding asset protection:

> Q.11 Did you consult with [Mark] with respect to asset protection . . .
>
> . . . . .
>
> A. And what period are you speaking of ? Q.13 Any period?
>
> A. The only discussions I would have had with [Mark], or not the only, sorry, but the discussions I had with [Mark] is with respect to asset protection that occurred in the spring of 2007, at which time we had a meeting and he indicated to me that he was having trouble with his business [the Borrower] and that he was just having difficulty meeting his obligation . . .
>
> . . . . .
>
> A. No, if you listened to my response I said it was in the spring of 2007 that I discussed his and the [Borrower]'s financial circumstances . . .

52 I would have thought that asset protection was also discussed on July 13, 2005, as the effect of the sale of the mobile home to the corporate defendant was to protect it from seizure by the Bank while in Mark's hands.

53 Mr. McDonald deposed that the consideration of $104,000 for the sale of the mobile home "represented the [corporate defendant]'s risk/exposure to the [Bank] by way of its pledge of securities to the [Bank]."

54 At paragraph 9(c) of his affidavit he stated:

> 9(c) . . . the transaction was entered into for the entirely legitimate purpose of transferring an asset of equivalent value to the guarantee and the pledge of the securities . . . The [corporate defendant] . . . was concerned that the securities which it has pledged might be seized. The transfer of the mobile home gave the [corporate defendant] the protection it required;

55 Again, on the issue of consideration, he answered:

> Q.42 . . .
>
> A. The consideration, the figure of a hundred and four thousand as reflected by the bill of sale was the one hundred and four thousand in specific securities that were pledged by [the corporate defendant] to the Bank.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

56 Mr. McDonald was asked what Mark got for the transfer of the mobile home:

> Q.35 . . .
>
> A. I suppose if you ask what he got was he got some reduction of his exposure from his personal guarantee to the Bank. He had personally guaranteed the indebtedness to the Bank . . . his exposure was reduced . . .

the evidence of Mark and the father

57 Mark and the father both delivered affidavits in opposition to the Bank's motion upon which they were cross-examined. Their affidavits largely adopt the affidavit of Mr. McDonald.

IV Summary judgment

No Genuine Issue for Trial

58 On a motion for summary judgment, the responding party "must set out, in affidavit or other evidence, specific facts showing that there is a genuine issue for trial": see rule 20.04(1) of the *Rules of Civil Procedure*.

59 The "court shall grant summary judgment if . . . the court is satisfied that there is no genuine issue for trial with respect to a claim or defence": see rule 20.04(2)(a).

60 It is implicit in rule 20.04 that the genuine issue for trial is as to any material fact: see *Irving Ungerman Ltd. v. Galanis* (1991), 4 O.R. (3d) 545 (Ont. C.A.) at 550.

Burden of Proof

61 "The appropriate test to be applied on a motion for summary judgment is satisfied when the [moving party] has shown that there is no genuine issue of material fact requiring trial . . . 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' (*Hercules*,[14] *supra*, at para. 15)": see *Guarantee Co. of North America v. Gordon Capital Corp.*, [1999] 3 S.C.R. 423 (S.C.C.) at para. 27, reversing (1998), 38 O.R. (3d) 563 (Ont. C.A.).

62 Yet, this two-part test does not affect the legal burden of proof that rests on the moving party "and it never shifts": see *Hi-Tech Group Inc. v. Sears Canada Inc.* (2001), 52 O.R. (3d) 97 (Ont. C.A.) at 105.

63 While the onus of establishing the absence of a triable issue is on the moving party, the responding party "must lead trump or risk losing": see *1061590 Ontario Ltd. v. Ontario Jockey Club* (1995), 21 O.R. (3d) 547 (Ont. C.A.) at 557.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Self-Serving Affidavits Not Sufficient

64 ". . . a self-serving affidavit is not sufficient in itself to create a triable issue in the absence of detailed facts and supporting evidence": see *Guarantee Co. of North America v. Gordon Capital Corp.*, *supra*, at para. 31.

Responding Party Not to Rest on the Pleadings

65 ". . . the party responding to a summary judgment motion . . . may not rest on the pleadings, but must provide evidence from which the motions judge can conclude that there is no genuine issue for trial": see *Transamerica Occidental Life Insurance Co. v. Toronto Dominion Bank* (1999), 44 O.R. (3d) 97 (Ont. C.A.) at 110.

Motions Judge Not to Resolve Issues of Credibility

66 "A motions judge, on a Rule 20 summary judgment motion, should not resolve issues of credibility, draw inferences from conflicting evidence, or from evidence that is not in conflict when more than one inference is reasonably available": see *Transamerica Occidental Life Insurance Co. v. Toronto Dominion Bank, ibid.*

67 "Evaluating credibility, weighing evidence, and drawing factual inferences are all functions reserved for the trier of fact": see *Aguonie v. Galion Solid Waste Material Inc.* (1998), 38 O.R. (3d) 161 (Ont. C.A.) at 173.

68 ". . . the mere existence of an issue of credibility will not defeat a motion for summary judgment. The issue of credibility must be a genuine issue": see *Transamerica Occidental Life Insurance Co. v. Toronto Dominion Bank, ibid*, citing *Irving Ungerman Ltd. v. Galanis, supra*, at 551-52.

Records to Contain ALL the Evidence

69 The motions judge is entitled to assume that the motion records contain all the evidence that the parties would adduce if there were to be a trial.

"Best Foot Forward" and "Hard Look"

70 On a motion for summary judgment, the parties must "put their best foot forward" and the motions judge is required to "take a hard look at the merits of the action": see *Rozin v. Ilitchev*, [2003] O.J. No. 3158 (Ont. C.A.) at para. 8, (2003), 66 O.R. (3d) 410 (Ont. C.A.), citing a number of earlier cases.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

71 Even where matters of credibility must be determined on conflicting evidence, the court must take "a 'hard look' at the merits [and] must decide if any conflict is more apparent than real": see *Pizza Pizza Ltd. v. Gillespie* (1990), 75 O.R. (2d) 225 (Ont. S.C.J.) at 238.

V Fraudulent conveyances

"Conveyance"

72 "Conveyance" is defined in s. 1 of the *Fraudulent Conveyances Act*, R.S.O 1990, c. F.29 (*"Act"*) to include "gift, grant, alienation, bargain, charge, encumbrance . . . of . . . personal property by writing or otherwise."[15] And, "personal property" means "goods, chattels . . ."

Where Conveyances Void as Against Creditors

73 "Every conveyance of . . . personal property . . . made with intent to defeat, hinder, delay or defraud creditors . . . of their just and lawful actions, suits, debts, accounts . . . are void as against such persons and their assigns": see s. 2 of the *Act.*

Where "Good Consideration," s. 2 Not Applicable

74 "Section 2 does not apply to an estate or interest in . . . personal property conveyed upon good consideration and in good faith to a person not having at the time of the conveyance to the person notice or knowledge of the intent set forth in that section": see s. 3 of the *Act.*

75 "Pursuant to section 3, if the conveyance is made upon good consideration, it is not subject to section 2, if the transferee was acting in good faith and without notice or knowledge of the fraudulent intent of the transferor. But if the conveyance was not made for good consideration it is not protected under section 3 and is subject to being set aside under section 2 regardless of the intent of the transferee. Accordingly, where a plaintiff establishes *prima facie* that a conveyance was made with fraudulent intent for purposes of section 2 and without good consideration for purposes of section 3, the conveyance is subject to be set aside unless the defendant establishes either that the transferor lacked the fraudulent intent or else (as required by section 3) that the conveyance was made for good consideration and that the transferee acted in good faith and without notice or knowledge of the fraudulent intent of the transferor": see *CIT Financial Ltd. v. Zaidi* (2006), 24 R.F.L. (6th) 78 (Ont. S.C.J.) at para. 21.

76 Where the conveyance was made for good consideration, "the plaintiff must show the fraudulent intent of both parties to the conveyance": see *Commerce Capital Mortgage Corp. v. Jemmett*, 1981 CarswellOnt 147 (Ont. H.C.) at para. 41.

Burden of Proof for Fraudulent Conveyances

77 The Bank must prove the necessary fraudulent intent.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

78 When determining whether a conveyance is fraudulent, "the applicable standard of proof is proof on a balance of probabilities, but to a higher degree of probability than would apply in an ordinary civil case. Where misconduct such as fraud is alleged, the degree of proof required must be commensurate with the gravity of such allegations. Proof commensurate with the occasion requires particular attention to the cogency of the evidence of fraud offered against the defendant": see *CIT Financial Ltd. v. Zaidi, supra*, at para. 23, citing *Continental Insurance Co. v. Dalton Cartage Co.* (1982), 131 D.L.R. (3d) 559 (S.C.C.) at 563 - 564.

79 "In other words, 'clear and sufficient proof' is required": see *CIT Financial Ltd. v. Zaidi, supra*, at para. 24, citing *Hickerson v. Parrington* (1891), 18 O.A.R. 635 (Ont. C.A.) at 643.

80 "This may be equated with 'substantial evidence' ": see *CIT Financial Ltd. v. Zaidi*, ibid, at para. 24, citing *Dwyer v. Fox* (1996), 43 Alta. L.R. (3d) 63 (Alta. Q.B.) at 73-74.

81 The court "is not compelled to draw this inference of fraudulent intent from badges of fraud pleaded by the plaintiff . . . The court may dismiss a fraudulent conveyance action because it has decided that the surrounding circumstances taken as a whole explain away the plaintiff's evidence": see *FL Receivables Trust 2002-A (Administrator of) v. Cobrand Foods Ltd.* (2007), 85 O.R. (3d) 561 (Ont. C.A.) at para. 40.

82 In cases where there are badges of fraud or suspicious circumstances surrounding a conveyance, "there is no 'onus' shift, but simply a question of legitimate explanation that may be required in circumstances of suspicion": see *Park v. Bhandari* [2007 CarswellOnt 3604 (Ont. S.C.J.)] CanLII 20981 at para. 38, aff'd 2008 ONCA 884 (Ont. C.A.) (CanLII).

Burden on Motion

83 This same enhanced burden of proof that I have been describing is applicable on a motion for summary judgment where the subject-matter involved is an alleged fraudulent conveyance.

Each Case Stands on Own Facts

84 In the area of fraudulent conveyances, "each case must stand on its own facts": see *Keystone Industries (1970) Ltd. v. Craleeco Ltd.*, 1997 CarswellOnt 5330 (Ont. Gen. Div.) at para. 20, affirmed 1999 CanLII 1053 [1999 CarswellOnt 2325 (Ont. C.A.)].

Intent

85 ". . . it is established by the authorities that in the absence of any . . . direct proof of intention, if a person owing debts makes a settlement which subtracts from the property which is the proper fund for the payment of those debts, an amount without which the debts cannot be paid, then, since it is the necessary consequence of the settlement (supposing it effectual) that some creditors must remain unpaid, it would be the duty of the judge to direct the jury that they must infer the intent of the settler to have been to defeat or delay his creditors . . .:" see *Sun Life Assurance Co. of Canada v. Elliott*, 1900

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

CarswellBC 17 (S.C.C.) *per* Sedgewick J., at para. 4, quoting Lord Hatherley L.C. in *Freeman v. Pope* (1870), 5 Ch. App. 538 (Eng. Ch. Div.) at 541.

86 "Where there is a voluntary conveyance, if the result of the transaction is to defeat the rights of the creditor, then there is an assumption that it was a conveyance to defeat the creditors": see *Atlantic Acceptance Corp. v. Distributors Acceptance Corp.*, [1963] 2 O.R. 18 (Ont. H.C.) at 21.

87 "Whether the intent exists is a question of fact to be determined from all of the circumstances as they existed at the time of the conveyance": see *Fancy, Re* (1984), 46 O.R. (2d) 153 (Ont. Bktcy.) at 159, followed in *Nuove Ceramiche Ricchetti S.p.A. v. Mastrogiovanni*, [1988] O.J. No. 2569 (Ont. H.C.) at p. 4 and in *392278 Ontario Ltd. v. Miletich Estate*, [2001] O.J. No. 400 (Ont. S.C.J.) at para. 38.

Where No Consideration, Intent Need Be Proved Only of Vendor

88 "It is only where a conveyance is made upon good consideration that it is necessary under the statute in order to set it aside to shew the fraudulent intent of both parties to it. But where a conveyance is voluntary, it is only necessary to shew the fraudulent intent of the maker of it": see *Oliver v. McLaughlin* (1893), 24 O.R. 41 (Ont. C.A.) at p. 51, per Armour, C.J., cited in *Solomon v. Solomon* (1977), 16 O.R. (2d) 769 (Ont. S.C.) at 774.

Intent to Defeat Future Creditors

89 "It is not too liberal a construction of the [*Fraudulent Conveyances Act*] to extend it to a case where the conveyance was made to defeat future creditors and it in fact defeats, delays or hinders existing creditors even though there might have been no intention to do so at the time of the conveyance": see *Petrone v. Jones*, [1995] O.J. No. 1478 (Ont. Gen. Div.) at para. 23.

Transaction Between Close Relatives

90 "Where the impugned transaction was . . . between close relatives under suspicious circumstances, it is prudent for the court to require that the debtor's evidence on *bona fides* be corroborated by reliable independent evidence": see *Fancy, Re, ibid*, followed in *Nuove Ceramiche Ricchetti S.p.A. v. Mastrogiovanni, ibid* and in *392278 Ontario Ltd. v. Miletich Estate, ibid.*

Badges of Fraud

91 In *Solomon v. Solomon, supra*, at p. 778, Krever J., as he then was, referring to a New Brunswick decision, accepted the following as badges of fraud:

1. Secrecy

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

2. Generality of conveyance, by which is meant the inclusion of all or substantially all of the debtor's assets

3. Continuance in possession by debtor

4. Some benefit retained under the settlement to the settlor

92 "But all the circumstances surrounding the conveyance of the property must be examined to determine if there are among them some which have been termed 'badges of fraud' ": see *Solomon v. Solomon*, *ibid.*

93 ". . . the existence of one or more of the traditional 'badges of fraud' may give rise to an inference of intent to defraud in the absence of an explanation from the defendant": see *Fancy, Re*, *ibid*, followed in *Nuove Ceramiche Ricchetti S.p.A. v. Mastrogiovanni*, *ibid*, and in *392278 Ontario Ltd. v. Miletich Estate*, *ibid.*

Where Debtor Still Solvent

94 It may be that, in circumstances where a debtor is still "perfectly solvent after the conveyance," it is difficult to impute "any intent to hinder or delay": see *Sun Life Assurance Co. of Canada v. Elliott*, 1900 CarswellBC 17 (S.C.C.) at para. 8, (1900), 31 S.C.R. 91 (S.C.C.) and *Crombie v. Young* (1894), 26 O.R. 194 (Ont. C.A.).

VI The positions of the parties

95 Although the positions taken by the parties should be apparent by now, I will briefly outline them again.

The Defendants

96 On behalf of the defendants, it is argued that the consideration of $104,000, set out in the bill of sale, represented the dollar value of the risk or exposure by the corporate defendant to the Bank, arising from the former's pledge of securities for $104,000 (which securities were seized by the Bank). As Mr. McDonald deposed in his affidavit, at paragraph 9(c), the sale was the transfer of "an asset of equivalent value to the guarantee and the pledge of the securities . . ."

97 Furthermore, when cross-examined on his affidavit, and asked what Mark got for the sale of the mobile home, Mr. McDonald said: "I suppose . . . he got some reduction of his exposure from his personal guarantee to the Bank."

the Bank

98 The Bank submits that the sale of the mobile home was the transfer of a substantial asset at a time when Mark ought to have known of the financial difficulties of the Borrower and of the Bank's concern.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

99 The Bank maintains that it relied on Mark's ownership interest in the mobile home when it decided to advance funds to the Borrower and when it agreed to accept Mark's personal guarantee of the Borrower's obligations to the Bank.

100 The sale was made with the intent and sole purpose of defeating, hindering, delaying and defrauding the Bank, as contemplated by the *Act*. It was a strategic move to put Mark's sole exigible asset beyond the reach of the Bank at a time when Mark knew that the Borrower was at risk of having the Bank seize its assets and call upon him pursuant to his personal guarantee.

VII Discussion

101 The bill of sale for the mobile home is dated July 13, 2005. On that date, as I have pointed out, Mark agreed that the Bank was concerned with the performance of the Borrower, but *he* believed "everything was just fine." There is some basis for Mark's belief because the Bank memorandum of June 30, 2005 referred to the Borrower's cash flow as having "improved from previous years." As well, in the letter of July 7, 2005, the Bank expressed its willingness "to renew the credit facility" for the Borrower (albeit on new terms and conditions). When all of this is added to the fact that the precipitating default by the Borrower did not happen until two years later (August 2007), the sale does not appear to have occurred on the eve of insolvency. Accordingly, despite the existence of some badges of fraud, it is difficult to impute an intent to "defeat, hinder, delay or defraud creditors," in the words of s. 2 of the *Fraudulent Conveyances Act*.

102 While there is much here to attract the suspicion of the court, I am not satisfied that the Bank, on this motion, has discharged the serious burden of proof needed to establish the fraudulent intent alleged. There is a triable issue in that regard. Yes, it is correct to say that the parties and Mr. McDonald have delivered affidavits upon which they have been cross-examined and it is true that the advantage of a trial judge's ability to see the testimony unfold from the witness box is sometimes more talked about than real, but, here, I think the advantage may exist.[16]

103 However, there is reason to doubt the legitimacy of the sale of the mobile home on other grounds. The bill of sale clearly stipulated that the consideration was (emphasis added): ". . . the sum of one hundred and four thousand ($104,000) dollars of lawful money of Canada, *paid* by the [corporate defendant] to [Mark] *at or before the sealing and delivery of this Indenture* (the receipt of which is hereby acknowledged) . . ." At the time of the bill of sale no money had been paid to Mark by the corporate defendant. Although, seven months earlier, the corporate defendant had given a guarantee and a pledge of securities for $104,000 in respect of the Borrower's indebtedness, that guarantee had not been called by the Bank (and it would not be called for two years). The guarantee was a conditional liability of the corporate defendant which, as of July 13, 2005, might, or might not, have ripened into something more. The consideration set out in the bill of sale did not pass as described. The bill of sale is a false document.[17]

104 The integrity of contracts and the world of commerce cannot condone documents deliberately saying one thing and the parties suggesting that they really mean something else. If I were left to my own devices, I would declare the sale of the mobile home to be void on the basis of the bill of sale itself. However, the notice of motion asks for summary judgment in accordance with paragraph 1 of the statement of claim "and such further and other relief as this Honourable Court may deem just." Paragraph 1 of the statement of claim seeks various fraud-related remedies, along with the same general prayer for relief. Neither the pleadings nor the argument on the motion addressed an invalid bill of sale as a discrete basis for a remedy.

105 I do not think that it would be fair to the defendants for me to grant summary judgment based upon an unargued issue. Consequently: (1) the Bank, if so advised, may return the motion, in its present form, before me for argument upon that issue alone; or (2) the Bank, if so advised, may amend its statement of claim to address the issue of the bill of sale and bring a

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

fresh motion for summary judgment based upon that issue alone. The Bank shall, by June 15, 2009, notify the defendants of its intentions in respect of (1) and (2).

VIII Conclusion

106 Subject to paragraph [105], the motion of the plaintiff is dismissed. Alleging, but failing to prove, fraud would usually attract substantial-indemnity costs. However, due to my views on the bill of sale, those costs are nullified (as are costs under subrule 20.06(1) of the *Rules of Civil Procedure*).[18] The costs of this motion, therefore, shall be in the cause (unless the Bank takes either of the courses of action described in paragraph [105], in which case the disposition of costs on this motion shall be left until then).

107 The order of Ramsay J. (enjoining the sale, transfer or encumbering of the mobile home) shall continue in force until trial or otherwise ordered.

Motion dismissed.

Footnotes

1 Mark was required by the Bank, from time to time, to provide personal financial statements as part of the Bank's ongoing monitoring of the Borrower and its security.

2 They included a guarantee from the corporate defendant for $104,000, backed by a pledge of its securities for that amount along with the father's personal guarantee for $71,000.

3 As well, the letter said that the loan was to be permanently reduced to, and capped at, $175,000 by

January 31, 2005.

4 I believe that the two pledged instruments were investment certificates.

5 The certificate does not mention the $71,000 personal guarantee from the father that had been listed in the Bank's letter of December 1, 2004, presumably because the guarantee was not something to be signed by the corporate defendant..

6 I understand that there were earlier defaults, but I do not have the dates.

7 This arrangement was confirmed by the father when he was cross-examined on the affidavit he swore in opposition to this motion:

> Q.58 Who pays for the costs of the mobile home?
>
> A. [Mark] does.
>
> Q.59 . . . Why does [Mark] continue to pay them if he doesn't own the home anymore?
>
> A. He uses it on a regular basis, so he pays the expenses.
>
> . . . . .
>
> Q.63 Okay. So he's responsible for all the fees and expenses?
>
> A. Yes.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

8 The reference to "he" is to the corporate defendant, the father's company.

9 And this, despite the fact that his personal financial statements purported to show other assets.

10 Ben Schu is an account manager with the Bank. He delivered two affidavits in support of the motion for summary judgment.

11 The father was questioned along the same line when he was cross-examined on his affidavit:

> Q.47 Okay. Now you were aware on July 7, 2005, that [the Borrower] was experiencing financial difficulty with the Bank, right?
>
> A. Yes, I think so, I can't remember exactly.

. . . . .

> Q.51 [On July 7, 2005] you were aware that the Bank had some concerns about the [Borrower]?
>
> A. Mm-hmm.

12 This is confirmed in Mr. McDonald's letter.

13 However, he is not a shareholder.

14 *Hercules Management Ltd. v. Ernst & Young*, [1997] 2 S.C.R. 165 (S.C.C.).

15 Although the word "sale" is not used in s. 1, a "sale" is obviously included, for example, in the terms "grant" and "alienation."

16 I also observe that the defendants' accountant may be an important witness at trial, as the sale seems to have flowed from his advice.

17 I cannot go so far as to conclude, on this motion, that the bill of sale is a fraudulent document.

18 Subrule 20.06(1) states: Where, on a motion for summary judgment, the moving party obtains no relief, the court shall fix the opposite party's costs of the motion on a substantial indemnity basis and order the moving party to pay them forthwith unless the court is satisfied that the making of the motion, although unsuccessful, was nevertheless reasonable.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 27

1996 CarswellOnt 440
Ontario Court of Justice (General Division)

Dapper Apper Holdings Ltd. v. 895453 Ontario Ltd.

1996 CarswellOnt 440, [1996] O.J. No. 426, 11 P.P.S.A.C. (2d) 57, 38 C.B.R. (3d) 284

DAPPER APPER HOLDINGS LIMITED v. 895453 ONTARIO LIMITED (c.o.b. DUNN'S FAMOUS DELICATESSEN), INA DEVINE, and FANNY DUNN (née FANNY DANKOVITCH), JASON NYMAN and HAROLD STRUZER (executors and trustees under last will and testament of MYER HYMAN DUNN)

Sedgwick J.

Judgment: February 5, 1996
Docket: Doc. Ottawa 56148/91

Counsel: *Stephen P. Horwitz*, for plaintiff.
Alan Riddell, for defendants.

Subject: Contracts; Corporate and Commercial; Torts; Insolvency; Property

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Fraud and Misrepresentation --- Fraudulent preferences

Fraud and Misrepresentation --- Fraudulent conveyances — Fraudulent intent

Fraudulent conveyances — Reviewable transactions — General security agreement granted by debtor to owners of debtor purporting to secure present and future debts of debtor to owners — Debtor insolvent at time — Creditor bringing action against debtor prior to granting of general security agreement — Moneys advanced by owners to debtor not loans but investments — Owners intending to protect their investment in debtor by shielding assets from unsecured claims of unpaid creditors — General security agreement void as fraudulent conveyance.

Fraudulent preferences — Creditor taking security — General security agreement granted by debtor to owners of debtor purporting to secure present and future debts of debtor to owners — Debtor insolvent at time — Creditor bringing action against debtor prior to granting of general security agreement — Moneys advanced by owners to debtor not loans but investments — Owners not creditors of debtor — Owners intending to protect their investment in debtor by shielding assets from unsecured claims of unpaid creditors — General security agreement void as fraudulent preference.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

The plaintiff brought an action against the defendant delicatessen in September, 1991. In June 1992, a general security agreement ("GSA") was granted by the delicatessen to the defendant ID (the sole director, officer and shareholder of the delicatessen) and the defendant MD purporting to secure all present and future debts and liabilities of the delicatessen to ID and MD by granting them a security interest in all present and future personal property of the delicatessen. No moneys were put into the delicatessen at the same time as the GSA was signed. The plaintiff sought a declaration that the GSA was void against creditors as a fraudulent conveyance or as a fraudulent preference.

Held:

The declaration was granted.

There were no documents supporting the assertion that the moneys put into the delicatessen by ID and MD were loaned to the delicatessen. ID and MD failed to discharge the burden on them to show on a balance of probabilities that the moneys were loans rather than investments. ID and MD were not creditors of the delicatessen. By granting a general security interest under the GSA, the delicatessen intended to put all its present and future assets and property out of reach of the lawful claims of its unsecured creditors, including the plaintiff. ID and MD both knew of and shared this intent. The delicatessen was insolvent at the time the GSA was signed. The giving and taking of the GSA was motivated by the pending action of the plaintiff against the delicatessen. The GSA was a fraudulent conveyance and a fraudulent preference.

Table of Authorities

Cases considered:

Bank of Montreal v. Jory (1981), 39 C.B.R. (N.S.) 30 (B.C. S.C.) — *referred to*

Corp. Agencies v. Home Bank of Canada, [1927] A.C. 318 (P.C.) — *referred to*

Robinson v. Countrywide Factors Ltd., [1978] 1 S.C.R. 753, [1977] 2 W.W.R. 111, (sub nom. *Kozan Furniture (Yorkton) Ltd. v. Countrywide Factors Ltd.)* 14 N.R. 91, 23 C.B.R. (N.S.) 97, 72 D.L.R. (3d) 500 — *referred to*

Statutes considered:

Assignments and Preferences Act, R.S.O. 1990, c. A.33 —

s. 4(1)

s. 5(1)

s. 5(5)(d)

Courts of Justice Act, R.S.O. 1990, c. C.43.

Fraudulent Conveyances Act, R.S.O. 1990, c. F.29 —

s. 2

s. 3

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Personal Property Security Act, R.S.O. 1990, c. P.10.

Action for recovery of debt and for declaration that general security agreement void as against creditors.

***Sedgwick J.*:**

1 This action was commenced by the plaintiff Dapper Apper Holdings Ltd. ("Dapper Apper") against the defendant 895453 Ontario Limited c.o.b. as Dunn's Famous Delicatessen ("Dunn's Deli") by a statement of claim dated September 25, 1991, which was amended on December 24, 1992 to include claims against the defendants Ina Devine ("I. Devine") and her father Myer Dunn ("M. Dunn").

2 The action was set down for trial by the plaintiff on June 8, 1993, and was tried on the Ottawa Civil Non-Jury List on July 5, 6, 7 and 12, 1995.

3 M. Dunn died on September 30, 1993, and on June 28, 1995, an order was made by the Registrar to continue the action against the executors and trustees of his estate, Fanny Dunn née Fanny Dankovitch, Jason Nyman and Harold Struzer. This order is now reflected in the style of cause of this action.

4 At the opening of trial on July 5, 1995, counsel informed me that Dunn's Deli had admitted the allegations in paragraphs 2-6, 8 and 9 of the amended statement of claim. Consequently, at the conclusion of trial on July 12, 1995, judgment was given against Dunn's Deli for $100,000 and pre-judgment interest calculated in the amount of $34,604.93, in accordance with subparagraphs 1.I(a), (b) and (c) of the amended statement of claim.

5 I reserved my decision as to the relief sought by Dapper Apper against the defendants I. Devine and M. Dunn in relation to a General Security Agreement between Dunn's Deli (as "debtor") and I. Devine and M. Dunn (as "secured party"), dated June 17, 1992.

6 A stay was ordered pending my decision as to the validity of the General Security Agreement, both of execution of the judgment against Dunn's Deli given on July 12, 1995, and of any steps or proceedings by the defendants I. Devine and M. Dunn to enforce the General Security Agreement (Letter to counsel, dated July 13, 1995).

7 As a result of the judgment given at the conclusion of trial on July 12, 1995, Dapper Apper is an unsecured judgment creditor of Dunn's Deli for $134,604.93 and post-judgment interest calculated in accordance with the *Courts of Justice Act*.

8 The sole issue remaining for determination by the court is whether the General Security Agreement granted by Dunn's Deli to I. Devine and M. Dunn is void as against creditors as a fraudulent conveyance under the *Fraudulent Conveyances Act*,

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

R.S.O. 1990, c. F.29 or as a fraudulent preference under the *Assignments and Preferences Act*, R.S.O. 1990, c. A.33.

Facts

9 At trial, the Plaintiff's Book of Documents was entered as Exhibit 1 and the Plaintiff's Supplemental Book of Documents was entered as Exhibit 2. The Defendant's Book of Documents was entered as Exhibit 4. When referring in these reasons to a document in these Books of Documents, I shall refer to it by the tab number in the appropriate Book of Documents (Ex. 1, Ex. 2 or Ex. 4).

Business Relationships

10 M. Dunn lived in Montreal. He was the founder of a well-known restaurant there known as "Dunn's Famous Delicatessen". His daughter I. Devine was associated with him in the restaurant business in Montreal. She continued to be associated with him in the Montreal restaurant business after her marriage to Stanley Devine ("S. Devine").

11 According to the evidence, in the early summer of 1990, the defendant M. Dunn decided to open a similar restaurant in Ottawa, to be carried on under the same name, "Dunn's Famous Delicatessen". For that purpose, the corporate defendant Dunn's Deli was incor porated on July 4, 1990, with the defendant I. Devine as its sole officer, director and shareholder (Ex. 1, Tab 3). The restaurant opened for business in October 1990.

12 S. Devine, the husband of I. Devine, was an employee of Dunn's Deli. He was also an authorized signing officer on the bank account of Dunn's Deli, with full power to act alone (Ex. 1, Tab 4). At the time of the events out of which this action arises, he was also an undischarged bankrupt, having made an assignment in bankruptcy on September 4, 1991.

13 Of these three individuals, only I. Devine testified at trial. M. Dunn passed away on September 30, 1993. S. Devine did not testify. However, from the evidence of I. Devine at trial as to the business relationship with her father and husband, and from the evidence of the defendants' other witnesses bearing on the decision-making process in relation to Dunn's Deli and other related family business activities, these three individuals were the management team for Dunn's Deli.

14 S. Devine was responsible to his father-in-law and wife for the daily operations of the restaurant and other business activities of Dunn's Deli. There is little doubt that he was allowed by them to represent himself as a proprietor in the business, both in its internal operations and in its external relations.

15 The arbiter in the decision-making process was M. Dunn, in consultation with his daughter, I. Devine. It was he who decided to open the restaurant in Ottawa. Later, it was he who in July 1992, decided to expand and to open a similar restaurant under the same name in Toronto. It was he who was asked by the Devines to consider and decide on a proposal to go public and franchise "Dunn's Famous Delicatessen" restaurants in Canada and the United States. Dunn's Deli had a role to play in both the expansion to Toronto and the franchising proposal.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

16 From the evidence of I. Devine at trial, I am satisfied that her business relationship with her father was close and based on trust between them. I do not think it likely or probable that they withheld any significant information from each other which related to their mutual business interests. A businessman of M. Dunn's experience and success would have recognized and not tolerated anything less than complete candour from his daughter and son-in-law. On the evidence, I am satisfied that this was the reality of how the business of Dunn's Deli was conducted.

Financial Records of Dunn's Deli

17 I am also bound to say that the business of Dunn's Deli, and particularly its financial record-keeping, was conducted with scant regard for the niceties of corporate form and generally accepted accounting principles. Other family businesses may be as informally conducted. However, in this case, the uncertainty about trustworthy internal accounting records has made the task of determining the factual issues more difficult.

18 The Ottawa business venture carried on by Dunn's Deli was not a financial success. In her evidence, I. Devine stated that Dunn's Deli has never earned a profit. To continue in its business, Dunn's Deli has, since the beginning, also required very large infusions of money from I. Devine and M. Dunn.

19 According to her evidence, I. Devine has put $1,750,526 into Dunn's Deli since the beginning and her father M. Dunn put $499,922.75. These aggregate amounts are based on summary statements prepared by the defendants for purposes of trial and purportedly based on Dunn's Deli's accounting records (Ex. 4, Tabs 1, 10, 11, 12, 13 and 14).

The General Security Agreement ("GSA")

20 For the purpose of this action, June 17, 1992 and June 29, 1992 are significant dates. The GSA, the validity of which is the subject of this action, is dated June 17, 1992 and was signed by I. Devine on behalf of Dunn's Deli on June 29, 1992 (Ex. 2, Tab 3). The GSA purports to secure all present and future debts and liabilities of Dunn's Deli to I. Devine and M. Dunn (the "Secured Party") by granting them a security interest in all present and future personal property of Dunn's Deli, tangible and intangible. The security interest created under the GSA (para. 1) was subsequently perfected by registration of a financing statement under the *Personal Property Security Act* (Ontario) on July 22, 1992 under No. 927221410-0028-4765.

21 On June 29, 1992, I. Devine and M. Dunn signed a security sharing agreement under which they agreed to share all proceeds realized on enforcement of the GSA rateably between them (Ex. 2, Tab 3).

22 In my view, the date at which the validity of the GSA must be determined is June 29, 1992, the date on which it was signed by I. Devine on behalf of Dunn's Deli.

Money Put into Dunn's Deli by I. Devine and M. Dunn

23 Up to June 29, 1992, according to the summary statements prepared by the defendants (Ex. 4, Tabs 1, 10, 11 and 12), I. Devine had put $809,617 into Dunn's Deli and her father M. Dunn had put $250,000. No moneys were put into Dunn's

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Deli at the same time as the GSA was signed on June 29, 1992. Prior to that date, I. Devine last put money into Dunn's Deli on December 11, 1991; and after that date, she next put money in on August 19, 1992. Prior to June 29, 1992, M. Dunn last put money into Dunn's Deli on June 19, 1991; and after that date, M. Dunn next put money in on March 22, 1993.

24 I would add that the summary statements from which these figures are derived were not the only calculations of the amounts put into Dunn's Deli by I. Devine and M. Dunn produced at trial. These statements were prepared and produced by the defendants on the eve of trial. The amounts are significantly greater than those set out in responses to undertakings given on the examinations for discovery of S. Devine on behalf of Dunn's Deli on July 7, 1992 (See Ex. 2, Tab 5, No. 4).

Was the Money Put into Dunn's Deli as Loans on Investments?

25 The defendants say that all moneys put into Dunn's Deli by I. Devine or M. Dunn, either before or after June 29, 1992, were loans made by them to Dunn's Deli. They say, therefore, that they are creditors of Dunn's Deli for those amounts. I would, however, observe that in the response to undertakings given on behalf of Dunn's Deli (referred to in the preceding paragraph of these reasons), they were referred to as "investments".

26 Dapper Apper says that these moneys were either put into Dunn's Deli as investments or, in the case of M. Dunn, possibly as a voluntary contribution to Dunn's Deli to assist his daughter and son-in-law in the business of the Ottawa restaurant or as a conduit to other family business ventures, such as the Toronto restaurant (through a separate corporation) or the franchising proposal.

27 In order to determine this issue, audited (or even unaudited) financial statements of Dunn's Deli prepared by an accountant would ordinarily have provided a useful starting point. However, in this case, the defendants have refused to produce any financial statements of Dunn's Deli prepared and signed by an accountant.

28 In particular, they have refused to produce annual statements for the financial years ending May 31, 1991 and May 31, 1992. Their refusal to produce these statements, particularly for the 1992 financial year, which ended on May 31, 1992, less than one month before the GSA was signed, has deprived the court of evidence which would have been helpful in determining the characterization of the moneys put into Dunns Deli by I. Devine and M. Dunn as loans or otherwise; and also in determining whether Dunns Deli was insolvent on June 29, 1992. I draw adverse inferences against the defendants on both these factual issues, from their refusal to produce any financial statements of Dunn's Deli prepared and signed by its external auditor or accountant; as well as from their unexplained failure to call the external auditor or accountant of Dunn's Deli as a witness at trial.

29 The only "financial statements" produced by Dunn's Deli at trial were draft unaudited financial statements for the period from July 4, 1990 to May 31, 1991 (Ex. 1, Tab 6), an unidentified balance sheet and statement of operations for the seven months ended December 31, 1991 (Ex. 1, Tab 6) and an internally produced computer printout of accounts payable and accrued liabilities at February 8, 1992 (Ex. 1, Tab 6). I shall comment later on the oral evidence of Gerald Thaw (Dunn's Deli's bookkeeper) which accompanied these "financial statements".

30 The balance sheet included in the draft financial statements of Dunn's Deli as at May 31, 1991, contains an item for

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

loans from shareholders and directors ($341,364); and the unidentified balance sheet as at December 31, 1991, contains a time for director loans ($553,737). The only director or shareholder of Dunn's Deli was I. Devine. Her father M. Dunn was neither a director nor a shareholder. Although there are specific items and notes in these documents which refer to Dunn's Deli's long-term debt and bank indebtedness (both current and long-term), there is no identifiable reference to any debt owing by Dunn's Deli to M. Dunn.

31 As to documents supporting the assertion that all these moneys put into Dunn's Deli were loaned to Dunn's Deli by I. Devine or M. Dunn, there are none. There are no loan agreements. There are no promissory notes or other evidences of indebtedness. There is no documentary evidence of any obligation to repay these moneys (other than entries in the computer cheque registers internally prepared by G. Thaw on instructions from S. Devine, see para. 35). There is no documentary evidence as to the terms of the alleged loans including any obligation to pay (or not to pay) interest.

32 The documentary evidence which was tendered by the defendants to support the assertion that all these moneys were loans to Dunn's Deli, is unsubstantial and inconclusive. Evidence of bank deposit books (Ex. 3) and cheques and monthly bank statements (Ex. 4) at most prove the deposit of the moneys into the bank account of Dunn's Deli. There is nothing in them which assists in the characterization of the deposits as loan proceeds or otherwise.

33 The computer cheque registers of Dunn's Deli (Ex. 1, Tabs 8-10) tendered by the defendants, as explained at trial by G. Thaw, who as the bookkeeper of Dunn's Deli prepared them, are also unsatisfactory as evidence of the characterization of loan proceeds and loan "repayments" which they purport to contain. From G. Thaw's evidence, it is clear that he took his instructions from S. Devine as to what computer entries were to be designated as loan proceeds and repayments. He exercised no independent judgment on the matter throughout the period with which this action is concerned.

34 Yet these registers were the basis for the summary statements (Ex. 4, Tabs 1, 10, 11, 12, 13 and 14) relied on by the defendants at trial as proof of loan advances and repayments.

Cheque Kiting Schemes

35 G. Thaw did as he was told by S. Devine in making entries in the computer cheque registers. Indeed, he was told to record a significant number and amount of advances from S. Devine himself to Dunn's Deli. Under vigorous re-examination by his own counsel, G. Thaw recalled that these "advances" were not really advances by S. Devine at all. In preparing the computer cheque registers, he had used the "wrong terminology". They were actually related to several cheque kiting schemes involving S. Devine and others to which, he said, I. Devine was privy.

36 It was explained that the purpose of these recurring cheque kiting schemes was to artificially inflate the balance in Dunn's Deli's bank account during periods when there were insufficient revenues coming in to pay its current debts. G. Thaw specifically identified May 1991, June-August 1991 (in excess of $100,000) and September-October 1992, as three periods when cheque kiting occurred.

37 Kiting consists of knowingly writing cheques against a bank account where there are insufficient funds in the account to cover them, in the expectation that the necessary funds will be deposited before the kited cheques are presented to the bank

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

for payment. The cheques are drawn against deposits that have not yet cleared through the banks involved. A kiting scheme takes advantage of the time which elapses between the deposit of a cheque in one bank and its collection at another. *Corp. Agencies Ltd. v. Home Bank of Canada*, [1927] A.C. 318 (P.C.). In Canada, kiting is a criminal offence. *N. L'Heureux, Le droit bancaire*, 86.

Treatment in Dunn's Deli's Financial Records

38 One of the reasons advanced by the defendants for characterizing the amounts put into Dunn's Deli by I. Devine and M. Dunn as loans (rather than investments) was that, in the accounting records of Dunn's Deli, some repayments of these moneys are recorded. However, in the summary statements (Ex. 4, Tabs 7, 10, 11, 12, 13 and 14) upon which the defendants rely, it is instructive to note that the specific repayment dates during successive periods are not stated, although specific dates are indicated for the advances. G. Thaw in his evidence said that there was "no particular reason "for the omission of specific repayment dates from these statements (referring in his evidence, specifically to Ex. 4, Tabs 10, 11).

39 Although G. Thaw stated that the "advances" referred to in these statements were treated as loans by I. Devine and M. Dunn in the books of Dunn's Deli and were also treated as loans by its "auditors", the external auditor or accountant of Dunn's Deli was not called to testify at trial to confirm this assertion.

Other than Corporate Purposes

40 There was also evidence that some of the money put into Dunn's Deli by I. Devine and M. Dunn was not used or intended to be used for the corporate purposes of Dunn's Deli at all, but was for other family projects such as the Toronto restaurant and the franchising proposal. For this money Dunn's Deli was merely a conduit.

41 According to I. Devine, planning for the Toronto restaurant began in July 1992 and it was opened in December 1992. Ronald C. Shryvman, a former employee of Dunn's Deli in Ottawa, testified that he went to Toronto in November 1992 to manage the Toronto restaurant, which was operated through a separate corporation (1004213 Ontario Limited) but was treated by I. Devine and S. Devine as if it were part of Dunn's Deli for management and operational purposes. The shareholder of 1004213 Ontario Limited was Nonie Devine, the daughter of I. Devine and S. Devine.

42 There is also evidence that on October 23, 1991, a cheque for $60,007.80 was drawn on the bank account of Dunn's Deli to pay for a U.S. dollar bank draft in favour of "Murray Baeal" (Ex. 1, Tab 10, p. 317). He was identified by G. Thaw as a "financier and stockbroker" advising M. Dunn, I. Devine and S. Devine about going public in connection with the franchising proposal which was under discussion in 1991 and 1992. G. Thaw was unable to recall the purpose of the specific payment to Murray Baeal on October 23, 1991. I. Devine testified that M. Dunn told S. Dunn to pay this amount out of the account of Dunn's Deli as "the franchising would come out of Ottawa".

43 In the circumstances of this case, the defendants carry an evidentiary burden to show on a balance of probabilities that the moneys put into Dunn's Deli by I. Devine and M. Dunn were loans made by them to Dunn's Deli. In my view, they have not discharged this burden. I am not satisfied by the documentary and oral evidence tendered at trial on their behalf that it is more probable than not that the moneys were in fact loans made by I. Devine and M. Dunn to Dunn's Deli.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Intention of Parties to GSA

44 The GSA was signed by I. Devine on behalf of Dunn's Deli on June 29, 1992. As I have stated, that is, in my view, the date at which its validity must be determined. That is the date at which the court must determine whether, as alleged by Dapper Apper, the GSA is void as against creditors of Dunn's Deli as a fraudulent conveyance under the *Fraudulent Conveyances Act* or as a fraudulent preference under the *Assignments and Preferences Act.*

45 In that regard, the intention and knowledge of the parties to the GSA on June 29, 1992, and the solvency of Dunn's Deli on that date are relevant to one or other or both of the statutory remedies upon which Dapper Apper relies.

46 As to the intention and knowledge of the parties to the GSA on June 29, 1992, the evidence of I. Devine upon which the defendants rely is that the intention of herself and her father M. Dunn as the recipients (or grantees) of the security interest created by Dunn's Deli (as grantor) under the GSA over all its present and future property and assets was solely to ensure that her loans and her father's loans were repaid. Their reason was to protect the loans "against any creditors". This candour was elicited on cross-examination. Although she says she was aware of the claim of Dapper Apper as a creditor, she denies that she had mentioned the claim to her father M. Dunn.

47 In creating the security interest in favour of I. Devine and M. Dunn under the GSA, Dunn's Deli as debtor may, in my view, be presumed to have had the same intention as I. Devine, who as its sole officer and director (as well as its sole shareholder), signed the GSA on its behalf.

48 In determining the intention and knowledge of the parties to the GSA on June 29, 1992, I have taken the following additional evidence into consideration:

(1) this action was commenced by Dapper Apper to enforce its $100,000 claim against Dunn's Deli on September 25, 1991. Service of the statement claim would have brought knowledge to Dunn's Deli and to I. Devine its sole officer, director and shareholder, if not to M. Dunn, who was only added as a defendant on December 24, 1992, as a consequence of the GSA.

(2) On May 15, 1992, six weeks before the GSA was signed, Dapper Apper had unsuccessfully moved for summary judgment against Dunn's Deli on the statement of claim.

(3) On June 2, 1992, four weeks before the GSA was signed, settlement discussions were held at the offices of the solicitors for Dunn's Deli regarding Dapper Apper's action and claim.

(4) After the settlement meeting had concluded, the CEO of Dapper Apper (Barry Appel) testified that the solicitor for Dunn's Deli said to him that if the proposed settlement was not agreed upon, Dunn's Deli would "slap on a GSA". This evidence was admitted, subject to my satisfaction as to its relevance. I am satisfied that it is relevant and confirm that in my view, the statement was not made in privileged circumstances.

(5) According to the evidence of I. Devine, her father M. Dunn's reaction to being informed of the proposal for Dunn's Deli to grant a general security interest under a GSA in favour of I. Devine and himself was to "take it out as fast as you can".

(6) Although examinations for discovery of S. Devine on behalf of Dunn's Deli were held about a week after the GSA was signed, and although S. Devine disclosed in response to a question that the GSA had been signed in favour of I.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Devine and M. Dunn, his counsel refused to let him disclose the date on which the GSA had been signed (Transcript, pp. 83-5, Q 506-511).

In the circumstances of this case, I am satisfied that by granting a general security interest under the GSA to I. Devine and M. Dunn on June 29, 1992, Dunn's Deli intended, in my view, to put all its present and future property and assets out of reach of the lawful claims of its creditors (including Dapper Apper). I am also satisfied that I. Devine and M. Dunn, the grantees of the general security interest both knew and shared this intent. The primary objective of the parties to the GSA was, in my view, to shield the present and future property and assets of Dunn's Deli from its unsecured creditors (including Dapper Apper) by making them subject to a general security interest in favour of the investments of family members in Dunn's Deli. I have made a finding that these investments were not loans to Dunn's Deli (see para. 43). It follows from that finding that I. Devine and M. Dunn are not creditors of Dunn's Deli.

Solvency of Dunn's Deli

49 The defendants maintain that Dunn's Deli was solvent at June 29, 1992. According to the evidence of I. Devine and G. Thaw, Dunn's Deli had a policy of not paying creditors when their debts were due. Debts were only paid under pressure from the creditors. Terms would be sought from the creditors and payment further delayed. Inevitably, some impatient creditors would take their claims to the courts and even obtain judgments against Dunn's Deli. During the course of their evidence, these witnesses recalled by name a significant number of these court proceedings by creditors but had great difficulty recalling when in the history of Dunn's Deli they had arisen or been settled or otherwise disposed. Apparently, they were treated as by Dunn's Deli as an incident of doing business with its creditors in this way.

50 In summary, the defendants say that Dunn's Deli was not insolvent on June 29, 1992, because it would have been able to pay its debts "if we so desired", and if its creditors were prepared to accept terms of 30, 60, 90 days or longer, even though it was admitted that there was no cash on hand in June 1992 (G. Thaw).

51 In determining the solvency of Dunn's Deli at June 29, 1992, I have also taken the following evidence into consideration:

(1) the draft financial statements of Dunn's Deli for the period from July 4, 1990 to May 31, 1991 (Ex. 1, Tab 6) indicate an excess of liabilities over assets of $154,618; and the unidentified balance sheet as at December 31, 1991 (Ex. 1, Tab 6) indicates an excess of liabilities over assets of $219,989. The same documents indicate a loss (before income taxes) of $154,718 during the financial period ending May 31, 1991 and a loss of $72,456 during the seven month financial period ending December 31, 1991. I have expressed my concerns about the unsatisfactory nature of these documents elsewhere in these reasons (paras. 17, 27-29). I have also expressed my view about the refusal of the defendants to produce signed financial statements of Dunn's Deli, for these periods and for the financial year ended May 31, 1992, immediately before the granting of the GSA (paras. 27-29). In the absence of other evidence, however, I would infer from these financial statements that Dunn's Deli liabilities exceeded its assets at the dates of the two financial statements; that the gap was widening; and that there is no reason to believe that the financial condition of Dunn's Deli improved between December 31, 1991 and June 29, 1992.

(2) the cheque kiting schemes described elsewhere in these reasons (paras. 35-37), which were conducted through the Dunn's Deli bank account for the admitted purpose of giving the corporate defendant the appearance of solvency and ability to pay its creditors.

(3) as to the $100,000 claim of Dapper Apper specifically, the admission by G. Thaw that Dunn's Deli did not have the money to pay Dapper Apper's claim in June 1992.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(4) evidence of I. Devine that during the first two years of operation, the cash flow problem was "awful" and that in the spring of 1992 the "money was all going out", as well as her acknowledgment that in June 1992, Dunn's Deli could not have paid its creditors in full.

52 On this evidence as to the financial condition of Dunn's Deli, I am satisfied that it is more probable than not that on June 29, 1992, Dunn's Deli was insolvent. There is no doubt that on that date it was unable to pay its creditors (and specifically, the claim of Dapper Apper) in full within the meaning of the *Assignments and Preferences Act*.

Law

53 Dapper Apper seeks a declaration on behalf of itself and other creditors of Dunn's Deli that the GSA granted by Dunn's Deli to I. Devine and M. Dunn on June 29, 1992, is void as against Dapper Apper and other creditors of Dunn's Deli.

54 Dapper Apper says that the GSA is void because it is a fraudulent conveyance under the *Fraudulent Conveyances Act* or a fraudulent preference under the *Assignments and Preferences Act*, or both. These statutory remedies will be considered in turn.

Fraudulent Conveyances Act

55 This Act applies to every "conveyance" (including a "charge") of real or personal property which is made "with intent to defeat, hinder, delay or defraud creditors and others". A conveyance made by the grantor with this intent is void as against the creditors and others (sec. 2).

56 If, however, a conveyance is made with this intent on the part of the grantor "upon good consideration and in good faith" to a person not having at the time of the conveyance to that person "notice or knowledge" of the intent of the grantor (sec. 3), the "conveyance" is not void as against the creditors and others.

57 If the court is satisfied that a conveyance is made with intent on the part of the grantor to defeat, hinder, delay or defraud creditors and others, the parties to the conveyance (the grantor and the grantees) must show that it was made for good consideration and good faith and to a person (or persons) who was (or were) without notice or knowledge of the grantor's fraudulent intent. *Bank of Montreal v. Jory* (1981), 39 C.B.R. (N.S.) 30 (B.C. S.C.). Otherwise, the conveyance is void against creditors of the grantor.

58 I am satisfied that Dunn's Deli (the grantor) by signing the GSA and delivering it to I. Devine and M. Dunn (the grantees) on June 29, 1992, intended to "defeat, hinder, delay or defraud" creditors within the meaning of section 2 of the *Fraudulent Conveyances Act*. By the stroke of a pen wielded by I. Devine (one of the grantees), she and her father M. Dunn (the other grantee) were given the status of secured creditors in respect of their investments in Dunn's Deli, while the property and assets of Dunn's Deli were shielded from the unsecured claims of Dapper Apper and other unpaid creditors of Dunn's Deli. That, in my view, indicates an intent to defeat, hinder, delay or defraud those unpaid unsecured creditors.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

59 In my view, the giving and taking of the GSA was motivated by the pending action of Dapper Apper against Dunn's Deli for $100,000, which was being vigorously prosecuted at the time and the inability or unwillingness of Dunn's Deli to settle the action on terms acceptable to Dapper Apper, as evidenced by the unsuccessful settlement discussions early in June 1992.

60 The defendants say that the GSA was motivated by the need of I. Devine and M. Dunn to protect their investments in Dunn's Deli. However, the protection of investments and the defeating, hindering and delaying of the claims of other creditors are two sides of the same coin.

61 Have the defendants discharged the evidentiary burden of showing, in the words of section 3 of the Act, that the GSA was given by Dunn's Deli in favour of I. Devine and M. Dunn:

(1) "upon good consideration"

(2) "and in good faith"

(3) "to a person not having at the time of the conveyance to the person notice or knowledge of the intent set forth in that section [2]".

In my view, they have not.

62 Based on the findings of fact set out earlier in these reasons as to the failure of the defendants to discharge the evidentiary burden as to the characterization of the moneys put into Dunn's Deli by I. Devine and M. Dunn as loans (para. 43), and as to the intention of the parties to the GSA (para. 48), I am not satisfied by the evidence of the defendants that it is more probable than not that the GSA was made "upon good consideration and in good faith". Even if I had decided in favour of the defendants on this issue, I am not satisfied that it is more probable than not that I. Devine or M. Dunn were persons who on June 29, 1992 had no notice or knowledge of the intent of Dunn's Deli to defeat, hinder, delay or defraud its creditors.

63 I. Devine signed the GSA on behalf of Dunn's Deli. She is clearly a person having notice or knowledge of the intent of Dunn's Deli of which she was the sole officer, director and shareholder. I am also satisfied that it is more probable than not that her father M. Dunn was also aware of the intent of Dunn's Deli. There was a close family and business relationship between father and daughter. He was kept closely informed by his daughter on business matters relating to Dunn's Deli and was well aware and concerned about its financial condition, as evidenced by his swift reaction to the suggestion that a GSA be obtained to protect his investment in Dunn's Deli.

Assignments and Preferences Act

64 This Act applies to every "gift, conveyance, assignment or transfer ..." of real or personal property which is made by a person when

(1) insolvent,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(2) unable to pay his debts in full, or

(3) he knows that he is on the eve of insolvency,

if the gift, conveyance, assignment or transfer is made "with intent to defeat, hinder, delay or prejudice" any one or more creditors of the person.

65 If made with this intent, the gift, conveyance, assignment or transfer is void as against the creditor(s) "injured, delayed or prejudiced" (sub-section 4(1)).

66 If, however, the gift, conveyance, assignment or transfer is made "in good faith" and "in consideration of a present actual payment in money" or "by way of security for a present actual advance of money" where the "money paid" bears "a fair and reasonable relative value to the consideration therefor", the "gift, conveyance, assignment or transfer is not void as against the creditor(s) (sub-section 5(1)).

67 The Act further provides that nothing in the Act invalidates a security given to a creditor for a pre-existing debt, where because of the giving of the security, "an advance in money" is made to the debtor by the creditor in the belief that the advance will enable the debtor to continue its trade or business and to pay the debts of the debtor in full [subsection 5(5)(d)].

68 The defendants I. Devine and M. Dunn rely on subsections 5(1) and 5(5)(d) of the Act as applying to the GSA. In my view, neither of these sub-sections applies to the GSA. Based on the finding of fact set out earlier in these reasons as to the failure of the defendants to discharge the evidentiary burden as to the characterization of the moneys put into Dunn's Deli by I. Devine and M. Dunn as loans (para. 43), the individual defendants are not creditors of Dunn's Deli but investors in Dunn's Deli (para. 48). Even if I had decided in favour of these defendants on this issue, no "present actual advance" [subsection 5(1)] or "an advance in money" [subsection 5(5)(d)] was made to Dunn's Deli by either of them at or about the same time as the GSA (June 29, 1992).

69 As pointed out in para. 23 of these reasons, no moneys were put into Dunn's Deli I. Devine between December 11, 1991 and August 19, 1992. No moneys were put into Dunn's Deli by M. Dunn between June 19, 1991 and March 22, 1993. However these moneys put into Dunn's Deli by I. Devine and M. Dunn may be characterized, they are not present actual advances within the meaning of sub-section 5(1) of the Act. In my view, subsection 5(5)(d) of the Act relates only to a security given to secure past advances and advances made at the same time as the giving of the security.

70 For the same reasons and based on the same evidence I have discussed in these reasons in relation to the *Fraudulent Conveyances Act*, I think that the GSA is a gift, conveyance, assignment or transfer which, within the meaning of the *Assignments and Preferences Act* was made by Dunn's Deli to I. Devine and M. Dunn with intent to defeat, hinder, delay or prejudice Dapper Apper and other creditors of Dunn's Deli.

71 By giving I. Devine and M. Dunn the status of secured creditors of Dunn's Deli, the GSA clearly creates a preference in their favour over the claims of Dapper Apper and other unsecured creditors of Dunn's Deli.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

72 On June 29, 1992, was Dunn's Deli (1) insolvent, (2) unable to pay its debts in full or (3) did it know itself to be on "the eve of insolvency", within the meaning of the Act? I note that the Act sets out three alternative financial conditions of Dunn's Deli, to be considered by the court. *Robinson v. Countrywide Factors Ltd.* (1977), 23 C.B.R. (N.S.) 97 (S.C.C.). I take "insolvency" to be a state in which Dunn's Deli is unable for any reason to pay its debts in the ordinary course of business as they generally become due. *Robinson v. Countrywide Factors Ltd., supra.*

73 On the evidence of the financial condition of Dunn's Deli reviewed earlier in these reasons and my finding of fact set out in para. 52, I have concluded that on June 29, 1992, Dunn's Deli was probably insolvent and was certainly unable to pay its creditors in full within the meaning of the Act.

74 Accordingly, the GSA is, in my opinion, both a fraudulent conveyance within the meaning of the *Fraudulent Conveyances Act* and void as against Dapper Apper and other creditors of Dunn's Deli un der that Act; and a fraudulent preference within the meaning of the *Assignments and Preferences Act* and void as against Dapper Apper and other creditors of Dunn's Deli. Dapper Apper is entitled to a declaration to that effect.

75 Dapper Apper is also entitled to its costs of this action on a party and party scale.

Action allowed.

End of Document Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 28

1977 CarswellAlta 175
Alberta Supreme Court, Trial Division

Burton v. R & M Insurance Ltd.

1977 CarswellAlta 175, 26 C.B.R. (N.S.) 49, 5 Alta. L.R. (2d) 14, 81 D.L.R. (3d) 455, 9 A.R. 589

BURTON v. R & M INSURANCE LTD. AND POOLE

Dechene J.

Judgment: December 19, 1977
Docket: Edmonton No. 121749

Counsel: *P. B. O'Leady*, for plaintiff.
K. R. Laycock, for defendants.

Subject: Corporate and Commercial; Insolvency; Contracts; Torts

Related Abridgment Classifications

For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Fraud and Misrepresentation --- Fraudulent preferences — Validity of provincial legislation

Fraud and Misrepresentation --- Fraudulent preferences — Practice and procedure — Burden of proof

Fraudulent preferences — Fraudulent conveyances — Payments to president and controlling shareholder of debtor company — All assets disbursed — No property available to satisfy judgment of plaintiff — Payments set aside.

The defendant company agreed to purchase an insurance business owned by the plaintiff, with the purchase price payable in instalments. By the time the plaintiff had recovered judgment against the defendant company, it had disposed of all its assets. Payments totalling $19,084.74 were made to the individual defendant for wages due and repayment of shareholders' loans. At all times the individual defendant was the majority shareholder, a director, the president and the chief executive officer of the defendant company. The plaintiff alleged that the payments made by the defendant company to the individual defendant were made fraudulently and with the intent to defeat, hinder, delay and prejudice the creditors of the company.

Held:

The payments should be set aside under both the Statute of Elizabeth, 1571, and the Fraudulent Preferences Act of Alberta. Under the Statute of Elizabeth, the intent to defraud the plaintiff must be presumed because the payments

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

divested the defendant company of all its assets, thereby defeating the claim of the plaintiff. The individual defendant did not satisfy the onus of proof placed upon him to establish that he had a bona fide claim against the defendant company. Under the Fraudulent Preferences Act, the defendant company was insolvent, and by stripping itself of its assets it defeated the plaintiff's claim. As a result of the close relationship between the defendant company and its major shareholder, there was a common intent between them.

Table of Authorities

Cases considered:

Applied:

Koop v. Smith (1915), 51 S.C.R. 554, 8 W.W.R. 1203, 25 D.L.R. 355.

Bludoff v. Osachoff, 22 Sask. L.R. 533, [1928] 2 W.W.R. 150, [1928] 3 D.L.R. 179 (C.A.).

Goyan v. Kinash, [1945] 1 W.W.R. 291, [1945] 2 D.L.R. 749 (Alta.).

Re Martineau (1969), 5 D.L.R. (3d) 165 (B.C.).

Bank of N.S. v. Zgurski (1970), 14 C.B.R. (N.S.) 185, 72 W.W.R. 464 (Alta.).

Faulhaber v. Ulseth, [1976] 4 W.W.R. 48, 66 D.L.R. (3d) 488 (Alta.)

Statutes considered:

Statute of Elizabeth, 1571, ss. 1, 2.

Fraudulent Preferences Act, R.S.A. 1970, c. 148.

Application to set aside payments as both fraudulent preferences and fraudulent conveyances.

***Dechene J.*:**

1 The plaintiff, James A. Burton, was a licensed insurance agent acting as a broker for the sale of various types of insurance contracts. In particular he became interested in selling to members of the Calgary Home Builders Association, later known as the Housing and Urban Development Association of Calgary, contracts of participation in a policy of group insurance issued by Crown Life Insurance Company. This was a remunerative undertaking, but in the fall of 1972 his health failed and he could no longer carry on his business. He thereupon entered into a verbal contract with the defendant company through the defendant Poole, its authorized representative, to sell all his right and interest as an agent of the above-mentioned group insurance plan for a total price of $10,000. The plaintiff performed his part of the contract by assigning all his interest

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

therein to the defendant. The price of $10,000 was payable in instalments which included a payment of $5,000 to be paid out of the first commissions earned by the defendant company from the sale of the said group insurance participation contracts. I find as a fact that the said earned commissions exceeded $5,000 so that the entire purchase price became due and payable.

2 No part of the said purchase price has been paid by the defendants to the plaintiff. In March 1974 the plaintiff sued the defendant R & M Insurance Limited and on 27th November 1975 obtained default judgment for $10,000 plus $912.45 costs. By that time the defendant company had disposed of all its assets in the manner described hereunder and the plaintiff recovered nothing.

3 At all material times, the defendant Poole was the majority shareholder, a director, the president and chief executive officer of the defendant company. After the issue and service of the first statement of claim against the company, Poole instructed his solicitors to file a statement of defence.

4 On 1st February 1974 Poole sold the assets of the company to one Boyd who paid the sum of $11,000 in cash to the company. Between 1st February 1974 and 30th July 1974 the company paid to the defendant Poole sums totalling $14,084.74. The plaintiff alleges that this distribution of the company's asset to the defendant Poole was made fraudulently and with intent to defeat, hinder, delay and prejudice the creditors of the company. The defendant Poole argues that he was a bona fide creditor of the company for wages due to him and for repayment of shareholders' loans which were credited to him on the company's books. He says that the payments which he received were apportioned as follows: management fees, $6,560; shareholders' loans, $7,525.

5 The company's operation was not very profitable. Its financial statements show losses in each year after paying salaries, commissions, shareholders' loans and management fees as shown on the following table compiled from its financial statements. The company's year end was 31st May, and each of the financial statements shows the following figures:

Year Ending	Income	Deficit	Salaries, etc.
31st May 1972	$12,626	$ 707	$10,000
31st May 1973	14,299	11	11,300
31st May 1974	7,435	7,010	6,550
31st May 1975	243	345	nil

6 In the last above-mentioned year the company had virtually ceased to carry on business. Its income from commissions was only $243 and its statement of assets and liabilities showed that the assets had been reduced to nil and revealed a deficit of $7,256. This was shown as a liability of the company in favour of the defendant Poole in the same amount.

7 The defendant company did not maintain complete and accurate books of account. After the first year of operation, it brought its records to an accountant, one Joseph Hautman. These consisted mainly of cancelled cheques, bank statements, deposit slips, cash and expense vouchers. Mr. Hautman prepared financial statements and income tax returns in such a way as to avoid liability for taxes by taking advantage of the defendant Poole's personal exemptions and by showing some payments to him as wages or salary and by showing others as repayment of shareholders' loans. In fact no actual loans of money had been made by Poole to the company. The loan account had been set up in the first place by showing an item of $15,000 for

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

goodwill. It is noted also that there are discrepancies between the amounts which the company records show as wages or management fees paid to Poole and the income of Poole reported in his personal income tax returns. These are signed by Poole but were prepared by the accountant and Poole says that he relied on the accountant and signed them without question.

8 The plaintiff called, as an expert witness, Mr. Leslie E. Skingle, a chartered accountant and graduate lawyer. He examined the defendants' financial records and questioned the validity of the original goodwill entry. I accept his evidence and find as a fact that there was no legal liability of the company to its shareholders for goodwill or loans.

9 When incorporated in June 1971, the company allotted 50 shares to each of the defendant Poole and one Stanley E. Marshall. On 15th January 1973 Marshall transferred 49 of his shares to the defendant Poole and the remaining one share to Mrs. Poole, the defendant's wife. The company did not prosper and in July 1973 attempts were made to sell its assets, culminating in the sale to Boyd on 1st February 1974. Poole agreed to work for Boyd for a time to familiarize him with the operation of the company's business. It therefore seems clear to me that Poole was not entitled to any salary or management fee from the company after 1st February 1974 and that the money which Boyd paid to the company was not subject to any personal claim by him. In fact Poole started to work for other employers on 1st April 1974 and the defendant company has sold no insurance nor conducted any business since 31st January 1974.

10 Coming back now to the plaintiff's original action against the company, the defendant Poole actively defended that action until the company had disbursed all its assets. It then instructed its solicitors to withdraw from the action by the plaintiff and on 24th October 1975 the plaintiff obtained an order from this court striking out the defendant's statement of defence because of the defendant's failure to carry out an undertaking to provide information and documents given during the course of the examination for discovery of the defendant Poole and for other reasons. This enabled the plaintiff to enter his default judgment above referred to. In October 1976, after the plaintiff commenced the present action, the corporate defendant applied to Kirby J. for leave to reopen the judgment and file its statement of defence, but that application was dismissed.

11 The question before me, therefore, is whether the depletion of the company's assets by payments to the defendant Poole was in contravention of the Statute of Elizabeth, 1571, described in its title as an Act against Fraudulent Deeds, Gifts, Alienations, etc., and of the Fraudulent Preferences Act, R.S.A. 1970, c. 148.

12 Sections 1 and 2 of the Statute of Elizabeth are in force in Alberta: see *Goyan v. Kinash*, [1945] 1 W.W.R. 291, [1945] 2 D.L.R. 749 (Alta.), and *Bank of N.S. v. Zgurski* (1970), 14 C.B.R. (N.S.) 185, 72 W.W.R. 464 (Alta.).

13 The distinction between the two statutes is that the Statute of Elizabeth does not require the plaintiff to prove that the debtor was insolvent. He need only show that result of the impugned conveyance has the necessary consequence that there is nothing left for his creditors: *Bludoff v. Osachoff*, 22 Sask. L.R. 533, [1928] 2 W.W.R. 150 at 153, [1928] 3 D.L.R. 179 (C.A.), and cases therein cited:

> It is not necessary in such a case as this to show that the debtor was insolvent. By the transfers and bill of sale he deprived himself of all his property, with the necessary consequence that there was nothing left for his creditors. The inference to be drawn from that fact is that the transfers were fraudulent. *Kent v. Riley* (1872), L.R. 14 Eq. 190; *Smith v. Cherrill* (1867), L.R. 4 Eq. 390 at 395.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> In such a case it is not necessary to prove an intention to defeat, delay or defraud, as the conveyance is calculated to have that effect. Even if there were good consideration, the conveyance must be *bona fide* as well to take the transaction out of *Statute of Elizabeth*, 13 Eliz., ch. 5.

14 Another rule which applies to conveyances between close relatives which have the effect of defeating the claims of creditors is that the onus of establishing the validity of the transaction is upon the parties upholding it: *Koop v. Smith* (1915), 51 S.C.R. 554, 8 W.W.R. 1203, 25 D.L.R. 355.

15 The provisions of the Fraudulent Preferences Act of Alberta, however, are limited to insolvent persons and to preferences of particular creditors or classes of creditors. There must be an intent to give, and by the creditor to receive, a preference over other creditors and the court must be satisfied that such preference was the predominant intent of the debtor.

16 The problem arose more frequently in cases of conveyances between close relatives. The same principles apply, however, to conveyances between individuals and companies controlled by those individuals: *Re Martineau* (1969), 5 D.L.R. (3d) 165 (B.C.), and *Faulhaber v. Ulseth*, [1976] 4 W.W.R. 48, 66 D.L.R. (3d) 488 (Alta.).

17 In the latter case, my brother Steer held in dealing with the question of intent to delay, hinder or defraud creditors that the intent of the company and the intent of defendant, who was the president and controlling force of the company, were one and the same. He states [pp. 59-60]:

> The fact that the company gave consideration cannot save the transaction if the company had an actual intent to defraud, delay or hinder Faulhaber in recovering his judgment: *Reutcke v. Reutcke* (1958), 24 W.W.R. 417 at 422-23 (Man.); *Bank of N.S. v. Zgurski* [supra].

18 Under both statutes, I conclude that the payments to the defendant Poole must be set aside.

19 Under the English statute which is in force in this province, the intent to defraud the plaintiff must be presumed as the transaction divested the defendant company of all its assets thereby defeating the claim of the plaintiff. The circumstances surrounding the payments to the defendant Poole do not establish a bona fide claim by him and he has not satisfied the onus of proof upon him. Under the Fraudulent Preferences Act, I find that the defendant company was insolvent or on the eve of insolvency, and by stripping itself of its assets it defeated the plaintiff's claim. Because of the close relationship between the company and its major shareholder, I find there was a common intent between them.

20 For the foregoing reasons there will be a judgment in favour of the plaintiff in the amount of $10,000 plus costs to be taxed on col. 4(c), (r), limiting rules not to apply.

Application granted.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 29

1992 CarswellAlta 293
Alberta Court of Queen's Bench

Alberta (Director of Employment Standards) v. Sanche

1992 CarswellAlta 293, [1992] A.W.L.D. 807, [1992] A.J. No. 910, 134 A.R. 149, 15 C.B.R. (3d) 58, 5 Alta. L.R. (3d) 243

Re Rules 442 through 453 of Alberta Rules of Court; DIRECTOR OF EMPLOYMENT STANDARDS v. HENRY A. SANCHE and PRICE WATERHOUSE LTD. (Trustee for Estate of ROBERT ALLEN EVANS, Bankrupt)

Andrekson J.

Judgment: October 9, 1992
Docket: Doc. Edmonton 9103 12331

Counsel: *B.A. Carr*, for respondent, Henry A. Sanche.
R.T. O'Neill, for respondent, Price Waterhouse Ltd.

Subject: Corporate and Commercial; Insolvency; Civil Practice and Procedure; Contracts; Torts

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy --- Assignments in bankruptcy

Bankruptcy --- Avoidance of transactions prior to bankruptcy — Fraudulent preferences — Insolvency of debtor at time of transaction

Bankruptcy --- Avoidance of transactions prior to bankruptcy — Fraudulent preferences — Time within which avoidable — General

Bankruptcy --- Avoidance of transactions prior to bankruptcy — Fraudulent preferences — View to prefer — General

Bankruptcy --- Practice and procedure in Courts — Discovery and examinations — Evidentiary issues — General

Fraud and Misrepresentation --- Fraudulent preferences — Preferences not attacked within 60 days — Proof of intent — General

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Fraudulent preferences — Practice — Act requiring action to set aside transaction as fraudulent preference to be brought within one year — Fraudulent Preferences Act, R.S.A. 1980, c. F-18.

Fraudulent preferences — Rebuttal of statutory presumption — Section 95(1) of Bankruptcy Act requiring that assignment be made within three months of debtor's bankruptcy to be fraudulent preference — Bankruptcy Act, R.S.C. 1985, c. B-3.

Fraudulent preferences — Proof of insolvency — Burden of proof — Trustee not proving bankrupt was insolvent when assignment made — No presumption assignment made with intent to prefer one creditor over others.

E gave a creditor a written assignment of up to $40,000 out of moneys owing or accruing to him by his employer, T. T was ordered by an officer of the Alberta Employment Standards Branch to pay to the Director of the branch $12,990.73 due to E for vacation pay. By a court order, $12,690.78 was paid into court by the Director. E then made an assignment in bankruptcy. The trustee in bankruptcy brought a motion claiming entitlement to the funds. The motion was dismissed when the trustee failed to attack the assignment successfully: there was no need to show consideration since the assignment was made under seal, the vacation pay was other compensation for labour or personal services under the *Personal Property Security Act* (Alta.) ("PPSA") and the PPSA did not apply, the assignment was not a settlement within s. 91(1) of the *Bankruptcy Act*, and the trustee could not prove a fraudulent preference since the evidence did not show that E's predominant intention was to give the creditor a preference over other creditors and that the creditor intended to receive a preference when he took the assignment. The trustee appealed.

Held:

The appeal was dismissed.

The action to set aside the assignment was commenced beyond the limitation in s. 3 of the *Fraudulent Preferences Act* (Alta.).

In order for the assignment to be a fraudulent preference, it had to have been made within three months of the debtor's bankruptcy. Here, the assignment was made beyond the three-month period established in s. 95(1) of the *Bankruptcy Act*.

The trustee did not prove, on a balance of probabilities, that E was insolvent when he made the assignment and therefore it could not be presumed that the assignment was made with a view to giving S a preference over other creditors.

Table of Authorities

Cases considered:

Barnett, Re (1983), 46 C.B.R. (N.S.) 211, 43 A.R. 215 (Q.B.) — *applied*

Burton v. R & M Insurance Ltd. (1977), 26 C.B.R. (N.S.) 49, 5 Alta. L.R. (2d) 14, 81 D.L.R. (3d) 455, 9 A.R. 589 (T.D.) — *applied*

Robinson v. Countrywide Factors Ltd., [1978] 1 S.C.R. 753, 23 C.B.R. (N.S.) 97, [1977] 2 W.W.R. 111, (sub nom. *Kozan Furniture (Yorkton) Ltd. v. Countrywide Factors Ltd.)* 14 N.R. 91, 72 D.L.R. (3d) 500 — *considered*

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Statutes considered:

Bankruptcy Act, R.S.C. 1985, c. B-3 —

s. 95

s. 95(1)

s. 95(2)

Fraudulent Preferences Act, R.S.A. 1980, c. F-18 —

s. 1

s. 1(a)

s. 2

s. 2(a)

s. 2(b)

s. 3

s. 4

Rules considered:

Alberta Rules of Court —

R. 5(a)

R. 442-453

Appeal from judgment reported at (1992), 12 C.B.R. (3d) 17, 2 Alta. L.R. (3d) 14, 3 P.P.S.A.C. (2d) 1, (sub nom. Re Evans (Bankrupt)) 128 A.R. 23 (Master) dismissing motion by trustee for entitlement to bankrupt's funds.

***Andrekson J.*:**

1 This appeal from the master involves a dispute as to priority to funds paid into court between Price Waterhouse ("the trustee") as trustee of the bankrupt Robert A. Evans ("Evans") and Henry A. Sanche ("Sanche"), a creditor of Evans. The relevant facts are as follows.

2 Sanche lent $15,000 on June 7, 1988 and a further sum of $15,000 on October 28, 1988 to Evans.

3 On June 8, 1990, Evans executed and delivered a written assignment of funds up to $40,000 in favour of Sanche out of

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

the first available funds and moneys owing or accruing due to Evans from Terra Mines Ltd. ("Terra"), which assignment was served on Terra on June 15, 1990.

4 On October 10, 1990, Terra was ordered to pay $12,990.73 due to Evans for vacation pay.

5 On February 8, 1991, Evans made an assignment in bankruptcy.

6 On June 20, 1991, an originating notice was filed by the Director of Employment Standards for an order to pay the funds into court.

7 On August 22, 1991, the applicant, Director of Employment Standards, paid into court the sum of $12,690.78.

8 By notice of motion dated December 30, 1991, pursuant to the *Alberta Rules of Court* relating to Interpleader Rules 442 to 453 inclusive, this matter came before the master in chambers on February 4, 1992 [reported at 12 C.B.R. (3d) 17, 2 Alta. L.R. (3d) 14, 3 P.P.S.A.C. (2d) 1, (sub nom. *Re Evans (Bankrupt))* 128 A.R. 23].

9 Sanche claims priority to the funds by reason of the assignment made by Evans in his favour (directed to Terra) eight months prior to the bankruptcy of Evans. The learned master concluded that the trustee failed to successfully attack the assignment in issue and also held that Sanche was entitled to his taxable costs on the application.

10 The trustee contends that the assignment of funds given by Evans to Sanche was a fraudulent preference. The trustee relies on ss. 1, 2 and 3 of the *Fraudulent Preferences Act*, R.S.A. 1980, c. F-18 and s. 95 of the *Bankruptcy Act*, R.S.C. 1985, c. B-3.

11 For reasons which will follow, this appeal is dismissed.

12 Sections 1 and 2 of the *Fraudulent Preferences Act*, supra, state:

> 1 Subject to sections 6 to 9, every gift, conveyance, assignment, transfer, delivery over or payment of goods, chattels or effects or of bills, bonds, notes or securities or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made
>
> (*a*) by a person at a time when he is in insolvent circumstances or is unable to pay his debts in full or knows that he is on the eve of insolvency, and
>
> (*b*) with intent to defeat, hinder, delay or prejudice his creditors or any one or more of them,
>
> is void as against any creditor or creditors injured, delayed or prejudiced.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

2 Subject to sections 6 to 9, every gift, conveyance, assignment, transfer, delivery over or payment of goods, chattels or effects or of bills, bonds, notes or securities or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made

(*a*) by a person at a time when he is in insolvent circumstances or is unable to pay his debts in full or knows that he is on the eve of insolvency, and

(*b*) to or for a creditor with intent to give that creditor preference over the other creditors of the debtor or over any one or more of them,

is void as against the creditor or creditors injured, delayed, prejudiced or postponed.

13 Initially, the trustee must prove on a balance of probabilities that Evans was in insolvent circumstances, or was unable to pay his debts in full or knew that he was on the eve of insolvency at the time when the assignment was made. In *Robinson v. Countrywide Factors Ltd.*, [1978] 1 S.C.R. 753, 23 C.B.R. (N.S.) 97, [1977] 2 W.W.R. 111, (sub nom. *Kozan Furniture (Yorkton) Ltd. v. Countrywide Factors Ltd.)* 14 N.R. 91, 72 D.L.R. (3d) 500, "insolvent circumstances" is described as the inability to pay debts in the ordinary course as they become due. The evidence tendered by the trustee to prove insolvency is found in Exhibit E of the affidavit of C. Pears, which consists of an examination of Evans by the official receiver. The following question and answer was given in the examination:

Q. To the best of your recollection when did you first become aware that you were unable to pay your debts?

A. Two or three years prior to Bankruptcy.

14 Even if it is inferred that Evans was insolvent at the time he gave Sanche the assignment, the trustee must prove that Evans' intention as a debtor at that time was to defeat, hinder, delay, or prejudice his creditors or any one of them. The evidence, in my view, does not disclose that the trustee has proved that Evans' intention was to defeat, hinder, delay or prejudice his creditors or any one of them at that time. The appeal fails under s. 1 of the Act.

15 Pursuant to s. 2(*a*), the requirement to prove insolvency is the same as in s. 1(*a*). Assuming that Evans was insolvent at the time he gave the assignment to Sanche, under s. 2(*b*) the trustee must prove that Evans' intention as a debtor was to give a preference to Sanche the creditor, and by the creditor Sanche to receive a preference over other creditors.

16 In *Burton v. R & M Insurance Ltd.* (1977), 26 C.B.R. (N.S.) 49, 5 Alta. L.R. (2d) 14, 81 D.L.R. (3d) 455, 9 A.R. 589 (T.D.), the court held at p. 18 [Alta. L.R.] that:

The provisions of The Fraudulent Preferences Act of Alberta, however, are limited to insolvent persons and to preferences of particular creditors or classes of creditors. There must be an intent to give, and by the creditor to receive, a preference over other creditors and the court must be satisfied that such preference was the predominant intent of the debtor.

17 In *Re Barnett* (1983), 46 C.B.R. (N.S.) 211, 43 A.R. 215 (Q.B.), the court held [at p. 219 A.R.] that:

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> There must be an intent to give and by the creditor to receive, a preference over other creditors and the Court must be satisfied that such preference was the predominant intent of the debtor.

18 The evidence must, on a balance of probabilities, show that such preference was the predominant intent of the debtor. The evidence that Evans was aware, at the time of bankruptcy, that two or three years prior he was unable to pay his debtors does not, in my view, support a finding that Evans' predominant intention in giving Sanche the assignment was to give Sanche a preference over other creditors. In my view, the trustee has failed to prove, on a balance of probabilities, that Sanche intended to receive a preference when he received the assignment. The examination of Sanche at pp. 17, 23 and 24 indicates that Sanche had no knowledge of debts owed by Evans to others. The evidence that the trustee relied on is found on p. 22, paras. 11 to 19 and, as stated by the master, was merely the legitimate and natural response of any creditor. I agree with the master's characterization. It shows only that Sanche was concerned in getting repaid but it does not, in my view, prove that he was aware of other creditors or that he intended to receive a preference before other creditors could get involved. Since Sanche was unaware of the existence of other creditors, he could not, in my view, have had an intent to receive a preference over them. The trustee's appeal fails under s. 2 of the Act.

19 Sections 3 and 4 of the *Fraudulent Preferences Act* state:

> 3 Subject to sections 6 to 9, every gift, conveyance, assignment, transfer, delivery over or payment of goods, chattels or effects or of bills, bonds, notes or securities or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made
>
> > (*a*) by a person at a time when he is in insolvent circumstances or is unable to pay his debts in full or knows that he is on the eve of insolvency, and
> >
> > (*b*) to or for a creditor and having the effect of giving that creditor a preference over the other creditors of the debtor or over any one or more of them,
>
> is, in and with respect to any action that within one year thereafter is brought to impeach or set aside the transaction, void as against the creditor or creditors injured, delayed, prejudiced or postponed.
>
> 4(1) A transaction shall be deemed to be one that has the effect of giving a creditor a preference over other creditors, within the meaning of section 3, if by the transaction a creditor is given or realizes or is placed in a position to realize payment, satisfaction or security for the debtor's indebtedness to him or a portion of it greater proportionately than could be realized by or for the unsecured creditors generally of the debtor or for the unsecured portion of his liabilities out of the assets of the debtor left available and subject to judgment, execution, attachment or other process.
>
> (2) Independently of the intent with which the transaction was entered into or of whether it was entered into voluntarily or under pressure, the preferential effect or result of the impeached transaction governs, and no pressure by a creditor or want of notice to the creditor alleged to have been so preferred of the debtor's circumstances, inability or knowledge as aforesaid, or of the effect of the transaction, avails to protect the transaction except as provided by sections 6 and 9.

20 There are three requirements of s. 3 which must be proved in order to set aside a transaction as a fraudulent preference:

> (a) insolvent circumstances of the debtor;
>
> (b) the granting, in the circumstances of this case, of the assignment which is deemed to have the effect of giving the creditor a preference; and

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(c) that an action was brought within one year to impeach or set aside the transaction.

21 Insolvent circumstances have been discussed supra.

22 The granting to Sanche of the assignment, in the circumstances, would clearly be deemed as giving him as a creditor a preference over other creditors.

23 Was the action brought within one year to set aside the transaction?

24 Section 3 clearly states that the action must be brought within one year from the granting of the assignment, which in this case was June 8, 1990. Section 5(*a*) of the Rules of Court states an action "includes any issue directed to be tried". *Black's Law Dictionary* states that an "action" is a proceeding by which one party seeks the enforcement or protection of a right in a court of justice.

25 By originating notice filed by the Director of Employment Standards on June 20, 1991, the Director sought an order permitting the applicant to pay into court $12,690.78 or dispose of it as the court directs. In my view, an originating notice falls within the definition of the words "any action", but that originating notice is not an action "to impeach or set aside the transaction", nor is it an action by which one party seeks to enforce some right or restrain the commission of some wrong by another party. In my view, it was not until December 30, 1991 that there was an action to impeach or set aside the transaction when the trustee caused to be issued a notice of motion, as hereinbefore stated, to have the moneys that were paid into court to be paid out to the trustee. It is my view that an action to impeach or set aside the transaction was originated on December 30, 1991 by notice of motion, which date is beyond the one-year time limitation in s. 3 of the Act.

26 It is my view that the trustee has failed to satisfy the elements of s. 3 of the *Fraudulent Preferences Act*.

27 Section 95 of the *Bankruptcy Act*, supra, states:

> 95.(1) Every conveyance or transfer of property or charge thereon made, every payment made, every obligation incurred and every judicial proceeding taken or suffered by any insolvent person in favour of any creditor or of any person in trust for any creditor with a view to giving that creditor a preference over the other creditors shall, if the person making, incurring, taking, paying or suffering it becomes bankrupt within three months after the date of making, incurring, taking, paying or suffering it, be deemed fraudulent and void as against the trustee in the bankruptcy.
>
> (2) Where any conveyance, transfer, charge, payment, obligation or judicial proceeding mentioned in subsection (1) has the effect of giving any creditor a preference over other creditors, or over any one or more of them, it shall be presumed, in the absence of evidence to the contrary, to have been made, incurred, taken, paid or suffered with a view to giving the creditor a preference over other creditors, whether or not it was made voluntarily or under pressure and evidence of pressure shall not be admissible to support the transaction.

28 The jurisprudence has established three elements that must be proven on a balance of probabilities to establish a

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

fraudulent preference under s. 95(1) of the *Bankruptcy Act*.

29 They are that:

(a) the effect of the transaction is to give the creditor a preference over other creditors;

(b) the debtor was insolvent; and

(c) the transaction took place within three months of the bankruptcy.

30 The transaction that gives Sanche the "preference" over other creditors is the assignment given to him on June 8, 1990. That is the time when Evans executed and delivered to Sanche the legally enforceable assignment of funds which authorized Terra to pay funds to Sanche. That is the transaction that the trustee is now contesting. The assignment was granted on June 8, 1990, which date precedes the December 30, 1991 date by approximately 18 months, far exceeding the three-months limit in the statute. It follows that the assignment is not deemed to be fraudulent and void by operation of s. 95(1), supra.

31 The trustee has not, in my view, provided sufficient evidence that Evans was an insolvent person on the date that he executed and delivered the assignment to Sanche.

32 Assuming that an "assignment" is a transfer of property within the meaning of s. 95(1) and (2) of the Act, I am satisfied that the trustee has not proven, on a balance of probabilities, that Evans was an insolvent person at the time he gave the assignment to Sanche and therefore it cannot be presumed, pursuant to s. 95(2), that the assignment was made with a view to giving Sanche a preference over other creditors.

33 The trustee's appeal pursuant to the *Bankruptcy Act* is dismissed.

34 The costs of the application shall be paid by the trustee in bankruptcy.

Appeal dismissed.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 30

1996 CarswellAlta 727
Alberta Court of Queen's Bench

Dwyer v. Fox

1996 CarswellAlta 727, [1996] A.W.L.D. 908, [1996] A.J. No. 769, 190 A.R. 114, 43 Alta. L.R. (3d) 63

Patrick Dwyer (Plaintiff) and Eugene Fox, 286618 Alberta Ltd. and 303554 Alberta Ltd. (Defendants)

Phillips J.

Judgment: September 3, 1996
Docket: Lethbridge/MacLeod 9406-01315

Counsel: *F.A. Mason*, for plaintiff.
J.S. Peacock, for defendant 303554 Alberta Ltd.

Subject: Contracts; Corporate and Commercial; Torts

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Fraud and misrepresentation --- Fraudulent conveyances — Fraudulent intent — "Badges of fraud"

Fraud and misrepresentation — Fraudulent conveyances — Fraudulent intent — "Badges of fraud" — Company selling off assets in four separate transactions — Sale proceeds paid directly to bank to reduce indebtedness but portion of debt remaining owing — Guarantor of debt claiming sales at less than market value and intent to defraud creditors — Evidence failing to establish sales at less than fair value or intent to defraud creditors — Fraudulent Conveyances Act, 1571 (U.K.), 13 Eliz. 1, c. 5.

The plaintiff sold half of his shares in a numbered company to the defendant F., and together and through the numbered company they worked on a number of construction contracts. Not long into the relationship, personal relations between the plaintiff and F. arose, and the plaintiff sold his remaining shares in the numbered company to F. F. soon found, for either personal or business reasons, that he could no longer operate the numbered company and so, over the next six months, he sold certain pieces of heavy equipment, in a series of four separate transactions, to S. and his company. Prior to purchasing the equipment, S. consulted with the bank which held security in the equipment for sale. The bank agreed to each of the transactions, provided it received the proceeds directly for the payment of the numbered company's creditors. In one of the transactions, the bank was advised that a portion of the purchase price was to be paid by the provision of services from S.'s company. The bank was satisfied by the proceeds of the several sales and released its security in the equipment sold. The plaintiff sued F., S. and S.'s company under the *Fraudulent Conveyances Act*,

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

claiming that the sales were fraudulent conveyances under the statute and that the company received the benefit of the fraudulent conveyance by obtaining the equipment at a price significantly below market value. The plaintiff claimed that, as a result, he was not able to fully satisfy his obligations as guarantor of the debts made by F. to his creditors.

Held:

Action dismissed.

In order to establish a fraudulent conveyance under the statute, the plaintiff was obliged to prove that the numbered company had the intent to delay, hinder or defraud creditors, that the numbered company retained an improper benefit from the conveyances and that the purchaser company had a fraudulent intent. There was no direct evidence to suggest fraudulent intent on the part of F. Moreover, the circumstances surrounding the transactions did not amount to "badges of fraud." The evidence failed to establish that the consideration was inadequate, that the conveyances were accomplished quickly, that the parties to the sale were related in a business sense or that the conveyances were of such a general nature that they disposed of virtually all of the numbered company's assets. Nor was there any evidence to suggest that the numbered company did not receive the services which amounted to partial payment of the third transaction, or that the value ascribed to the services was more than the services were worth. Even if S. had known that F.'s ultimate plan was to ensure that the plaintiff would be left solely responsible as a guarantor for his loan obligations, that in itself would have been inconclusive. In order to succeed, the plaintiff was obliged to show that S. actively participated in the fraud to achieve a benefit for F. and himself. The evidence did not support that kind of activity and, in any event, it could not be said that the numbered company retained any improper benefits, given that all of the proceeds from the transactions were directed to F. and the numbered company's creditors to reduce their indebtedness. Likewise, there was no evidence to suggest that, by the fact that the service work was performed, the numbered company and F. somehow retained an improper benefit, given that the indebtedness continued to decline even as the service work was provided.

Table of Authorities

Cases considered:

Alberta (Attorney General) v. Samuel Doz Professional Corp., 9 Alta. L.R. (3d) 201, 31 R.P.R. (2d) 161, [1993] 6 W.W.R. 260, 139 A.R. 198 (Q.B.) — *applied*

Barnett, Re (1983), 46 C.B.R. (N.S.) 211, 43 A.R. 215 (Q.B.) — *considered*

Canadian Imperial Bank of Commerce v. Grande Cache Motor Inn Ltd. (1977), 4 Alta. L.R. (2d) 319, (sub nom. *Hobbema Farms Ltd. v. Fowlis)* 25 C.B.R. (N.S.) 207, (sub nom. *Hobbema Farms Ltd. v. Grande Cache Motor Inn Ltd.)* 9 A.R. 208 (T.D.) — *applied*

Lambert v. Quinn (1994), 50 M.V.R. (2d) 90, 110 D.L.R. (4th) 284, 68 O.A.C. 352 (C.A.) — *referred to*

Mackow v. Sood (1993), 18 C.P.C. (3d) 371, 141 A.R. 233, 46 W.A.C. 233 (C.A.) — *referred to*

Mulcahy v. Archibald (1898), 28 S.C.R. 523 — *applied*

Nicholson v. Milne (1989), 67 Alta. L.R. (2d) 130, 96 A.R. 114, 74 C.B.R. (N.S.) 263 (Q.B.) — *considered*

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Schlumpf v. Corey, 25 C.B.R. (3d) 297, 19 Alta. L.R. (3d) 385, [1994] 7 W.W.R. 570, 153 A.R. 272 (Master) — *considered*

Sun Sudan Oil Co. v. Methanex Corp. (1992), 5 Alta. L.R. (3d) 292, [1993] 2 W.W.R. 154, 134 A.R. 1 (Q.B.) — *applied*

Statutes considered:

Fraudulent Conveyances Act, 1571 (U.K.), 13 Eliz. 1, c. 5 — *considered*

Fraudulent Preferences Act, R.S.A. 1980, c. F-18

s. 1*referred to*

s. 2*referred to*

s. 3*referred to*

Action by plaintiff claiming fraudulent conveyance.

***Madam Justice C.S. Phillips*:**

1 In March of 1991 the Plaintiff, Patrick Dwyer, sold shares in his heavy equipment construction company, 286618 Alberta Ltd. (also known as Pat Dwyer Construction) to the Defendant, Eugene Fox. As a result of that sale, Mr. Fox acquired a 50 percent interest in 286618 Alberta. Together and through this company, Mr. Dwyer and Mr. Fox worked on a number of construction contracts to build irrigation canals on the Blood Reserve at Standoff, Alberta. Unfortunately, it was not long after in late 1992 that this relationship between Mr. Dwyer and Mr. Fox began to deteriorate rapidly. Mr. Fox was drinking heavily and there was a mutual distrust between the two. In the spring of 1993 Mr. Dwyer decided the partnership was over and so he sold his remaining shares in 286618 Alberta to Mr. Fox effective May 19, 1993. But Mr. Fox soon found either for personal or business reasons that he could no longer operate 286618 Alberta. So over the late fall of 1993 and spring of 1994, Mr. Fox and 286618 Alberta sold certain pieces of heavy equipment to Mr. Brian Seaman and his company, 303554 Alberta Ltd. (also known as Brians Excavating).

2 The Plaintiff, Mr. Dwyer, claims that this sale or disposition of heavy equipment to 303554 Alberta was a fraudulent conveyance caught by the provisions of the *Statute of Elizabeth*. Mr. Dwyer takes the position that the Defendant, 303554 Alberta, has received the benefit of this fraudulent conveyance by obtaining the equipment at a price significantly below market value. In the result, Mr. Dwyer finds himself in the position of not being able to fully satisfy his obligations as a guarantor of debts made by the Defendant Mr. Fox to his creditors, the Royal Bank of Canada and Treaty Seven Business Development Centre.

3 The Defendant, 303554 Alberta, denies both the allegations of a fraudulent conveyance and that the equipment was purchased significantly below market value. 303554 Alberta submits that the equipment, which was purchased, was bought for fair, adequate, and reasonable consideration under the circumstances. As far as 303554 Alberta is concerned the transaction of purchase and sale or disposition of this equipment was *bona fide* and done at arm's length; in no way was it done with the intent to defeat, hinder, delay or prejudice anyone, and in particular creditors of 286618 Alberta or Mr. Fox. In

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

fact, 303554 Alberta argues any monies that were paid by it for the purchase of this equipment were paid over to Mr. Fox's and 286618 Alberta's creditors to reduce their indebtedness. None of these proceeds ever went to Mr. Fox and 286618 Alberta. Therefore, it is submitted that the Plaintiff, Mr. Dwyer, is not entitled to any relief whatsoever and this claim should be dismissed.

4 At trial, I gave oral judgment and agreed with the Defendants that Mr. Dwyer's claim should be dismissed. I indicated that I would issue written reasons for my decision to dismiss this claim.

5 At the conclusion of the trial, it became evident that the issue to be decided upon was whether the disposition of the equipment to the Defendant, 303554 Alberta by the Defendants, Mr. Fox and 286618 Alberta constituted a fraudulent conveyance within the ambit of the *Statute of Elizabeth* [*Fraudulent Conveyances Act*], 1571 (U.K.), 13 Eliz. 1, c. 5

I Background

6 The narrative to follow includes the various documents that were filed as exhibits during the course of the trial, as well as my findings of fact derived from the *viva voce* evidence at trial.

7 Commencing March of 1993, Mr. Dwyer proceeded to divest himself of all of his interest in 286618 Alberta. As alluded to earlier, Mr. Dwyer and the other shareholder of 286618 Alberta, Mr. Fox, were not getting along. Initially, in 1991 the Federal Government through the then Department of Industry and Science and Technology had provided $75,000 by way of a grant to Mr. Fox, which he used as a deposit for the purchase of his 50 percent interest in 286618 Alberta. When difficulties arose between Mr. Dwyer and Mr. Fox, Mr. Dwyer recommended that Mr. Fox contact representatives of the Department of Industry and Science and Technology for their assistance in resolving these difficulties. A Mr. Rolfe was sent in by the Department and he conducted a thorough investigation of 286618 Alberta's corporate and banking records and vendors' lists. Indeed, Mr. Dwyer had a two hour discussion with Mr. Rolfe. As a result Mr. Dwyer concluded he was at serious financial risk if he continued this partnership with Mr. Fox. Therefore, by agreement dated May 19, 1993 marked as Exhibit 3, Mr. Dwyer sold all of his shares to Mr. Fox for one dollar. As further consideration for the sale of his shares to Mr. Fox, Mr. Dwyer also received those assets referred to in Schedule C of the May 19, 1993 agreement (which were valued at $32,900) together with "all other small pieces" and "whatever is not listed in this report". Mr. Dwyer acknowledged that at no time did he pay 286618 Alberta $32,900 for these Schedule C assets.

8 At May 19, 1993 Mr. Dwyer claims 286618 Alberta owned either under Lease Purchase Contract or under Conditional Sales Contract the equipment set out in Schedule "A" to this judgment. Mr. Seaman admits this except with respect to items (i) and (j) of Schedule "A" for which Mr. Seaman has no knowledge. Mr. Dwyer gave evidence about the condition of all of this equipment as of May 1993. Three other individuals, who had earlier worked for 286618 Alberta, also gave evidence on behalf of the Plaintiff, Mr. Dwyer. These employees were Mr. Dennis, Mr. Dziedzic and Mr. Thompson. They testified as to the condition of certain pieces of equipment subsequent to May 1993 while they were in the employ of 286618 Alberta (then known as Fox Construction). It is clear from their evidence that no matter what the quality the equipment was at May 1993, the quality of that equipment had definitely deteriorated during the course of these individuals employment with Fox Construction. Certainly, the equipment was not maintained to the same extent Mr. Dwyer suggested when he was operating 286618 Alberta prior to May of 1993. Furthermore, these employees testified to certain problems they had with Mr. Fox and his lack of presence on the job site after May 1993. Mr. Fox was drinking both on and off the job sites and was definitely not attending to the business of 286618 Alberta. Over the period of March 1993 to the fall of 1993, Mr. Fox was also experiencing criminal difficulties with the law, especially as a result of his drinking and driving. Mr. Fox spent some time in jail in the fall of 1993 as a result of those difficulties.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

9 Faced with all of this, Mr. Fox decided to dispose of certain pieces of construction equipment. He did this himself or through his representative, Mr. Brown over a period of several months from November of 1993 to May of 1994. Although Mr. Dwyer disputes this, I am satisfied from the evidence there were four separate transactions between Mr. Fox and Mr. Seaman's company with respect to this equipment. The first transaction concerned the sale by way of Bill of Sale dated November 29, 1993 (marked Exhibit 25) from 286618 Alberta to 303554 Alberta of the 1990 Kobelco Model K9121C Mark YC000594 and the 1983 Komatsu Model D60E Crawler 0003 40678 for $57,800. Originally this equipment had been financed by 286618 Alberta through GE Capital Financing Canada Equipment by way of a loan. In November of 1993 286618 Alberta was in default of that loan and GE Capital advised it of this by way of a demand letter dated November 16, 1993. GE Capital copied Pat Dwyer, as a guarantor of that loan, with this demand letter as noted by the cc: "Pat Dwyer P.O. Box 38, Lundbreck, Alta. T0K 1H0 Re: Personal Guarantee". The payout amount for the loan as of November 15, 1993 was $57,550.37 with a per diem rate of interest until paid. Shortly after the issuance of this demand letter, Mr. Brown, on behalf of Mr. Fox, had discussions with Mr. Seaman concerning the disposition of the Kobelco and the Komatsu. They agreed Mr. Seaman's company would purchase these items for a sum sufficient to retire the loan amount with GE Capital. This amount as at November 29, 1993 was the $57,800 shown on the Bill of Sale. A Ms. Sonia G. Tibbatts, Account Manager at the Royal Bank of Canada was advised of this. She agreed on behalf of the Royal Bank by way of letter dated November 26, 1993 (marked as Exhibit 13) that the Royal Bank would release its interest in the Kobelco and the Komatsu "upon proof G.E. Capital Corporation has been paid in full for their contract(s) covering the above-noted equipment and that no surplus funds were paid." Ms. Tibbatts received that confirmation once the sale was concluded and so the Royal Bank released its interest in these items.

10 The second transaction involved the sale of the UH 07 Hitachi Excavator (parts only - not in running condition), the 1980 Willock Low Bed Serial No. 80 WRL 068 (used), and the 5th Wheel End Dump Trailer (Rock Boy - Homemade, as is). As in the case of the first transaction, both Mr. Fox and Mr. Seaman retained their previous legal counsel to act on their behalf. Once the first transaction was completed, Mr. King (who acted on behalf of Mr. Seaman and 303554 Alberta) wrote to Mr. Pollock (who acted on behalf of Mr. Fox and 286618 Alberta) on December 8, 1993. Mr. King advised they were now to deal with the purchase of the Hitachi Excavator parts, the used 1980 Willock Low Bed and the End Dump Trailer (home made). Their respective clients had agreed 303554 Alberta would pay $15,000 immediately to 286618 Alberta for this equipment and 303554 Alberta would provide $30,000 worth of hourly work, which was to include equipment and operator to be charged at the normal hourly rate by the Purchaser. On that same date of December 8, 1993 Mr. King wrote Mr. Pollock again and enclosed a $15,000 trust cheque for these items on certain express trust conditions. One of the trust conditions was the vendor, 286618 Alberta, was to provide a signed Bill of Sale for the equipment stating the consideration as $15,000 and $30,000 worth of hourly work to 286618 Alberta or its designate. Mr. Pollock faxed a draft form Bill of Sale for these three pieces of equipment to Mr. King on December 15, 1993 for his review. Notwithstanding the Bill of Sale and service agreement had not been finalized and executed, Mr. King amended his trust conditions around December 15, 1993 so that Mr. Pollock could release $10,000 of the $15,000 to GE Capital. This was done to avoid the equipment being seized by GE Capital as a result of 286618 Alberta being in default of its lease payments. Mr. Seaman made Ms. Tibbatts of the Royal Bank aware of this second transaction around December 14, 1993 as he had in the case of the first transaction. Mr. Dwyer takes issue with Mr. Seaman as to what he actually told Ms. Tibbatts about the details of the second transaction; specifically those details relating to the $30,000 worth of work.

11 On December 14, 1993 Ms. Tibbatts wrote Mr. Pollock. She advised Mr. Pollock that it was the Royal Bank's understanding this second transaction generated approximately $15,000. The Bank was in agreement that Mr. Pollock use $10,000 of the $15,000 to pay GE Capital for the November, December 1993 and January 1994 lease payments. The residual $5,000 was to be paid to the Bank for payment of Mr. Fox's loans with the Royal Bank and at the Treaty Seven Development Centre office. On December 16, 1993 Ms. Tibbatts received a letter from Mr. Pollock enclosing a trust cheque for $5,000 to be applied against Mr. Fox's loans and confirming the $10,000 had been paid to GE Capital. The Royal Bank then released its security on the 1980 Willock Low Bed, the Hitachi Excavator parts, and the End Dump Trailer. At no time with respect to any of the transactions did the Royal Bank conduct an appraisal of the equipment being sold to 303554 Alberta.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

12 On January 5, 1994, Mr. King provided Mr. Pollock with a draft service agreement for his review and advised that the Bill of Sale, which Mr. Pollock had provided, should be amended. Mr. King suggested that the consideration "ought to be identified as $45,000, $15,000 cash, and $30,000 for services to be provided." Mr. King testified that he never did receive a revised Bill of Sale nor was a Bill of Sale ever executed with respect to this second transaction. As well, the service agreement was never finalized and executed. By February of 1994, 303554 Alberta had completed its $30,000 worth of work for 286618 Alberta or its designate. Therefore, Mr. Pollock wrote Mr. King on February 17, 1994 and indicated that he had reviewed the matter with his client and "it appears this whole contract may be redundant as the work contemplated has now been finished."

13 The third transaction relates to those items purchased under a Bill of Sale incorrectly dated April 20, 1993; it should have been dated April 20, 1994. Mr. Dwyer disputes that this transaction occurred in April of 1994, arguing that the equipment set out in the April 1993 Bill of Sale was in fact sold to Brian Seaman for the benefit of 303554 Alberta at the time of the second transaction. My review of the evidence does not support this. In the spring of 1994 Mr. Seaman had ongoing discussions with Mr. Fox concerning the purchase of additional equipment. Mr. Seaman testified he and Mr. Fox argued back and forth about the price of these items. Mr. Fox wanted a better price than Mr. Seaman was willing to pay for this additional equipment. Mr. Seaman was only willing to pay $19,500 for this equipment and finally the parties settled on that amount. Mr. Seaman specifically noted on the Bill of sale: "As is Where is - Purchaser responsible for pick-up as machinery in very terrible condition. All proceeds to go to Royal Bank and Treaty 7 as agreed to by Sonya Tibbits and to be distributed between both Banks as agreed." Mr. Seaman kept a note of the values of the equipment he discussed with Mr. Fox in his diary dated Thursday, February 24, 1994. Mr. Fox also offered to sell Mr. Seaman other equipment such as: a sand unit, a holiday trailer, a bobcat trailer, a water tank, a newer white construction type trailer with tarps, heavy equipment and mechanics tools, a fuel truck, three half-tons, a water pump, a welder and another half-ton with a welder, a service truck and a white Dodge service truck. Mr. Seaman chose not to buy those items in April of 1994 because he didn't want them.

14 Mr. Seaman spoke with Ms. Tibbatts in the spring of 1994 concerning this third transaction. Ms. Tibbatts testified that, although she could not recall the exact date, Mr. Seaman had called around that time to advise her that he was looking at purchasing some additional assets. Mr. Seaman advised her he was only prepared to buy so many assets for $19,500 and he read her the list of those assets. Ms. Tibbatts could not remember if Mr. Seaman had mentioned a price of $19,500. She did however indicate to him that he could buy whatever assets he wanted from 286618 Alberta so long as the sale proceeds were paid to the Royal Bank. Sometime during the period of June to August of 1994, Ms. Tibbatts contacted Mr. Seaman and asked him to send a copy of the Bill of Sale for this third transaction. Mr. Seaman faxed Ms. Tibbatts the Bill of Sale after she had requested it.

15 Mrs. Seaman wrote a cheque dated April 7, 1994 to the Royal Bank and 286618 Alberta Ltd. (Fox) for the purchase of the additional equipment described in the third Bill of Sale. The Royal Bank cashed the cheque on or about May 9, 1994. Again, the Royal Bank did not conduct an appraisal on the equipment purchased from 286618 Alberta. Also, the Royal Bank applied all of the $19,500 to Mr. Fox's Royal Bank and Treaty Seven loans proportionately; thereby reducing the indebtedness to the Royal Bank from $83,000 in September of 1993 to $55,000 in April of 1994. Ultimately, the Royal Bank released its security interest on the equipment set out in the April 1994 Bill of Sale when it satisfied itself it had received the $19,500 and an executed Bill of Sale.

16 The fourth and final transaction involves the assumption of a lease by 303554 Alberta from 286618 Alberta with respect to a 1990 Hitachi Hydraulic Excavator Model EX220. Mr. Seaman had agreed with GE Capital on May 26, 1994 that 303554 Alberta would assume the obligations of 286618 Alberta under a lease it had entered into originally with National Bank Leasing Inc. on February 14, 1992 in respect of the EX220 Hitachi Excavator. GE Capital consented to that assignment

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

and assumption by 303554 Alberta on May 26, 1994. The payout amount under the lease for this equipment was $86,138.64 at November 15, 1993 and had been reduced to about $71,000 in May of 1994.

17 Prior to 303554 Alberta taking over these lease obligations and the EX220 Hitachi Excavator, there were about three or four discussions between Mr. Dwyer and Mr. Seaman. According to Mr. Seaman, Mr. Dwyer approached him in April of 1994 and inquired whether Mr. Seaman was going to purchase the EX220 Hitachi Excavator. Initially Mr. Seaman was unsure as to whether he was going to buy this piece of equipment, but ultimately he did decide to assume the lease for it. Earlier on Mr. Dwyer had approached GE Capital on the EX220 Hitachi Excavator, but a Mr. Cooper of GE Capital did not want to deal with him and so he turned to Mr. Seaman. Mr. Dwyer testified that when he discussed the EX220 Hitachi Excavator with Mr. Seaman, he indicated that he needed this piece of equipment. There was equity in it which Mr. Dwyer wished to apply against his indebtedness to the Banks. In other words, Mr. Dwyer had suggested to Mr. Seaman that if he bought the EX220 Hitachi Excavator from him, he would reimburse Mr. Seaman for whatever he had paid GE Capital plus any associated costs. Mr. Seaman denied that that had been the tenor of their conversation. In any event, whether or not Mr. Dwyer's version on this is correct, it is clear that he fully intended to obtain the same deal on the EX220 Hitachi Excavator that Mr. Seaman had negotiated with GE Capital.

18 Prior to the conclusion of the Plaintiff's case, the Plaintiff called Mr. Leaver, an appraiser with Sterling Heavy Equipment Appraisals, to give evidence concerning the value of the assets disposed of by 286618 Alberta to 303554 Alberta. Mr. Leaver testified that the values of the assets shown in his appraisal report of May 12, 1995, were based on what the assets would sell for at public auction. Mr. Leaver was of the opinion that if the assets had sold at public auction, they would have sold for an amount in excess of what they actually did sell for. Mr. Leaver also provided some general information as to the cost that one could anticipate in getting a particular asset ready for public auction. He acknowledged that with respect to the equipment he examined and which is the subject of his appraisal, he did not determine the specific costs that would have to be incurred to prepare the equipment for public auction. Without factoring in these costs, Mr. Leaver admitted he was unable to present a true comparison with what had actually been paid by 303554 Alberta for the equipment. Mr. Seaman argues this is the weakness of the Plaintiff's case when he claims that 303554 Alberta bought equipment from 286618 Alberta at a price significantly less than the market value at the time.

19 At trial, Mr. Dwyer's counsel advised they were not proceeding against the Defendants, Mr. Fox and 286618 Alberta. Mr. Fox was bankrupt and 286618 Alberta had been dissolved on September 1, 1994.

20 With this factual background, I will now deal with the requirements the Plaintiff, Mr. Dwyer, should have satisfied (and failed to do so) in order to succeed in his claim under the *Statute of Elizabeth*. I will comment further on the facts as required. However, before doing so, I must indicate that I have not dealt with the matter of whether the Plaintiff would have succeeded under the *Fraudulent Preferences Act*. In argument, counsel for Mr. Dwyer conceded he was not going to advance a claim that was difficult under the *Fraudulent Preferences Act*, R.S.A. 1980, c. F-18, and amendments thereto. It was clear that under that Act the Plaintiff would fail in its claim under either sections 1, 2 and 3 primarily because he could not prove the various creditor requirements under those sections.

II Alleged Fraudulent Conveyance Pursuant to the Statute of Elizabeth

21 Mr. Dwyer has pursued a claim against 303554 Alberta declaring that these transactions between 286618 Alberta and 303554 Alberta are fraudulent conveyances caught by the provisions of the *Statute of Elizabeth*. The thrust of Mr. Dwyer's claim is that substantially all of the assets of 286618 Alberta were disposed of to 303554 Alberta and at prices significantlybelow fair market value. Mr. Seaman disputes that and states that in any event certain requirements must be

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

satisfied under the Statute for the Plaintiff to succeed in his claim.

22 Under the *Statute of Elizabeth*, a fraudulent conveyance can be set aside even though the grantor is solvent and the prejudiced creditor has not reduced his claim to judgment. The Statute states that it applies to conveyances made "...to delay, hinder or defraud creditors and others...". In the case before me, "the others" could include Mr. Dwyer as he was a guarantor of the indebtedness of 286618 Alberta as it related to both the GE Capital obligation and the loans of Mr. Fox to the Royal Bank and Treaty Seven. Although Mr. Dwyer may be able to establish that he was a "creditor or other" of the Defendant 286618 Alberta at the time of the transactions in question, I am satisfied from my review of the law and cases supplied to me that there are other requirements the Plaintiff must satisfy in order to succeed under the Statute. Mr. Dwyer must also prove the following:

1. The Defendant 286618 Alberta had the intent to delay, hinder, or defraud a creditor;
2. The Defendant 286618 Alberta retained an improper benefit from the conveyances in question; and
3. Since there was more than nominal consideration paid, the Defendant 303554 Alberta had a fraudulent intent.

23 In this case, Mr. Dwyer has done none of this for the reasons I will now elaborate on.

Alleged Fraudulent Intent

24 In arriving at this conclusion, I have reviewed the circumstances surrounding the four transactions. I have done this primarily to assess if in fact there was a fraudulent intent by both 286618 Alberta and 303554 Alberta to delay, hinder or defraud the Plaintiff, Mr. Dwyer or any other creditor of 286618 Alberta and Mr. Fox. For as the fraudulent preference case of *Canadian Imperial Bank of Commerce v. Grande Cache Motor Inn Ltd.* (1977), (sub nom. *Hobbema Farms Ltd. v. Grande Cache Motor Inn Ltd.)* 9 A.R. 208 [4 Alta. L.R. (2d) 319] (T.D.), points out at page 221:

> Halsbury's Laws of England (3d Ed.), Volume 17, Page 656, Paragraph 1265 states:
>
> > The question of intent to defraud creditors is always one of fact, which the court has to decide on the merits of each particular case after taking all the circumstances surrounding the making of the alienation into account.
> >
> > I acknowledge that any allegation of fraudulent intent is a serious one and should not be found as a fact without the presence of substantial evidence in which to base such a finding.

25 Dealing then with the first point and third points, what evidence is there that Mr. Fox on his own behalf and as the governing mind of 286618 Alberta and Mr. Seaman as the governing mind of 303554 Alberta had an intent to delay, hinder or defraud the guarantor, Mr. Dwyer or any other creditor?

26 There is no clear evidence of a fraudulent intent on the part of Mr. Fox. Mr. Fox did not appear at trial to testify, so I do not have any first-hand knowledge as to his state of mind at the time these four transactions occurred. The case of *Alberta (Attorney General) v. Samuel Doz Professional Corp.* (1993), 139 A.R. 198 [9 Alta. L.R. (3d) 201] (Q.B.), recognized it is

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

unlikely for a debtor to admit to an intent to defeat or defraud his creditors. Consequently, the Plaintiff must look to the circumstances surrounding the transactions to prove such a fraudulent intent. In *Alberta (Attorney General) v. Samuel Doz Professional Corp., supra*, Ritter J. at page 202 looked at what is commonly called the "badges of fraud" to establish fraudulent intent on the part of the debtor. Ritter J. noted these "badges of fraud" included:

(i) The consideration was grossly inadequate;

(ii) The conveyance was accomplished quickly;

(iii) The parties to the transaction were related in a business sense; and

(iv) The conveyance was very general in nature in that it disposed of virtually all of the assets of the debtor.

27 Are these badges of fraud present in this case so as to establish not only a fraudulent intent on the part of Mr. Fox but also on Mr. Seaman, the owner/operator of 303554 Alberta and the transferee in these transactions? I have determined from the evidence that these "badges of fraud" are not present so as to sufficiently conclude the fraudulent intent that the Plaintiff must prove.

28 The Plaintiff argues from the cases of *Schlumpf v. Corey* (1994), 25 C.B.R. (3d) 297 [19 Alta. L.R. (3d) 385] (Alta. Master), *Re Barnett* (1983), 46 C.B.R. (N.S.) 211 (Alta. Q.B.), and *Nicholson v. Milne* (1989), 74 C.B.R. (N.S.) 263 [67 Alta. L.R. (2d) 130] (Alta. Q.B.), that he need not establish all of the "badges of fraud" in order to prove the fraudulent intent of the parties to these transactions. As per *Re Barnett* at page 216, the Plaintiff submits that under the *Statute of Elizabeth*: "The applicants need only show that the result of the impugned conveyance has the necessary consequence that there is nothing left for the debtor's creditors...". This is a position I do not accept from my reading of *Re Barnett, supra*, and the other cases the Plaintiff has referred to. For in the same paragraph on page 216 of *Re Barnett*, Hope J., goes on to say: "Further, it is necessary that the transfer be made in good faith and I have already found that not to be the case."

29 It is clear from the case of *Re Barnett* and the other authorities the Plaintiff has relied on, that the Courts are cognizant of the fact that fraudulent intent should not be found without substantial evidence. To require a plaintiff to prove the disposition of substantially all of a defendant's assets and nothing else for fraudulent intent, is far too narrow a view and flies in the face of requiring substantial evidence for fraudulent intent. I suspect that Mr. Dwyer has only put forward this position now as he recognizes the weakness of his evidence on fraudulent intent. For in the Plaintiff's Statement of Claim and in his counsel's summation following argument, the Plaintiff not only claimed that there had been a substantial disposition of 286618 Alberta's assets to 303554 Alberta but that disposition had been done at a price significantly below market value. Mr. Dwyer knows that proving fraudulent intent is a much broader concept than just showing a complete disposition of assets. Furthermore, I question the applicability of the Plaintiff's authorities on this point. In my reading of the Plaintiff's cases there was no bank or other creditor instructing a debtor to liquidate its assets to pay its outstanding indebtedness in those cases, as is the situation here with 286618 Alberta.

(i) Was the consideration grossly inadequate?

30 Turning back to the question of whether the "badges of fraud" are present in this case, I will now deal with the first badge of fraud relating to the consideration paid. It is Mr. Dwyer's contention that the consideration paid by 303554 Alberta for 286618 Alberta's equipment was grossly inadequate in that the equipment was sold significantly below market value. I have not found that to be the case.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

31 The evidence is that Mr. Seaman's company 303554 Alberta paid approximately $193,300 in cash and services to Mr. Fox's company 286618 Alberta for certain pieces of equipment it was disposing. This is equipment, if sold at public auction, could have been sold for about $346,000 according to the appraiser, Mr. Leaver. But this equipment did not sell at public auction and that is a factor I cannot ignore when deciding whether the consideration was grossly inadequate. It became clear on cross-examination of Mr. Leaver that had this equipment been sold at public auction, 286618 Alberta would have had to incur a number of costs (including transportation expenses and commissions) for which he could not give a definite amount. That uncertainty in itself, is sufficient in my opinion to conclude Mr. Dwyer is not able to prove that the consideration paid was grossly inadequate.

32 Furthermore, I cannot ignore that Mr. Dwyer himself often attributed different values to certain assets for different purposes. For example, about a year prior to the fourth transaction Mr. Dwyer acquired certain assets of 286618 Alberta in consideration of selling all of his shares in 286618 Alberta to Mr. Fox. These assets were given a value of $32,900 as set out in Schedule "C" to the May 20, 1993 agreement. A Bill of Sale was executed that purported to show that $32,900 was paid by Mr. Dwyer and received by 286618 Alberta. However, Mr. Dwyer paid no monies for those assets. Mr. Dwyer claims that that was the consideration for his shares. But as was pointed out on behalf of Mr. Seaman that wasn't consideration for Mr. Fox to give Mr. Dwyer for those shares. Those assets that were disposed of for $32,900 to Mr. Dwyer belonged to 286618 Alberta, not to Mr. Fox, and yet they were treated as consideration for the purchase of shares by Mr. Fox. I find it curious that Mr. Dwyer was prepared to accept this low value of $32,900 on the equipment he was acquiring from 286618 Alberta under the May 20, 1993 agreement. Yet, one year later Mr. Dwyer challenges Mr. Seaman on the price paid by 303554 Alberta for other equipment it purchased from Mr. Fox and 286618 Alberta in the fall of 1993 and the spring of 1994. But even more importantly Mr. Dwyer listed those acquired assets with an established value of $32,900 in the February 1995 edition of Trader magazine at significantly higher values. The AtlasCopco tank drill was listed in the magazine at $38,000, although in Schedule "C" of the May 20, 1993 agreement it was shown at $16,000. In the case of the Poclain 600 shovel, on Schedule "C" it showed a value of $15,000, but in the magazine it was listed for $85,000. In the result, I am satisfied that the Plaintiff, Mr. Dwyer, has received a benefit in these Schedule "C" assets which is significantly higher than the listed value of $32,900. Mr. Dwyer cannot now be heard to complain that 303554 Alberta has purchased equipment from 286618 Alberta for prices significantly below market value when Mr. Dwyer himself would appear to have done that very thing. Furthermore, if this $32,900 worth of assets, which belonged to the company, had remained with 286618 Alberta and not been transferred to Mr. Dwyer in May of 1993 for no consideration, this claim of Mr. Dwyer's may well not have arisen. In any event, all of this in it itself demonstrates to me that the amounts paid by 303554 Alberta for 286618 Alberta's equipment may not have been out of line under the circumstances. This is especially so, given that Mr. Fox and 286618 Alberta sold the equipment under what was really a distress situation.

33 GE Capital, the Royal Bank and Treaty Seven Development Centre served demands under their loans in the fall of 1993 on Mr. Fox, 286618 Alberta, and Mr. Dwyer as guarantor. At trial, Ms. Tibbatts made it clear that in the fall of 1993 and 1994 the Royal Bank was worried about its ability to collect on its loan to Mr. Fox. Ms. Tibbatts was aware that Mr. Fox and 286618 Alberta, with the Bank's encouragement, were selling assets to 303554 Alberta and then using the proceeds to pay off their loans. Certainly, the Royal Bank was not overly concerned about the consideration paid by 303554 Alberta for this equipment. The Royal Bank conducted no appraisals prior to the sale of equipment to 303554 Alberta. It was the Bank's attitude that 303554 Alberta could pay those amounts Mr. Seaman had disclosed in his conversations to Ms. Tibbatts, so long as those monies went to the Royal Bank to reduce Mr. Fox's loan. That is in fact what happened. Never did Ms. Tibbatts of the Royal Bank question whether the amounts paid by 303554 Alberta for this equipment were grossly inadequate.

34 Mr. Dwyer submits the key to this issue of consideration is: whether Mr. Seaman misled Ms. Tibbatts as to the values of the equipment he was buying from 286618 Alberta. Mr. Dwyer contends that Mr. Seaman misled Ms. Tibbatts concerning the first three transactions between 286618 Alberta and 303554 Alberta. In the first transaction, Mr. Dwyer submits that Mr. Seaman did have a conversation with Ms. Tibbatts concerning the value of the 1990 Kobelco and the 1983 Komatsu. Mr. Dwyer refers to Mr. Seaman's responses in lines 23-27 on page 24 and lines 1 and 2 of page 25 of his Examination for Discovery on October 31, 1994, as evidence of this. In his Examination for Discovery Mr. Seaman acknowledged that when

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

asked by Ms. Tibbatts what he thought this equipment was worth, he thought it was something less than was owing on it. At trial on cross-examination, Mr. Seaman initially responded to this question by saying that he told Ms. Tibbatts he was prepared to pay $57,800 (the payout amount) for both pieces of equipment. Mr. Seaman made no mention of value or worth of the equipment in this reply. On further cross-examination, Mr. Seaman admitted that he had told Ms. Tibbatts that the value of the equipment was less than the payout amount. The Plaintiff submits that these inconsistent statements of Mr. Seaman's prove that he misled Ms. Tibbatts on the value of the 1990 Kobelco and the 1983 Komatsu. Mr. Dwyer contends that it is clear from Ms. Tibbatt's letter of November 26, 1993 to 303554 Alberta's solicitor, Mr. King, that she based her decision to release the Bank's security on the Kobelco and the Kamatsu on this misleading conversation with Mr. Seaman. I do not agree. If that were the case, Mr. Seaman would have paid an amount for this equipment that was less than the payout amount of $57,800. In fact, what happened is as stated in the letter of November 26, 1993. Mr. Seaman paid an amount sufficient only to retire the debt with GE Capital Corporation.

35 Furthermore, I am satisfied Ms. Tibbatts did not recall any specific conversations on value with Mr. Seaman. Certainly, it wasn't put to Ms. Tibbatts by Mr. Dwyer's counsel that she was relying on some appraisal conducted by Mr. Seaman as to the value of those assets. If that is the theory Mr. Dwyer wished to advance, his counsel had an obligation to put that question to Ms. Tibbatts and he did not do so.

36 In the second transaction of early December 1993, Mr. Dwyer again contends that Mr. Seaman in his conversation with Ms. Tibbatts misled her as to the details of this transaction. Specifically, Mr. Dwyer states that Mr. Seaman did not advise Ms. Tibbatts that $30,000 of the $45,000 consideration to be paid by 303554 Alberta was to be $30,000 worth of hourly work to 286618 Alberta or its designate; nor did Mr. Seaman provide Ms. Tibbatts with a copy of the service agreement. It is suggested on behalf of Mr. Dwyer that had Ms. Tibbatts been advised of this $30,000 service agreement, the Royal Bank may not have consented to the sale of the Hitachi Excavator parts, the Willock Low Bed and the End Dump Trailer to 303554 Alberta for $15,000 cash and $30,000 worth of work. That hypothetical was in fact put to Ms. Tibbatts on direct examination but she never did indicate that the Bank would not have approved of this second transaction. Her answer to that question was: "We were trying to recover funds so we wouldn't try to recover cash from that." In no way does that response of Ms. Tibbatt's suggest disapproval by the Bank if it had been made aware of the $30,000 service agreement.

37 In fact, Ms. Tibbatt's evidence on whether she was advised of the service agreement or $30,000 worth of work is "fuzzy" at best, to quote Mr. Dwyer's counsel. On cross-examination, Ms. Tibbatts acknowledged the best she could say about what Mr. Seaman had told her about the $30,000 worth of work was that she didn't recall being told about it. I believe that to be the case and that in fact Mr. Seaman did tell her about the $30,000 worth of work when he spoke to her concerning these three pieces of equipment. Granted he may not have specifically said to Ms. Tibbatts "I've got a service agreement", but then he is not a lawyer and is unlikely to speak in those terms. More importantly, Mr. King pointed out to Mr. Pollock in his letter of January 5, 1994 that the Bill of Sale should be amended to properly reflect the consideration of $15,000 cash and $30,000 for services. That amendment wasn't done and the correspondence and Mr. King's testimony satisfies me as to why that wasn't done. Accordingly, I cannot accept Mr. Dwyer's submission that there was a side deal made between 286618 Alberta and 303554 Alberta for this $30,000 worth of work of which the Royal Bank was never advised of. Quite the contrary; in fact, Ms. Tibbatts signed off on this transaction in her letter of December 14, 1993 to Mr. Pollock. When the Royal Bank received $5,000 of the sale proceeds and the confirmation it required for the $10,000 lease payments to GE Capital, it released its security in the three pieces of equipment. At no time did the Royal Bank make any enquiries of Mr. Seaman as to the adequacy of consideration for these three pieces of equipment nor, as indicated earlier, did it conduct an appraisal.

38 As for the third transaction, Mr. Dwyer does not take issue with the fact that Mr. Seaman did have a conversation with Ms. Tibbatts at some time concerning the purchase of additional equipment from 286618 Alberta for $19,500. What he does dispute is Mr. Seaman's claim that this third transaction occurred in April of 1994. Mr. Dwyer contends that this additional equipment described in a Bill of Sale marked as Exhibit 18 was actually purchased by Mr. Seaman on behalf of 303554

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Alberta at the time of the second transaction in December of 1993 and this in fact was not disclosed to Ms. Tibbatts. I do not accept this claim of Mr. Dwyer's for reasons to be discussed under subheading (iv) below.

39 Finally, Mr. Dwyer claims the equipment 303554 Alberta acquired from 286618 Alberta was not in the state of disrepair as testified to by Mr. Seaman. Therefore, he argues the prices paid by 303554 Alberta for this equipment should have been higher than they were. Mr. Dwyer points to the testimony of his employees Mr. Dennis, Mr. Dziedzic and Mr. Thompson as evidence of this. However, those witnesses and in particular Mr. Thompson were on the job site only until November of 1993. While Mr. Thompson can speak to the condition of the Kobelco and the Kamatsu up to the time they were transferred to 303554 Alberta and to within a month of the Willock Low Bed and the other two pieces of equipment that were transferred in December of 1993, he cannot speak to the balance of the equipment transferred in April of 1994. Thus, there has been no evidence from the Plaintiff as to the condition of these assets as at April 1994. There is, however some evidence from Mr. Seaman and found in Exhibit 18 with respect to their condition at that time. In Exhibit 18, the parties to that transaction wrote into the Bill of Sale that the machinery was "in very terrible condition." Mr. Seaman could have been cross-examined on this point but was not and so I accept Mr. Seaman's testimony on the state of disrepair of the equipment.

40 Mr. Dwyer argues I should not overlook the fact that Mr. Seaman's mechanic, Mr. Canesson, lives in the Crowsnest Pass and if called to testify, he would have been able to give the best evidence as to the state of the equipment purchased by 303554 Alberta. Mr. Canesson was not called by 303554 Alberta to give evidence and so it is submitted I should follow the case law presented by the Plaintiff and draw an adverse inference against 303554 Alberta on this point. Mr. Dwyer states that 303554 Alberta must have feared what Mr. Canesson had to say about the state of the equipment and the below market prices 303554 Alberta paid for it. That is why Mr. Canesson was not called as a witness. But as was pointed out on behalf of 303554 Alberta, if the missing evidence could have equally been called by either party, no adverse interest should be drawn against either party. I am satisfied based on my reading of a recent Ontario Court of Appeal case, *Lambert v. Quinn* (1994), 110 D.L.R. (4th) 284, that this is not a proper case to draw an adverse inference.

41 During cross-examination, Mr. Dwyer indicated he had met with Mr. Canesson and a Mr. McDonald a couple of weeks prior to trial. There is no evidence to suggest that these individuals could not have been called by Mr. Dwyer. In fact, they could have been called by Mr. Dwyer but were not. In the result, no adverse inference will be drawn against 303554 Alberta with respect to the price paid for and the state of the equipment sold to 303554 Alberta.

42 As I have determined there is insufficient evidence to support Mr. Dwyer's claim that the consideration paid by 303554 Alberta for the equipment was grossly inadequate, I will now deal with the remaining "badges of fraud".

(ii) Was the conveyance accomplished quickly?

43 In this particular case, the sale of equipment was not accomplished quickly. There were four separate transactions concerning disposition of this equipment from 286618 Alberta to 303554 Alberta. These transactions took place between November of 1993 and May of 1994. More importantly, these transactions were not done in secrecy. All of the creditors being GE Capital, Royal Bank, and Treaty Seven were involved. The evidence of Mr. Dwyer and Ms. Tibbatts supports the fact Mr. Seaman dealt with his creditors on these transactions. Furthermore, the Royal Bank signed off on the first three transactions and released its security in the equipment sold to 303554 Alberta.

(iii) Were the parties related to the transaction in a business sense?

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

44 286618 Alberta and 303554 Alberta had no relationship in a business sense and there was no evidence before me to support this. Neither one of these parties was a shareholder of or a parent or subsidiary company of the other or a landlord or tenant of the other; neither did they carry on business in the same premises as the other party. In no way could they be said to be directly or indirectly related or associated. I am satisfied these parties were dealing at arm's length during the course of these transactions.

(iv) Was the conveyance very general in nature in that it disposed of virtually all of the assets of 286618 Alberta?

45 The position of Mr. Dwyer is that the disposition of this equipment to 303554 Alberta was general in nature and substantially all of 286618 Alberta's equipment was disposed of to 303554 Alberta. Mr. Dwyer argues that the consequence of that is there was nothing left for creditors such as the Royal Bank. Therefore, the transactions in question should be caught by the provisions of the *Statute of Elizabeth*. I do not accept this position as it is not borne out by the evidence.

46 In fact, the transactions were not general in nature; they were quite specific. The first transaction dealt with the Kobelco and the Kamatsu. The second transaction dealt with three specified pieces of equipment. The third Bill of Sale in April of 1994 dealt with identified equipment. Finally, the Hitachi Excavator was dealt with separately in May of 1994 through an assumption of lease consented to by GE Capital. Even if I were to accept Mr. Dwyer's claim (which I do not) that the third transaction occurred concurrently with the second transaction, there still were three separate identifiable transactions which in my view could not be classified as being general in nature.

47 Mr. Dwyer has made much of the fact that in his view Mr. Seaman and 303554 Alberta fabricated the third transaction involving the Bill of Sale marked Exhibit 18. He relies to a very large extent on some of the admissions he was able to obtain from Mr. Seaman during his October 31, 1994 Examination for Discovery. But Mr. Seaman testified at trial that he was mistaken about these admissions made at the Examination for Discovery. I accept that to be the case as the weight of the evidence supports that conclusion.

48 At his October 31, 1994 Examination for Discovery, Mr. Seaman stated at page 35, lines 10 and 11, he believed there should have been more items listed on his lawyer's (i.e. Mr. King's) letter of December 8, 1993. This December 8, 1993 letter marked Exhibit 15, only referred to the purchase by 303554 Alberta of the Willock Low Bed, the Hitachi Excavator parts and the End Dump Trailer. On further questioning by Mr. Dwyer's counsel, Mr. Seaman then explained why he did not ask for a Bill of Sale for the additional items. Mr. Seaman's explanation was that a lot of these items never had serial numbers on them. In addition, he couldn't obtain a clear answer as to whether these items were liened and if so, whether the Royal Bank would clear them. At trial, Mr. Seaman was again asked on cross-examination whether he had purchased more pieces of equipment at the time he purchased the Willock Low Bed, the Hitachi Excavator parts and the End Dump Trailer. His initial response was to the effect that only those three pieces of equipment had been purchased. Mr. Seaman was then reminded of what he had said at his Examination for Discovery. Mr. Seaman acknowledged the answers that he had given at that time were truthful but that he was not really prepared for the Examination for Discovery. It was really the first time that he had gone through the details of all of the transactions. At trial he indicated that he was in error on the responses he gave at the time of the Examination for Discovery. His lawyer, Mr. King, conceded that he did not go into the Examination for Discovery of Mr. Seaman with a great deal of preparation. Mr. King admitted that at the Examination for Discovery, he himself was not clear as to what pieces of equipment were included in the second transaction of December 1993 and what were included in the third transaction of April 1994. I can understand how confusion and uncertainty developed on this matter on the part of Mr. Seaman.

49 Mr. Dwyer points out that notwithstanding Mr. Seaman's initial response at trial, Mr. Seaman later on in

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

cross-examination agreed with Mr. Dwyer's counsel that he had made a conscious decision not to disclose these additional items to the Royal Bank in December of 1993 because he was worried about liens. But the fact of the matter was, as Mr. Seaman later explained in his cross-examination, the reason there was no disclosure on this additional equipment nor correspondence with the Royal Bank asking for the release of its security on this other equipment was because as Mr. Seaman stated "I never made the deal on those other pieces at that time." It is evident to me that Mr. Seaman was not prepared to speak with Ms. Tibbatts concerning the purchase of the additional equipment until he was fully satisfied he could obtain a release of the Bank's security. That in fact did happen in April of 1994 when Mr. Seaman had a conversation with Ms. Tibbatts concerning the purchase of additional equipment for the sum of $19,500. At trial, Ms. Tibbatts confirmed this transaction of April 1994. The Royal Bank received the $19,500 in May of 1994 and applied it to reduce the indebtedness of Mr. Fox to it. It is clear that the Royal Bank was aware of this third transaction and that it occurred at the time that Mr. Seaman claims it is to have occurred.

50 Mr. Dwyer submits I should be bound by the answers that were given by Mr. Seaman in his Examination for Discovery. Mr. Dwyer argues to the extent that there are any inconsistencies in Mr. Seaman's testimony at trial from that given at the Examination for Discovery, I should look only to his evidence given at the Examination for Discovery for presumably Mr. Seaman's memory was fresher at that time. However, as has been pointed out as per the case of *Mackow v. Sood* (1993), 141 A.R. 233 (C.A.), at pages 236-37, where, as here, Mr. Seaman has given evidence at trial, I am free "to exercise (my) normal function of assessing credibility, finding facts, and reaching conclusions from all the evidence, and (I am) not bound to accept those discovery extracts read in..." (wording in brackets is mine). I have done that and accepted Mr. Seaman's explanation that he was in error on certain admissions he made at his Examination for Discovery.

51 Mr. Dwyer has suggested there were other pieces of equipment not covered by the Bills of Sale that were transferred to 303554 Alberta in the first three transactions. Mr. Seaman denies that and is adamant that he only acquired those pieces of equipment as specified in the Bills of Sale for the three transactions and the assignment of lease consented to by GE Capital. I believe him and so I accept his evidence on this.

52 Mr. Dwyer has alleged that Mr. Seaman stole or wrongfully came into possession of an additional two buckets, the quick change adapter and the Twist-O-Wrist. I see no basis for this allegation. Firstly, all that was presented at trial was hearsay evidence as to anything being stolen on the attachments to the 1991 Hitachi EX 220 Hydraulic Excavator. Secondly, there was no evidence whatsoever presented by Mr. Dwyer indicating that Mr. Seaman was involved in the alleged theft. On cross-examination, Mr. Seaman made it dear that no RCMP officer had questioned him about the buckets to the Hitachi. Interestingly, Mr. Seaman was never asked how he came into possession of those attachments. Certainly, if Mr. Dwyer is going to accuse Mr. Seaman of theft, he must have sufficient evidence to prove it beyond a reasonable doubt. In this case, Mr. Dwyer is far from that.

53 The next equipment Mr. Dwyer claims 303554 Alberta obtained from 286618 Alberta were the trailer contents identified in paragraph (I) of Mr. Leaver's appraisal. It is clear to me there was no evidence to prove that Mr. Seaman on behalf of 303554 Alberta ever bought the trailer contents or that they were in the trailers when he purchased those trailers. Even if I accept Mr. Thompson's evidence there were certain tools, tarps and construction supplies in the trailers when he left his job in November of 1993, I note 303554 Alberta did not acquire these trailers until April of 1994. Accordingly, I am satisfied the evidence presented is not sufficient to make the inference that these items were in the trailers when they were disposed of to 303554 Alberta in April of 1994.

54 Again, the same set of circumstances applies to the 4'' gas powered water pump and any other items not included in the three Bills of Sale and the Assignment of Lease. When Mr. Leaver conducted the appraisal of the equipment together with Mr. Dwyer, he did not view any gas powered water pump, assorted hand tools, tarps and construction supplies. From

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Mr. Dwyer's testimony, it is evident he does not know what happened to the gas powered water pump after May of 1993. Mr. Thompson did however say that the gas powered water pump was there in November of 1993, but there is no evidence as to what happened to it between November of 1993 and April of 1994. In fact, Mr. Seaman's hand written note marked as Exhibit 22 shows a value of zero for the 4" gas powered water pump. In short, there is no evidence that Mr. Seaman or his company purchased the gas powered water pump or for that matter any of those items Mr. Seaman specifically denied acquiring, such as the sand unit. Consequently, I am satisfied that 303554 Alberta acquired only the equipment and items that are the subject matter of the three Bills of Sale and the Assignment of Lease and nothing more. 303554 Alberta did not acquire virtually all of the assets of 286618 Alberta as Mr. Dwyer alleges.

55 As I have determined that the "badges of fraud" have not been established to prove the fraudulent intent of Mr. Fox and Mr. Seaman, Mr. Dwyer's claim must fail under the *Statute of Elizabeth*. As Justice Ritter pointed out in *Alberta (Attorney General) v. Samuel Doz Professional Corp., supra,*:

> Stripped to its essentials, the *Statute of Elizabeth* provides a mechanism whereby creditors and others can attack conveyances and other transactions made by persons with the intent to delay, hinder or defraud creditors or others. The intent required, as with the *Fraudulent Preferences Act*, is that of the donor although s. V(1) makes the intent or knowledge of the donee a relevant and crucial consideration.

56 In this case, the Plaintiff, Mr. Dwyer, focused entirely on the conduct of the donee, Mr. Seaman and has not addressed the intent of the donor, Mr. Fox. That in itself is a fatal weakness of the Plaintiff's case. Moreover, Mr. Dwyer somehow suggests that Mr. Seaman has taken advantage of the situation and that he and his company 303554 Alberta have paid too little for the equipment acquired from 286618 Alberta. I find this ironic, given that Mr. Dwyer would have purchased the equipment from 286618 Alberta for the very price Mr. Seaman had paid, had he been given that opportunity; and yet, because he was denied that opportunity Mr. Dwyer now alleges these transactions are suspect. Having looked at the whole of the evidence surrounding these transactions, I do not find there to be any merit to Mr. Dwyer's allegation. Even if Mr. Seaman had known that Mr. Fox's ultimate plan was to ensure that Mr. Dwyer would be left solely responsible as a guarantor for his loan obligations, that in itself would have been inconclusive. In order to succeed in his claim, Mr. Dwyer must be able to show that Mr. Seaman actively participated in the fraud to achieve a benefit for Mr. Fox and himself. The evidence in no way supports that kind of activity. Furthermore, as has been pointed out in the case of *Mulcahy v. Archibald* (1898), 28 S.C.R. 523, at page 529:

> ... it has been decided over and over again that knowledge on the part of such a transferee of the motive or design of the transferor is not conclusive of bad faith or will not preclude him from obtaining the benefit of his security.

Alleged Retention of an Improper Benefit

57 I now turn to consider whether Mr. Fox or his company 286618 Alberta retained an improper benefit from the conveyances in question. As Madam Justice Hunt pointed out in *Sun Sudan Oil Co. v. Methanex Corp.* (1992), 5 Alta. L.R. (3d) 292 (Q.B.), this is the key in determining whether these transactions are void under the *Statute of Elizabeth*. Madam Justice Hunt at page 317 of *Sun Sudan Oil Co. v. Methanex Corp., supra*, states:

> A claim was also put forward under the Statute of Elizabeth [1571 (U.K.), 13 Eliz. 1, c. 5]. However, as I read the cases that Statute (which is not directed at fraudulent preferences per se but rather at fraudulent conveyances; in other words, it does not require that a debtor-creditor relationship be established and is from this point of view broader than the Fraudulent Preferences Act) only comes into play when the assignor reserves some benefit to himself: see, e.g., *Anderson Lumber Co. v. Canadian Conifer Ltd.*, [1977] 5 W.W.R. 41, 77 D.L.R. (3d) 126, 25 C.B.R. 35, 4 A.R. 282

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(C.A.), and *Mulcahy v. Archibald* (1898), 28 S.C.R. 523. There is no evidence of such a situation here.

58 In the case at bar, what improper benefit have Mr. Fox and/or 286618 Alberta retained? There is none whatsoever. In fact, the evidence is that any money that 303554 Alberta paid for the equipment was directed to Mr. Fox's and 286618 Alberta's creditors to reduce their indebtedness. None of those sale proceeds were retained by Mr. Fox and 286618 Alberta for their own use. Mr. Dwyer's evidence corroborates that finding. Mr. Dwyer acknowledged that at the time he sold his shares in 286618 Alberta to Mr Fox, the indebtedness to Treaty Seven and the Royal Bank was $60,000 and $110,000 respectively. By the time Mr. Dwyer was sued as a guarantor of these loans by the Royal Bank and Treaty Seven in May of 1994, the indebtedness to the Royal Bank had been reduced to about $56,000 and the indebtedness to Treaty Seven had been reduced to a like amount of $55,000 or $56,000. Likewise, Mr. Dwyer's liability as a guarantor under a guarantee bond to GE Capital had been virtually eliminated by May of 1994.

59 Mr. Dwyer suggests that Mr. Fox and 286618 Alberta retained an improper benefit through the $30,000 service agreement. He argues that if in fact the service agreement does exist, it was a benefit to Mr. Fox and 286618 Alberta which survived the conveyance of certain equipment in December of 1993.

60 Although I do not dispute that the obligations under the service agreement survived the conveyance, I can find no evidence to suggest that by performing the $30,000 worth of work after December 1993 Mr. Fox and 286618 Alberta somehow retained an improper benefit. Clearly, the evidence suggests the contrary. I am satisfied from the evidence presented that there was a valid existing service agreement between 303554 Alberta and 286618 Alberta or its designate for $30,000 worth of work to be performed in the general vicinity of the Blood Indian Reserve at Standoff, Alberta. That $30,000 worth of work was in fact performed by 303554 Alberta at the construction site at Standoff and completed by February of 1994. During that period the indebtedness to creditors, such as the Royal Bank, continued to decline. In the result, Mr. Fox and 286618 Alberta did not retain any improper benefit through the service agreement.

III Conclusion

61 As I understand the cases, the *Statute of Elizabeth* is designed to prevent a debtor from placing his assets out of the reach of potential creditors and others while at the same time he retains the benefit of those assets. That is not what occurred in this case. Mr. Fox and 286618 Alberta sold specific items of equipment to 303554 Alberta for fair and valuable consideration. Mr. Dwyer comes to this Court and submits that this consideration was not enough. He claims he needs more to reduce his liability to creditors. Mr. Dwyer has been called on his guarantee and understandably he wants to protect his own position. That is why he wants more in the way of consideration. But at the time Mr. Fox and 286618 Alberta sold and transferred the equipment to 303554 Alberta, Mr. Dwyer did not complain and was quite prepared to take the benefit of the sale proceeds that were paid over to creditors from these transactions. For Mr. Dwyer to now say the consideration paid by 303554 Alberta was not enough, does not in my opinion bring this case within the provisions of the *Statute of Elizabeth.* After having heard all of the evidence, I am satisfied these transactions relating to the transfer of the equipment from 286618 Alberta to 303554 Alberta were made bona fide for good consideration and thus are not caught by the Statute of Elizabeth.

62 For all of the foregoing reasons, I have dismissed the plaintiff's claim. Although Mr. Seaman's counsel has submitted a written brief with respect to costs, I have not made any award as to costs at this time. However, the matter of costs may be addressed if the parties wish at a time convenient to counsel.

Action dismissed.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Appendix 'A'

a. 1991 HITACHI EX220 Hydraulic Excavator;

b. 1990 KOBELCO K912LC-II Hydraulic Excavator;

c. 1979 CHAMPION 740 Motor Grader;

d. 1968 CATERPILLAR 955K Crawler Loader;

e. 1979 KENWORTH W900 TA Tractor;

f. CANCAR 3240F 40' Storage Van;

g. CANCAR 4240F 40' TA Storage Van;

h. CUSTOMBUILT 10'X38' Skidded Steel Building;

i. 4'' Gas Powered Water Pump;

j. Assorted Hand Tools, Tarps and Construction supplied in parts van;

k. 1983 KOMATSU D60E-7 Crawler Tractor;

l. 1987 FRUEHAUF DB4-M2-28-6-96 28' End Dump Trailer;

m. 1980 WILLOCK 40 Ton TA Single Drop Ramp Lowbed Trailer;

n. 1985 HITACHI UH07LC-7 Hydraulic Excavator;

o. 1980 INTERNATIONAL F2575 TA Dump Truck;

p. SCONA 35 Ton TA Oilfield Float;

q. EDMONTON STEEL FABRICATORS 6,000 Gallon Skidded Fuel Tank;

r. 1972 GARDINER DENVER SPFGB 85 CFM Portable Air Compressor;

s. CUSTOMBUILT 48'' Sheepsfoot Packer;

t. CUSTOMBUILT 48'' Sheepsfoot Packer;

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

u. KUBOTA Generator Set.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 31

2011 ABQB 213
Alberta Court of Queen's Bench

Taylor & Associates Ltd. v. Louis Bull Tribe No. 439

2011 CarswellAlta 796, 2011 ABQB 213, [2011] A.W.L.D. 2845, 201 A.C.W.S. (3d) 710, 46 Alta. L.R. (5th) 182, 525 A.R. 141, 79 C.B.R. (5th) 65

Taylor & Associates Ltd. (Plaintiff) and Louis Bull Tribe No. 439, 677626 Alberta Ltd., 415992 Alberta Ltd., Bear Hills Service Centre Ltd., Pigeon Lake Golf Club (1991) Ltd., Bear Hills Land Developments Ltd., Pigeon Lake Golf Club (1991) Holdings Ltd., K.H. Restaurants Ltd. (Defendants)

Louis Bull Tribe No. 439, 677626 Alberta Ltd., 415992 Alberta Ltd., Bear Hills Service Centre Ltd., Pigeon Lake Golf Club (1991) Ltd., Bear Hills Land Developments Ltd., Pigeon Lake Golf Club (1991) Holdings Ltd., K.H. Restaurants Ltd. (Plaintiffs by Counterclaim) and Taylor & Associates Ltd., Dwayne Taylor, 835537 Alberta Ltd., carrying on business as Mearon Construction, Harold Mearon, Verlie Sison, Po Chan, Helen Bull, Solomon Bull, Virgil Deschamps, Elaine Roasting and John Does No. 1 through 10 (Defendants by Counterclaim

A.W. Germain J.

Heard: February 28, 2011
Judgment: March 29, 2011
Docket: Edmonton 0103-11021

Counsel: G. James Thorlakson, for Louis Bull Tribe No. 439, 677626 Alberta Ltd., 415992 Alberta Ltd., Bear Hills Service Centre Ltd., Pigeon Lake Golf Club (1991) Ltd., Bear Hills Land Developments Ltd., Pigeon Lake Golf Club (1991) Holdings Ltd., K.H. Restaurants Ltd.
Dwayne Taylor, for himself, Taylor & Associates Inc.

Subject: Contracts; Corporate and Commercial; Torts; Civil Practice and Procedure; Public; Insolvency

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Debtors and creditors --- Fraudulent preferences — General principles

T Inc.'s claim was dismissed and counterclaim of First Nation band and various corporations owned by band was allowed — T Inc. was at all relevant times directed by DT, its majority shareholder, director and namesake — Number of parties, including DT and T Inc. were found jointly and severally liable to band and band-owned corporation for number of judgment amounts — Amount of $91,126.38 of band judgment against DT remained unpaid — Band brought application for declaration regarding certain funds taken from band and deposited into account of T Inc., alleging these funds were removed from T Inc. by DT under circumstances which constituted fraudulent preference — Application

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

granted — On balance of probabilities, DT removed $490,013.50 from his company T Inc., at time when T Inc. was insolvent — DT ended up with $490,013.50 in question — Criteria of s. 2 of Fraudulent Preferences Act were satisfied — DT paid himself in priority over another creditor, being band — DT was given benefit of doubt that he might have also been creditor for amount of money that he took for himself — T Inc. was indebted to band in amount equal to $520,769.67 — DT was presumptively owed $490,013.50 — Together, T Inc.'s debt was $1,010,783.17 — Band's share was 51.5 per cent — DT improperly, based on Act, took $490,013.50 from T Inc. — That transaction was reversed under Act, and T Inc. was owed $490,013.50 by DT — As creditor of T Inc., band was entitled to 51.5 per cent of amounts preferred to DT or $252,356.96 — Therefore, band had additional judgment against DT, based on fraud, in amount of $252,356.96.

Table of Authorities

Cases considered by *A.W. Germain J.*:

Don Forsey & Blackfalds Investments Ltd. v. Hydro Kleen Systems Inc. (2011), 74 C.B.R. (5th) 8, 2011 CarswellAlta 96, 2011 ABQB 14 (Alta. Q.B.) — referred to

Krumm v. McKay (2003), 47 C.B.R. (4th) 38, 2003 ABQB 437, 2003 CarswellAlta 961, [2003] 9 W.W.R. 442, 342 A.R. 169, 17 Alta. L.R. (4th) 103 (Alta. Q.B.) — referred to

Palechuk v. Fahrlander (2006), 61 Alta. L.R. (4th) 71, 397 A.R. 151, 384 W.A.C. 151, [2006] 10 W.W.R. 68, 28 R.F.L. (6th) 294, 26 E.T.R. (3d) 79, 2006 ABCA 242, 2006 CarswellAlta 1062, 273 D.L.R. (4th) 332 (Alta. C.A.) — considered

Palechuk v. Fahrlander (2007), 367 N.R. 394 (note), 2007 CarswellAlta 243, 2007 CarswellAlta 244, 425 A.R. 400 (note), 418 W.A.C. 400 (note) (S.C.C.) — referred to

Proprietary Industries Inc. v. Workum (2005), 2005 ABQB 610, 2005 CarswellAlta 1228 (Alta. Q.B.) — referred to

Proulx v. Proulx (2002), 25 R.F.L. (5th) 370, 316 A.R. 150, 2002 CarswellAlta 151, 2002 ABQB 151 (Alta. Q.B.) — referred to

Ramgotra (Trustee of) v. North American Life Assurance Co. (1996), 1996 CarswellSask 212F, 1996 CarswellSask 418, [1996] 3 W.W.R. 457, 37 C.B.R. (3d) 141, 10 C.C.P.B. 113, 13 E.T.R. (2d) 1, [1996] 1 C.T.C. 356, (sub nom. *Ramgotra (Bankrupt), Re)* 193 N.R. 186, (sub nom. *Ramgotra (Bankrupt), Re)* 141 Sask. R. 81, (sub nom. *Ramgotra (Bankrupt), Re)* 114 W.A.C. 81, (sub nom. *Royal Bank v. North American Life Assurance Co.)* 132 D.L.R. (4th) 193, (sub nom. *Royal Bank v. North American Life Assurance Co.)* [1996] 1 S.C.R. 325, (sub nom. *Royal Bank v. North American Life Assurance Co.)* 96 D.T.C. 6157 (S.C.C.) — considered

Shengli Oilfield Freet Petroleum Equipment Co. v. Ascension Virtual Group Ltd. (2010), 2010 CarswellAlta 2020, 2010 ABQB 597, 72 C.B.R. (5th) 285 (Alta. Master) — considered

Taylor & Associates Ltd. v. Louis Bull Tribe No. 439 (2006), 2006 CarswellAlta 1388, 2006 ABQB 698, 423 A.R. 164 (Alta. Q.B.) — considered

Taylor & Associates Ltd. v. Louis Bull Tribe No. 439 (2007), 423 A.R. 257, 2007 CarswellAlta 682, 2007 ABQB

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

350 (Alta. Q.B.) — considered

Titan Investments Ltd. Partnership, Re (2005), 2005 ABQB 637, 2005 CarswellAlta 1153, 14 C.B.R. (5th) 112, 383 A.R. 323 (Alta. Q.B.) — considered

834658 Alberta Ltd. v. 763319 Alberta Ltd. (2008), 2008 ABCA 371, 2008 CarswellAlta 1700, 75 C.L.R. (3d) 107, 48 C.B.R. (5th) 9, 438 W.A.C. 290, 440 A.R. 290 (Alta. C.A.) — referred to

Statutes considered:

Fraudulent Conveyances Act, 1571 (13 Eliz. 1), c. 5
Generally — referred to

Fraudulent Preferences Act, R.S.A. 2000, c. F-24
Generally — referred to

s. 1(a) — referred to

s. 1(b) — referred to

ss. 1-2 — referred to

ss. 1-3 — referred to

s. 2 — considered

s. 2(a) — referred to

s. 2(b) — referred to

s. 3 — considered

s. 11(1) — referred to

s. 11(2) — referred to

s. 11(4) — referred to

Rules considered:

Alberta Rules of Court, Alta. Reg. 390/68
R. 359 — referred to

Alberta Rules of Court, Alta. Reg. 124/2010
R. 9.24(1) — referred to

Tariffs considered:

Alberta Rules of Court, Alta. Reg. 124/2010
Sched. C, Tariff of Costs, column 5 — referred to

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

APPLICATION for declaration regarding certain funds taken from applicant and deposited into account of company, alleging that these funds were removed from company under circumstances which constituted fraudulent preference.

A.W. Germain J.:

1. Procedural History and Supplemental Judgment Overview

1 In October of 2006, I released my Reasons for Judgment in *Taylor & Associates Ltd. v. Louis Bull Tribe No. 439*, 2006 ABQB 698, 423 A.R. 164 (Alta. Q.B.) ["Taylor v. Louis Bull #1"]. In that judgment I dismissed the claim of Taylor & Associates Ltd. [Taylor Inc.] and allowed the counterclaim of Louis Bull Tribe No. 439 and various corporations owned by the Band [Louis Bull]. Taylor Inc. was at all relevant times directed by Dwayne Taylor, its majority shareholder, director, and namesake.

2 In *Taylor v. Louis Bull #1* I concluded a number of parties, including Mr. Taylor and Taylor Inc., were liable (jointly and severally) to Louis Bull and a Louis Bull owned corporation for a number of judgment amounts. These awards are summarized at paras. 130-131. I also concluded that the misconduct of Dwayne Taylor, Taylor Inc., and Mr. Po Chan (an accountant) warranted punitive damages (paras. 124-128). $91,126.38 of the Louis Bull judgment against Dwayne Taylor remains unpaid.

3 On May 14, 2007, I released supplemental reasons that flowed from the request of certain of the Defendants by counterclaim for reconsideration of some elements of *Taylor v. Louis Bull #1*. Those supplemental reasons were reported as *Taylor & Associates Ltd. v. Louis Bull Tribe No. 439*, 2007 ABQB 350, 423 A.R. 257 (Alta. Q.B.) ["Taylor v. Louis Bull #2"].

4 This supplemental judgment relates to a further application by Louis Bull for a declaration regarding certain funds taken from Louis Bull and deposited into the account of Taylor Inc. Louis Bull alleges these funds were removed from Taylor Inc. by defendant Dwayne Taylor under circumstances which constitute a fraudulent preference.

5 This is not the only allegedly fraudulent preference which has emerged in this matter. Louis Bull originally also applied for a declaration that Mr. Po Chan had engaged in a fraudulent preference when he transferred his home entirely into the name of his wife. That aspect of this application has been settled, and Mr. Chan in fact gave evidence for the Plaintiffs against Mr. Taylor. I understand that Mr. Chan has now paid off in full the judgment I granted in favor of Louis Bull against him in *Taylor v. Louis Bull #1*.

6 I will not in this supplemental judgment repeat the observations and findings that I made about how Louis Bull was taken advantage of by Mr. Dwayne Taylor and Taylor Inc. Nor will I repeat the observations I made about the minority shareholder in Taylor Inc., accountant Po Chan. These are detailed in *Taylor v. Louis Bull #1* .

7 This decision involves three issues:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

1. were the transfers of money out of Taylor Inc. a fraudulent preference,

2. who was the recipient of the funds removed from Taylor Inc., and

3. if the transfers were fraudulent, what amount can Louis Bull recover from Taylor Inc.?

2. The Position of the Parties

8 The position of Louis Bull is that in my first judgment I granted Louis Bull judgment against Taylor Inc.; that made Louis Bull a judgment creditor against Taylor Inc. Further, before Louis Bull became a judgment creditor it was a direct creditor because Dwayne Taylor improperly placed band monies into a new bank account maintained by Taylor Inc., and immediately thereafter diverted the bulk of these funds by money order to someone else. Louis Bull asserts that on a balance of probabilities, Dwayne Taylor was the ultimate recipient of these funds.

9 However, Taylor Inc. allegedly has other debts. Louis Bull accepts that Dwayne Taylor might also have been a creditor to his own company, as he generated the work effort that caused the band to pay the monies to Taylor Inc. As such, Louis Bull asserts that when Dwayne Taylor took the monies out of his company he preferred himself (as an employee/director creditor) over other creditors, though the only identified alternative creditor is Louis Bull.

10 Dwayne Taylor's position was given partially under oath in his own defense. He argues that if he took the monies out of the company, and he is not prepared to state that one way or the other, then all the funds involved went to lawyers who provided poor professional legal services, or alternatively the money may have gone to Po Chan. In any case, Mr. Taylor says he did not get the money, and adding a fraudulent preference amount to his personal judgment would be unfair to him. He says he is attempting to pay off the damages ordered in *Taylor v. Louis Bull #1*.

3. The Law

11 There are two legislative bases on which this Court can declare Mr. Taylor engaged in a fraudulent preference. The first is the *Fraudulent Preferences Act*, R.S.A. 2000, c. F-24 [the "*FPA*"]. This legislation has the effect of 'unwinding' or 'reversing' transactions which fall into certain categories. A general authority is provided by *FPA*, ss. 1-2 to unwind any transaction that was *intended* to defeat creditor debt recovery, if:

1. the person making a transfer of property knows that person is insolvent or is about to become insolvent (*FPA*, ss. 1(a), 2(a)), and

2. the transfer is intended to prevent the person's creditors from recovering their debts (*FPA*, s. 1(b)), or to prefer one creditor over another (*FPA*, s. 2(b)).

12 *FPA*, s. 3 provides a parallel authority to unwind a transaction that has the *effect* of defeating creditor debt recovery, provided the application is made within one year of the transaction. *FPA*, s. 3 does not require the applicant demonstrate there was any *intention* to favour one creditor over another.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

13 The Plaintiffs here say that a transfer of funds out of Taylor Inc. was intended to prevent Louis Bull from recovering the funds it was owed by preferring one creditor (Taylor) over another (Louis Bull), a *FPA*, s. 2 type scenario. That requires proof on a balance of probabilities of four factors (*Titan Investments Ltd. Partnership, Re*, 2005 ABQB 637 (Alta. Q.B.) at para. 13, (2005), 383 A.R. 323 (Alta. Q.B.); *Shengli Oilfield Freet Petroleum Equipment Co. v. Ascension Virtual Group Ltd.*, 2010 ABQB 597 (Alta. Master) at para. 8):

> ... under s. 2 of the FPA, the applicant must show (1) that there was a transfer of property, (2) by an insolvent person or a person who is on the eve of insolvency, (3) to a creditor, (4) with the intent of giving that creditor a preference.

14 If a fraudulent preference is identified and falls within the *FPA*, ss. 1-3 criteria, then the a creditor may seize and recover of the 'preferred' property or the proceeds of its sale (*FPA*, s. 11(1)). Alternatively, 'preferred' property may be the subject of a court application for an order to recover the 'preferred' property (*FPA*, s. 11(4)). Property or proceeds of property recovered under the *FPA* belong to all creditors, and not merely the party or parties who initiated the *FPA* procedure (*FPA*, s. 11(2)).

15 The second basis for the Plaintiffs' claim is the *Fraudulent Conveyances Statute*, 13 Eliz. 1, Chapter 5 (U.K.) [the "*Statute of Elizabeth*"]. This is a 16th century English act that has been 'inherited' by certain Canadian jurisdictions: *Ramgotra (Trustee of) v. North American Life Assurance Co.*, [1996] 1 S.C.R. 325 (S.C.C.) at paras. 61-63, (1996), 132 D.L.R. (4th) 193 (S.C.C.). Gonthier J. explains at para. 62 that the *Statute of Elizabeth* operates in manner parallel to that of the *FPA*, but allows a transfer to be unwound even where insolvency is not a risk.

> Several of the provincial fraudulent conveyance statutes impose an insolvency requirement, like that contained in Alberta's Act: Nova Scotia, New Brunswick, Prince Edward Island, Saskatchewan and Yukon. Thus, ... it would allow creditors to challenge fraudulent conveyances without having to prove that, at the time of the conveyance, the debtor was insolvent, was unable to pay his or her debts in full, or knew that he or she was on the eve of insolvency.

16 In *Palechuk v. Fahrlander*, 2006 ABCA 242, 273 D.L.R. (4th) 332 (Alta. C.A.), leave denied (2007), [2006] S.C.C.A. No. 405 (S.C.C.), the court at para. 31 identified five elements required for application of the *Statute of Elizabeth*:

> 31 To obtain a remedy under the Statute of Elizabeth, the plaintiff must establish the following:
>
> (1) there must be a conveyance of real or personal property;
>
> (2) for no or nominal consideration;
>
> (3) with intent to defraud, delay, or hinder creditors;
>
> (4) the party challenging the conveyance must be someone who was a creditor at the time of the conveyance or someone with a legal or equitable right to claim against the transferor; and
>
> (5) the conveyance must have had the intended effect.

See also *Proulx v. Proulx*, 2002 ABQB 151 (Alta. Q.B.) at para. 14, (2002), 316 A.R. 150 (Alta. Q.B.), and *Don Forsey & Blackfalds Investments Ltd. v. Hydro Kleen Systems Inc.*, 2011 ABQB 14 (Alta. Q.B.) at para. 100.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

17 A judgment creditor such as Louis Bull is authorized by the *Alberta Rules of Court* (*Alberta Rules Of Court*, Alta. Reg. 124/2010, s. 9.24(1); *Alberta Rules of Court*, Alta. Reg. 390/1968, s. 359) to apply under either the *FPA* or the *Statute of Elizabeth*; see also *834658 Alberta Ltd. v. 763319 Alberta Ltd.*, 2008 ABCA 371 (Alta. C.A.) at para. 6, (2008), 440 A.R. 290 (Alta. C.A.). The right to claim under the *FPA* or the *Statute of Elizabeth* arises on the date that a party to an action alleges a debt in its pleadings: *Krumm v. McKay*, 2003 ABQB 437 (Alta. Q.B.) at paras. 29-30, 40, (2003), 342 A.R. 169 (Alta. Q.B.); *Proprietary Industries Inc. v. Workum*, 2005 ABQB 610 (Alta. Q.B.) at paras. 13-18, (2005), 142 A.C.W.S. (3d) 100 (Alta. Q.B.); *Don Forsey & Blackfalds Investments Ltd. v. Hydro Kleen Systems Inc.* at para. 95.

4. The Facts

18 In a few short months in 2000 Mr. Dwayne Taylor, Mr. Po Chan, and their company Taylor Inc. inflicted much harm on Louis Bull. These two men and their corporation aligned themselves with a sympathetic faction of the Louis Bull leadership and systematically transferred the assets from the tribe to their own corporate account. Details of this egregious conduct may be found in the two prior judgments recorded by me that describe this troubling period of time for Louis Bull: *Taylor v. Louis Bull #1*; *Taylor v. Louis Bull #2*.

19 The Louis Bull Band Counsel was badly split at the time. By way of short summary, in May of 2000 a group of band leaders wrestled financial control of the Band from the chief Helen Bull and her counsel supporters. The Chief's faction was aligned with Mr. Taylor; they had hired him and his company to manage a number of struggling Band-owned businesses.

20 However, the Band received significant sums of borrowed money immediately prior to this takeover. The part of the Louis Bull leadership that was aligned with Mr. Taylor created a new Band account at the Treasury Branch in Wetaskiwin Alberta. The chief and her followers deposited large sums of borrowed money into the Treasury Branch, and systematically wrote similar large cheques to Taylor Inc. on the deposited funds: Notionally, all of these checks were to pay bills due to Taylor Inc.

Cheque Date	***Cheque Amount***
May 16, 2000	$186,000.00
May 25, 2000	$170,000.00
May 26, 2000	$164,769.67
	Total = $520,769.67

Notionally, all of these checks were to pay bills due to Taylor Inc.

21 Taylor Inc. was owned 70% by Dwayne Taylor and 30% by Po Chan. Dwayne Taylor was the bank signing authority and the clearly the business mind who directed the company. Taylor Inc was, effectively, the alter-ego of Dwayne Taylor. The company had no business other than managing the affairs of Louis Bull.

22 The financial records of Taylor Inc. were released to Louis Bull by court order in 2009. Its Toronto Dominion Canada Trust corporate account was opened on January 24, 2000 with an initial deposit of $150,000.00 from Louis Bull. Thereafter, and consistent with normal business practices, numerous small dollar amount corporate cheques were written which seemed to distribute that money in the normal course of business. However all of this changed in May 2000.

23 In that month three large money orders were purchased. In each case, a money order was issued the same day a cheque

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

was deposited. Their recipient is unknown; the financial institution is no longer able supply the information to indicate the payee of these money orders. There is a clear correlation between the money orders and the May payments to Taylor, Inc.:

Date	*Cheque Amount*	*Money Order Amount*
May 16, 2000	$186,000.00	$165,006.75
May 25, 2000	$170,000.00	$175,000.00
May 26, 2000	$164,769.67	$150,006.75
	Total = $520,769.67	Total = $490,013.50

24 I find that the money orders were unusual and not in the ordinary course of business. The money orders were clearly timed to withdraw money from Taylor Inc. as soon as the large amounts were received by that company. Dwayne Taylor knew about the monies coming in and was able to control their removal.

25 There were only two possible people who would have access to the Taylor Inc. account and who could authorize those type of transfers. One was Po Chan, the other was Dwayne Taylor. Po Chan gave evidence at this fraudulent preference hearing and denied that he had any cheque writing ability whatsoever on this company. He was only a minority shareholder. Generally his credibility is weak. I have previously concluded he fully and knowingly collaborated with Taylor's schemes to take money from the Band.

26 However, on this point he is believable because Dwayne Taylor was clearly the alter-ego of Taylor Inc. Dwayne Taylor was the major shareholder and director. Also, in the trial which I heard now some years ago there was no evidence whatsoever that Po Chan was able to write any cheques on the Taylor Inc. account. He would in some cases *prepare* cheques but Mr. Taylor would sign them.

27 At the hearing for this application Mr. Taylor testified as to what he remembered about the money orders. His evidence is vague and self-serving. Even so, he cannot bring himself to *completely* deny knowing anything about the money orders, so instead he blames members of the legal community and professionals who he said received this money. In short, while he remembers the money coming into and leaving Taylor Inc., Dwayne Taylor denies he was the ultimate recipient of these funds. He provides no particulars about who the payee was on these large money orders. I find that incredible and reject it.

28 The exclusive knowledge and factual possession by Mr. Taylor means he could easily show where this money went. The suspicious circumstances here lead me to conclude that Mr. Taylor purchased money orders, if not directly to himself, then instead to an entity or third-party over which he had full and complete control. Directly or indirectly, Mr. Taylor received this money.

29 He may later have spent some in an attempt to prove a $10 million mortgage penalty arising out of his claim in the main action, but that does not make the money any less attributable to him or to his order or benefit. Despite Mr. Chan's general lack of credibility I accept that he did not receive any of these monies.

5. Analysis and Conclusion

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

30 I find on a balance of probabilities that in May 2000 Dwayne Taylor removed $490,013.50 from his company Taylor Inc., at a time when Taylor Inc. was insolvent. I have concluded that one way or another Dwayne Taylor ended up with the $490,013.50.

31 That satisfies the criteria of *FPA*, s. 2; Dwayne Taylor paid himself in priority over another creditor, Louis Bull.

32 The next question is whether Mr. Taylor had any right at all to that money. Here Louis Bull takes a fair, reasonable and generous position. A strong argument can be made that Mr. Dwayne Taylor was not a creditor of the company; he received various monies by usual and ordinary cheque transfers throughout the history of Taylor Inc. If so, Louis Bull would be entitled to the entire monies.

33 Louis Bull however concedes that despite the strong inference that Mr. Taylor was fully paid by the cheque transfers, it accepts that Dwayne Taylor was a comparable creditor for the monies he took. In short, that means Louis Bull accepts that Mr. Taylor would have been attracting a compensation package of over $100,000.00 a month over and above the other payments by cheque in the ordinary course of business.

34 The forensic expert at the original trial felt the monies taken by Taylor Inc. from Louis Bull were ludicrous as compensation for Taylor Inc.'s work efforts. That same argument could be made for the diversion of funds from the company to Mr. Taylor. Dwayne Taylor is a businessman. He operated an A&W franchise at one point, was perhaps a partner in a lumberyard at another, and generally made a living as a retail merchant businessman. He exhibits no special training, professional status, or credentials. He caught the Louis Bull tribe at a particularly vulnerable time (see *Taylor v. Louis Bull #1*, Schedule 1) and rode their vulnerability to the point that he nearly bankrupted them.

35 There is therefore a strong inference that he was *not* entitled to any of that money, but I accept Louis Bull's analysis that it cannot, on a balance of probabilities, do anything more than proved that they were creditors of Taylor Inc. and give Mr. Taylor the benefit of the doubt and conclude that he too had that same status.

36 Recent cases of our court indicates the criteria for fraudulent preference: *Don Forsey & Blackfalds Investments Ltd. v. Hydro Kleen Systems Inc., Titan Investments Ltd. Partnership, Re, Shengli Oilfield Freet Petroleum Equipment Co. v. Ascension Virtual Group Ltd.*. It is a common sense approach. One creditor who has an inroad into the debtor diverts to himself assets that should be shared by all creditors. That is a fraudulent preference when the transfer occurs during a time when the debtor is insolvent.

37 I find on a balance of probabilities that in May 2000 Dwayne Taylor removed $490,013.50 from his company Taylor Inc., at a time when Taylor Inc. was insolvent. That satisfies the criteria of *FPA*, s. 2; Dwayne Taylor paid himself in priority over another creditor, Louis Bull.

38 In coming to that conclusion I give Dwayne Taylor the benefit of the doubt (one which some may argue unreasonably generously) that he may have also been a creditor for the amount of money that he took for himself. He gets this benefit primarily because the trail has gone cold and it is difficult for Louis Bull to prove the contrary.

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

39 Given my conclusion I do not need to consider the *Statute of Elizabeth*. That said, I do not think that legislation applies here because Louis Bull has, in effect, admitted that Mr. Taylor has a claim for unpaid services worth nearly half a million dollars. That means the money orders were in exchange for substantial unpaid services, and not for "no or nominal consideration", the second requirement identified in *Palechuk v. Fahrlander*, at para. 31.

40 What remains is assessing the relative claims of Dwayne Taylor and the Louis Bull. As of February 28, 2010 Taylor Inc. is indebted to Louis Bull in an amount equal to $520,769.67. Mr. Taylor is presumptively owed $490,013.50, the amount he removed for his own benefit. Together, Taylor Inc.'s debt is $1,010,783.17; Louis Bull's share is 51.5%.

41 I have concluded that Dwayne Taylor improperly (based on the *FPA*) took $490,013.50 from Taylor Inc. That transaction is reversed under *FPA*, s. 2, Taylor Inc. is owed $490,013.50 by Dwayne Taylor.

42 As a creditor of Taylor Inc. Louis Bull is entitled to 51.5% of the amounts preferred to Dwayne Taylor or $252,356.96. Therefore Louis Bull has additional judgment against Dwayne Taylor, based on fraud, in the amount of $252,356.96, which they may add to their outstanding balance of $91,126.38.

6. The Costs of Louis Bull

43 Louis Bull was successful in this litigation. Louis Bull is entitled to their costs of these proceedings, on the basis of Schedule C, Column 5 of the *Alberta Rules of Court*, plus their litigation disbursements.

Application granted.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 32

2006 ABQB 630
Alberta Master

Mako Megbiz, K.F.T. v. Osprey Energy Ltd.

2006 CarswellAlta 1111, 2006 ABQB 630, [2006] A.W.L.D. 3111, 405 A.R. 165, 63 Alta. L.R. (4th) 115

Mako Megbiz, K.F.T. (Applicant) and Osprey Energy Ltd. and 1064702 Alberta Ltd. (Respondents)

Master J.B. Hanebury

Heard: May 24, 2006
Judgment: August 25, 2006
Docket: Calgary 0401-01651

Counsel: Jeff Moroz for Applicant
Jennifer L. Smith for Respondent

Subject: Contracts; Corporate and Commercial; Torts; Insolvency

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Debtors and creditors — Fraudulent preferences — Intention to prefer

Energy company defaulted on loan secured by debenture to creditor which obtained judgment against company — Energy company was in dire financial straits and its auditors demanded to be paid $55,000 before they would sign their audit which company required in order not to be de-listed from stock exchange — Energy company assigned interest in some petroleum producing properties ("assignment") to shell company owned by auditors — Secured judgment creditor brought application to set aside assignment as fraudulent preference pursuant to ss. 2 and 3 of Fraudulent Preferences Act — Application dismissed — Requirements of s. 3 of Act were not met, since application was not brought within one year after assignment was made — Requirements of s. 2 of Act were not met, since evidence showed that dominant intent of energy company was to stay in business despite other evidence which showed intent to prefer auditors' shell company over other creditors — Auditors knew that energy company was in dire financial straits and were determined to protect their outstanding receivable by taking assignment which showed number of badges of fraud and some intent of energy company to prefer auditors' shell company over other creditors — Assignment was back-dated and done hastily, in secret, with numbered company, and for consideration that did not clearly match up with value of receivable — Intent of preferring auditors' shell company was not dominant intent, since evidence also showed energy company primarily wanted to turn around and become profitable, needed signed audit in order not to be de-listed from stock exchange, and actually continued operation for further 18 months.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Table of Authorities

Cases considered by *Master J.B. Hanebury*:

Alberta (Director of Employment Standards) v. Sanche (1992), 5 Alta. L.R. (3d) 243, 15 C.B.R. (3d) 58, (sub nom. *Evans (Bankrupt), Re)* 134 A.R. 149, 1992 CarswellAlta 293 (Alta. Q.B.) — referred to

Barnett, Re (1983), 1983 CarswellAlta 250, 46 C.B.R. (N.S.) 211, 43 A.R. 215 (Alta. Q.B.) — referred to

Coast Wire Rope & Supply Ltd. (Trustee of) v. Trans Pacific Hardware Inc. (1999), 1999 CarswellBC 638, (sub nom. *Coast Wire Rope & Supply Ltd. (Bankrupt) v. Trans Pacific Hardware Inc.)* 122 B.C.A.C. 257, (sub nom. *Coast Wire Rope & Supply Ltd. (Bankrupt) v. Trans Pacific Hardware Inc.)* 200 W.A.C. 257, 1999 BCCA 217, 9 C.B.R. (4th) 255 (B.C. C.A.) — considered

Dwyer v. Fox (1996), 43 Alta. L.R. (3d) 63, 190 A.R. 114, 1996 CarswellAlta 727 (Alta. Q.B.) — referred to

Grep Properties (II) Ltd. v. 371154 Alberta Inc. (1995), 1995 CarswellAlta 432, 34 Alta. L.R. (3d) 210, 175 A.R. 361 (Alta. Q.B.) — considered

Krumm v. McKay (2003), 47 C.B.R. (4th) 38, 2003 ABQB 437, 2003 CarswellAlta 961, [2003] 9 W.W.R. 442, 342 A.R. 169, 17 Alta. L.R. (4th) 103 (Alta. Q.B.) — considered

Stephen v. J.B. Creative Office Interiors Ltd. (1985), 1985 CarswellAlta 728 (Alta. Q.B.) — considered

Statutes considered:

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

Pt. IV — referred to

s. 38 — considered

s. 69 — referred to

s. 69.4 [en. 1992, c. 27, s. 36(1) — considered

ss. 91-101 — referred to

Fraudulent Preferences Act, R.S.A. 2000, c. F-24
Generally — referred to

s. 2 — considered

s. 3 — considered

Rules considered:

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Alberta Rules of Court, Alta. Reg. 390/68
R. 383 — considered

Tariffs considered:

Alberta Rules of Court, Alta. Reg. 390/68
Sched. C, Tariff of Costs, column 1 — referred to

APPLICATION by secured judgment creditor to set aside assignment as fraudulent preference.

***Master J.B. Hanebury*:**

1 This application concerns a failing company, some accountants eager to be paid, and a judgment creditor trying to collect 1.6 million dollars. In November, 2003, Osprey Energy Ltd. was in dire financial straits and its auditors, Dick Cook Schulli, were demanding that they be paid before they were prepared to sign their audit. In order to get paid, the principals of the auditors set up a shell company, 1064702 Alberta Ltd., and Osprey assigned to the shell company its interest in some petroleum producing properties in Alberta operated by ConocoPhillips Canada Ltd. With that arrangement made, Dick Cook Schulli completed its audit and then resigned as Osprey's auditors.

2 In February, 2004, Mako Megbiz, K.F.T., a judgment creditor of Osprey, served a garnishee on ConocoPhillips for Osprey's share of the income from the same properties. Mako Megbiz and 1064702 are now arguing over who is entitled to that income. Mako Megbiz alleges that the assignment to 1064702 was a fraudulent preference. 1064702 says Mako Megbiz has no right to bring this application, denies that there was a fraudulent preference and says it was merely a situation where auditors were trying to get their account paid. Meanwhile, in 2005, Osprey sought the protection of a proposal under the *Bankruptcy and Insolvency Act*.

3 There are three issues to be decided:

(a) Has Mako Megabiz complied with the requirements under the *Bankruptcy and Insolvency Act* that are necessary to bring this application?

(b) If it has, then is Mako Megabiz able to proceed with this application in light of its acceptance of the provisions of the proposal of Osprey that waive reliance on the fraudulent settlements sections of the *Bankruptcy and Insolvency Act*?

(c) If it can, then was the assignment by Osprey to 1064702 a fraudulent preference?

Facts

4 In 2002, Osprey was indebted to Mako Megabiz for approximately 1.5 million dollars for a loan which was secured by a

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

debenture. Osprey defaulted on the loan and in May, 2003, Mako Megbiz filed a statement of claim in Ontario. Osprey filed no defence and a judgment with costs was entered in favour of Mako Megbiz, in Ontario, on September 23rd, 2003. On January 30th, 2004, Mako Megbiz registered the judgment in Alberta and on February 4th, 2004 filed a writ of enforcement. Mako Megbiz was the only judgment creditor of Osprey in Alberta. Mako Megbiz then served a garnishee summons on ConocoPhillips, for funds owing to Osprey pursuant to its working interest in a petroleum production facility operated by ConocoPhillips.

5 1064702 said that the parties to the assignment agreement between it and Osprey started signing the document in November, 2003, and by the closing date of January 15, 2004, it had been signed by all parties. It was made effective as of September 1st, 2003. The consideration for the assignment was $75,000, which, the agreement says, was paid by way of an offset of accounts owing by Osprey. The agreement also says that the consideration for the assignment was 1064702 providing accounting services to Osprey. In March, 2004, ConocoPhillips was served with notice of the assignment by Osprey to 1064702.

6 Despite service of the assignment, in 2004 and 2005 funds were paid into court by ConocoPhillips and then out to Mako Megbiz pursuant to its garnishee summons. So, in the summer of 2005, 1064702 intervened in Mako Megbiz's Alberta action and alleged that it was the party entitled to the money paid from the working interest as a result of the assignment from Osprey of its interest in the production.

7 After this arrangement Osprey operated for a further 18 months and then sought the shelter of a proposal under the bankruptcy legislation. Mako Megbiz voted for the proposal, which was ultimately approved by all of Osprey's creditors and the Supreme Court of British Columbia. It filed a proof of claim in the proposal for the amount of its judgment.

8 In 1064702's application to set aside Mako Megbiz's garnishee summons, Mako Megbiz argued that the assignment by Osprey to 1064702 was a fraudulent preference. Master Laycock held that Mako Megbiz required leave of the bankruptcy court if it wished to seek a declaration that the conveyance was a fraudulent preference. He ordered that the funds continue to be paid into court and held there to allow Mako Megbiz to apply for leave to lift the stay of proceedings that was put in place with the filing of the proposal by Osprey pursuant to the *Bankruptcy & Insolvency Act.*

9 On January 25th, 2006, Registrar Patterson of the Supreme Court of British Columbia lifted the stay of Mako Megbiz's proceedings and permitted it to bring this application. As a result, Mako Megbiz is now before this court seeking to set aside the assignment of Osprey's interest in the Alberta petroleum producing properties, alleging it was a fraudulent preference.

Has Mako Megabiz complied with the requirements of the *Bankruptcy and Insolvency Act* necessary to bring this application?

10 1064702 first argues that Mako Megbiz cannot proceed with its application as it has failed to satisfy the requirements of s. 38 of the *Bankruptcy and Insolvency Act.*. Section 38 sets out the steps to be taken by a creditor when a trustee has refused to take a proceeding that the creditor believes would be for the benefit of the estate. The creditor can seek leave to do so on behalf of the trustee. The creditor must meet certain requirements and obtain an order requiring the trustee to transfer its right in the proceeding to the creditor.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

11 In this case, Master Laycock required Mako Megbiz to seek an order under s. 69.4 of the *Bankruptcy and Insolvency Act* for leave to proceed with its application. Section 69 provides that a proposal stays proceedings involving the bankrupt. However, a creditor can apply under s. 69.4 to lift that stay in relation to its proceedings if it demonstrates that the creditor is likely to be materially prejudiced by the continuation of the stay, or, it is equitable that the stay is lifted.

12 Mako Megbiz's applied under s. 69.4, as it was directed to do, and Registrar Patterson found that it was equitable to lift the stay and allow Mako Megbiz to proceed with its application. The Registrar did not consider s. 38 of the Act, nor did she need to. Section 69.4 involves the lifting of a stay in relation to a creditor's own litigation and the creditor can proceed with its action in its own name. Section 38 provides for the situation where the trustee has refused to act in relation to litigation that a creditor believes would be beneficial to the estate. If the creditor is prepared to proceed with the litigation on the trustee's behalf, the court can require the trustee to assign it to the creditor. Section 38 is not relevant to the factual situation before me.

13 1064702 then argues that Mako Megbiz is not a creditor and so cannot bring this application. It says that when Mako Megbiz accepted Osprey's proposal it no longer qualified as a creditor of Osprey. No legislation or case law was cited to support that proposition. This argument is circular and would gut the purpose of s. 69.4 of the Act. There would be no purpose in the lifting of a stay to allow a creditor to continue its action if a creditor were no longer a creditor.

Is Mako Megbiz able to proceed with this application in light of the provisions of the proposal that waive reliance on the fraudulent settlements sections of the *Bankruptcy and Insolvency Act*?

14 The next preliminary argument of 1064702 is that, by accepting the proposal of Osprey, Mako Megbiz is bound by its terms that preclude the trustee from relying on sections 91 to 101 inclusive of the *Bankruptcy and Insolvency Act.* Those sections are found in Part IV of the Act and deal with the trustee's rights in relation to settlements and preferences of the bankrupt's property. The response to this argument is straightforward. Mako Megbiz is not the trustee and is not acting on behalf of the trustee. The prohibition in the proposal is not effective against Mako Megbiz. As none of these preliminary arguments have met with success, I turn next to the merits of the substantive question before the court.

Was the assignment to 1064702 a fraudulent preference?

15 In *Krumm v. McKay*, [2003] A.J. No. 724 (Alta. Q.B.), the court concurred with the author of *Creditor-Debtor Law in Canada* (2nd Edition) Carswell, C.R.B. Dunlop, at page 598, where he stated that the purpose of the *Fraudulent Preferences Act* is to "strike down all conveyances of property made with the intention of defrauding crditors, except for conveyances made for good consideration and bona fide to persons not having notice of fraud". The court agreed that the legislation is to be interpreted liberally. Mako Megbiz is relying on the *Fraudulent Preferences Act*, R.S.A. 2000 c. F-24, sections 2 and 3. As s. 3 is less stringent in its requirements then s. 2, it will be considered first.

16 Section 3 states that if, within a year of a transfer, an action is commenced to set it aside, the complaining creditor must only demonstrate that the debtor is insolvent and that the effect of the transfer is a preference. The complaining creditor does not need to prove any actual intent to fraudulently prefer one creditor over another.

17 1064702 argues that Mako Megbiz cannot rely on s. 3 of the Act, as it did not bring an action within one year of the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

assignment to 1064702 of Osprey's interest in the petroleum producing properties. 1064702 relies on the decision of McIntyre J. in *Grep Properties (II) Ltd. v. 371154 Alberta Inc.*, [1995] A.J. No. 843 (Alta. Q.B.). In that case, as in the case before me, the creditor sought to set aside the alleged fraudulent transaction by way of an application pursuant to rule 383 of the Rules of Court. The notice of motion was filed more than one year after the date of the alleged fraudulent transaction. Therefore, to meet the requirements of s. 3 of the Act, the creditor relied on the original statement of claim as the "action" that was brought within one year of the transaction. The court held that the statement of claim was not an action within the meaning of s. 3 of the Act as it was not an action brought to impeach or set aside the transaction. The facts and relief pleaded in the action did not support such a characterization.

18 In response, Mako Megbiz argues that it is not required to bring an action; its application is within Mako Megbiz's existing action against Osprey and the registration of its judgment in Alberta. It relies on the decision of Master Funduk in *Stephen v. J.B. Creative Office Interiors Ltd.*, [1985] A.J. No. 370 (Alta. Q.B.). In that case the court held that where a creditor has already obtained a judgment against a debtor, the creditor does not need to start a fresh action against the debtor and the assignee to impeach the assignment. The creditor can bring an application under r. 383 of the Rules of Court and rely on the provisions of s. 3 of the Act. This is what Mako Megbiz has done in this case.

19 Mako Megbiz is correct. *Stephen* stands for the proposition that an application under rule 383 is sufficient to come within the requirements of s. 3 of the Act. *Grep* does not overturn that proposition; it says that when that application under rule 383 is brought outside the one year limitation period, the action relied upon by the creditor to meet the requirements of s. 3 of the Act must be an action that seeks, as part of its requested relief, the setting aside of the fraudulent transaction. In this case, as in *Grep*, the application under rule 383 was brought over a year after the attacked transaction and the statement of claim and extra-provincial registration of judgment make no mention of an alleged fraudulent transaction by Osprey. Mako Megbiz cannot rely on s. 3 of the act as its requirements have not been met.

20 Mako Megbiz then turns to s. 2 of the Act. It states:

> Subject to sections 6 to 9, every gift, conveyance, transfer, delivery over or payment of goods, chattels or effects of bills, bonds, notes or securities or of shares, dividends, premiums or bonus in any bank, company or corporation or of any other property, real or personal, made
>
> > (a) by a person at a time when the person is in insolvent circumstances or is unable to pay the person's debts in full or knows that the person is on the eve of insolvency, and
> >
> > (b) to or for a creditor with intent to give that creditor preference over the other creditors of the debtor or over any one or more of them,
>
> is void as against the creditor or creditors injured, delayed, prejudiced or postponed.

21 Osprey meets the first part of the test, as at the time of the assignment to 1064702 it was unable to pay its debts in full as it was unable to pay Mako Megbiz the amount outstanding pursuant to its loan.

22 The second part of the test requires an intent to give 1064702 a preference over Mako Megbiz or other creditors. The evidence establishes that in 2003, 1064702 was aware that Osprey was millions of dollars "in the red", or, as Mr. Schulli, a partner with Osprey's auditors and the witness for 1064702, put it, in "dire financial straits". The principles of 1064702 had

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

seen the Management Discussion and Analysis that accompanied the June 2003 financial statements. It said:

> ...Due to inadequate funding the debentures are again in arrears and in default and one holder has obtained a judgment for his interest in arrears. This judgment further makes funding the Company difficult at best...In recognition of the limited production in the U.S. properties (Due to lack of funds) and in accordance with conservative accounting principles, the Company has substantially written off most of the value of its properties. In addition, due to the lack of funds the Company has abandoned its participation in the Prince Edward Island and Nova Scotia projects...We did have a discovery in Western Louisiana, The Woodlawn Field Augustine #1 well, and expect cash flow in the later part of fiscal 2004, once the well reaches pay out.
>
> .....
>
> Outlook: The Company continues to negotiate with its two debenture holders. It is obvious that their cooperation will be necessary to "turn" the company around. In addition, management will continue to seek funds to accomplish the plans for the two remaining fields. We do need to point out that the reserves in both fields are still there, but need funding to be realized. Management believes that all changes necessary for the "turn" around are in place except the necessary negotiations with the debenture holders and the funding. If we all pull together we are hopeful that the Company can become profitable and successful. We appreciate the support of all of our shareholders, employees and creditors.

23 The principals of Dick Cook Schulli were concerned and determined that their outstanding receivable of approximately $55,000 be protected. Mr. Schulli confirmed that Osprey was listed on the Toronto Stock Exchange and without an audit, it would be de-listed. Clearly, the auditors had the upper hand. Mr. Schulli said that Dick Cook Schulli "negotiated a routine business transaction" with Osprey whereby the auditors set up a shell company for the sole purpose of receiving an assignment from Osprey of its interest in the ConocoPhillips properties. The auditors assigned their receivable to the shell company for nominal consideration. The receivable was then satisfied by Osprey's assignment of its interest in the ConocoPhillips petroleum properties. Osprey's interest is valued in the agreement at $75,000. Mr. Schulli said that he assumes that a cheque was written to Osprey for the difference between that amount and the $55,000 owing for the receivable. With this arrangement made, at the end of November, 2003, the auditors signed the audit for the financial period ending June 30, 2003, and then resigned as Osprey's auditors.

24 Under questioning, Mr. Schulli admitted that it is not "routine" for a public company's auditor to enter into transactions with a company it audits, however he pointed out that the firm itself did not enter into the transaction. He said that auditors can enter into business transactions with respect to audit clients when it comes to providing services and getting paid for those services. He concluded by commenting that "there was a business transaction undertaken, and the purposes and the reasons for that business transaction were solely the business of the two parties involved in that business transaction".

25 The evidence before me is sufficient to find that 1064702 had an intent to prefer itself over Osprey's other creditors. The principals behind the company were well positioned to know of the desperate situation of Osprey; they knew that the company was insolvent and they were focussed on putting into place an arrangement to ensure that their debt was paid despite the claims of other creditors.

26 However, to meet the test under s. 2 of the *Fraudulent Preferences Act*, there must also be an intent by Osprey to prefer 1064702 over its other creditors. 1064702 argued that for the test to be met, the intent to prefer a creditor must be the debtor's dominant intent. Where the debtor's dominant intent is to keep its business going, a preference given to one creditor over another is not a fraudulent preference. 1064702 relied on a number of cases in support of this proposition: *Dwyer v. Fox*, [1996] A.J. No. 769 (Alta. Q.B.), *Alberta (Director of Employment Standards) v. Sanche*, [1992] A.J. No. 910 (Alta. Q.B.), *Coast Wire Rope & Supply Ltd. (Trustee of) v. Trans Pacific Hardware Inc.*, [1999] B.C.J. No. 748 (B.C. C.A.).

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

27 In *Debtor-Creditor Law in Canada*, Dunlop says at pages 629 and 630, that for the impugned assignment to be struck down the dominant intention of the transferor must be to prefer the creditor to whom the impugned assignment is made. He notes that there are many motives other than the desire to prefer that can remove a transaction from fraudulent preference legislation. Frequently the debtor yields to a pressing creditor demanding security. He says that the transaction will not be struck down where the debtor has made the conveyance in order to continue in business and meet its obligations, rather than to prefer a favoured creditor.

28 In *Coast Wire* the court held that the intention of the debtor is to be determined objectively and not subjectively. In deciding the dominant intention of the debtor, the reasonableness of the asserted intention to stay in business must be shown on a balance of probabilities.

29 In *Barnett, Re*, [1983] A.J. No. 909 (Alta. Q.B.), the debtor transferred a cottage to a "good acquaintance" at a bargain price. The purchaser did not examine the property and sought no valuation. The debtor continued to use the cottage and the purchaser was rarely, if ever, there. The court found that the purchaser knew that the debtor's creditors would be looking to the cottage to help pay their claims and he helped his friend to save the property from them. The court also found that the debtor could not get funds on mortgages at a reasonable rate of interest and his principal intention was to pay off a certain mortgage and to secure some funds for other debts, apparently related to a business he had. His dominant intent was not to give a preference to the purchaser, who the court noted, was not a creditor in any event.

30 I agree with the proposition of 1064702 that the dominant intent of Osprey must be determined, and if that dominant intent was to save its business, this application must fail. The first question to be determined is whether there was an intent by Osprey to prefer 1064702 over its other creditors.

31 No evidence was filed by Osprey or by the trustee on its behalf. In *Dwyer*, the court found that where direct evidence of the intent of the debtor to prefer one creditor over another was insufficient, the court could look to the badges of fraud to determine if the necessary intent existed. The badges of fraud are described by Dunlop in *Creditor-Debtor Law in Canada* at p. 613 and include the following:

(a) the transaction was secret;

(b) the transfer was made pending the writ;

(c) the deed contained self-serving provisions such as "the gift was made honestly, truly, and bona fide";

(d) the deed contains false statements as to the consideration;

(e) the consideration is grossly inadequate;

(f) there is unusual haste to make the transfer; and

(g) a close relationship exists between the parties to the conveyance

32 In the case before me a number of the badges of fraud are present. The transaction was done in secret with a numbered company. It was done hastily and back-dated. The consideration does not clearly match up with the value received. The assignment includes the statement that the transfer is "in consideration of the Purchaser providing accounting services to the

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Vendor". The numbered company did not provide accounting services to Osprey and Dick Cook Schulli resigned as auditors once this arrangement was made. Furthermore, Mr. Schulli was not able to state that a cheque for the difference between the outstanding receivable and the value of the asset was paid to Osprey. Looking at these badges of fraud, I am satisfied that Osprey had an intent to prefer 1064702 over its other creditors.

33 However, Mr. Schulli's evidence also indicates that Osprey would be de-listed from the stock exchange if its auditors would not complete their audit of the June 30, 2003 statements. Those statements showed that Osprey had sustained a material loss of $8,732,805 and had an accumulated deficit of $16,015,830. It had a working capital deficiency of $3,963,088. The company expected some unquantified future income from a property in Louisiana and there were other reserves, although no money to develop them. As noted earlier, Osprey said in its Management Discussion and Analysis that it was negotiating with major creditors and "[m]anagement believes that all changes necessary for the 'turn' around are in place except the necessary negotiations with the debenture holders and the funding". It added that "[i]f we all pull together we are hopeful that the Company can become profitable and successful". Osprey obviously hoped to still have a future.

34 These statements by Osprey, filed with its financial statements; the evidence of Schulli as to the critical importance to Osprey that its financial statements be filed; the essential role the principals of Dick Cook Schulli played in making this happen; and the fact that Osprey did carry on for a further 18 months before going into protection under the *Bankuptcy and Insolvency Act*, have convinced me that the dominant intent of Osprey when it provided the assignment to 1064702, was to stay in business.

35 As a result, I must dismiss this application. To be successful under s. 2 of the *Fraudulent Preferences Act*, a dominant intent by the debtor to prefer the creditor must be found, and I am unable to do so.

36 1064702 is entitled to its costs of this application under column 1. If the parties cannot agree as to those costs or wish to seek further direction in relation to the monies paid into court they may do so within 30 days of the date of this decision.

Application dismissed.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Tab 33

2010 ONSC 222
Ontario Superior Court of Justice [Commercial List]

Canwest Publishing Inc./Publications Canwest Inc., Re

2010 CarswellOnt 212, 2010 ONSC 222, [2010] O.J. No. 188, 184 A.C.W.S. (3d) 684, 63 C.B.R. (5th) 115

IN THE MATTER OF THE COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, C-36, AS AMENDED AND IN THE MATTER OF A PROPOSED PLAN OF COMPROMISE OR ARRANGEMENT OF CANWEST PUBLISHING INC./PUBLICATIONS CANWEST INC., CANWEST BOOKS INC. AND CANWEST (CANADA) INC.

Pepall J.

Judgment: January 18, 2010
Docket: CV-10-8533-00CL

Counsel: Lyndon Barnes, Alex Cobb, Duncan Ault for Applicant, LP Entities
Mario Forte for Special Committee of the Board of Directors
Andrew Kent, Hilary Clarke for Administrative Agent of the Senior Secured Lenders' Syndicate
Peter Griffin for Management Directors
Robin B. Schwill, Natalie Renner for Ad Hoc Committee of 9.25% Senior Subordinated Noteholders
David Byers, Maria Konyukhova for Proposed Monitor, FTI Consulting Canada Inc.

Subject: Insolvency; Corporate and Commercial

Related Abridgment Classifications
For all relevant Canadian Abridgment Classifications refer to highest level of case via History.

Headnote

Bankruptcy and insolvency --- Companies' Creditors Arrangement Act — Miscellaneous

CMI, entity of C Corp., obtained protection from creditors in Companies' Creditors Arrangement Act ("CCAA") proceedings in October 2009 — CPI, newspaper entities related to C, sought similar protection — CPI brought application for order pursuant to CCAA and for stay of proceedings and other benefits of order to be extended to CPI — Application granted — CPI was clearly insolvent — Community served by CPI was huge — Granting of order premised on anticipated going concern sale of newspaper business, which would serve interests of CPI and stakeholders and also community at large — Order requested would provide stability and enable CPI to pursue restructuring and preserve enterprise value for stakeholders — Without benefit of stay, CPI would have been required to pay approximately $1.45 billion and would have been unable to continue operating business.

Bankruptcy and insolvency --- Companies' Creditors Arrangement Act — Arrangements — Approval by creditors

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

CMI, entity of C Corp., obtained protection from creditors in Companies' Creditors Arrangement Act ("CCAA") proceedings in October 2009 — CPI, newspaper entities related to C, sought similar protection — CPI brought application for order pursuant to CCAA and for stay of proceedings and other benefits of order to be extended to CPI — Application granted — CPI was clearly insolvent — Community served by CPI was huge — Granting of order premised on anticipated going concern sale of newspaper business, which would serve interests of CPI and stakeholders and also community at large — Order requested would provide stability and enable CPI to pursue restructuring and preserve enterprise value for stakeholders — Without benefit of stay, CPI would have been required to pay approximately $1.45 billion and would have been unable to continue operating business — In circumstances, it was appropriate to allow CPI to file and present plan only to secured creditors.

Table of Authorities

Cases considered by *Pepall J.*:

Anvil Range Mining Corp., Re (2002), 2002 CarswellOnt 2254, 34 C.B.R. (4th) 157 (Ont. C.A.) — considered

Anvil Range Mining Corp., Re (2003), 310 N.R. 200 (note), 2003 CarswellOnt 730, 2003 CarswellOnt 731, 180 O.A.C. 399 (note) (S.C.C.) — referred to

Canwest Global Communications Corp., Re (2009), 2009 CarswellOnt 6184, 59 C.B.R. (5th) 72 (Ont. S.C.J. [Commercial List]) — followed

Grant Forest Products Inc., Re (2009), 2009 CarswellOnt 4699, 57 C.B.R. (5th) 128 (Ont. S.C.J. [Commercial List]) — considered

Lehndorff General Partner Ltd., Re (1993), 17 C.B.R. (3d) 24, 9 B.L.R. (2d) 275, 1993 CarswellOnt 183 (Ont. Gen. Div. [Commercial List]) — referred to

Muscletech Research & Development Inc., Re (2006), 19 C.B.R. (5th) 54, 2006 CarswellOnt 264 (Ont. S.C.J. [Commercial List]) — followed

Philip Services Corp., Re (1999), 13 C.B.R. (4th) 159, 1999 CarswellOnt 4673 (Ont. S.C.J. [Commercial List]) — considered

Sierra Club of Canada v. Canada (Minister of Finance) (2002), 287 N.R. 203, (sub nom. *Atomic Energy of Canada Ltd. v. Sierra Club of Canada)* 18 C.P.R. (4th) 1, 44 C.E.L.R. (N.S.) 161, (sub nom. *Atomic Energy of Canada Ltd. v. Sierra Club of Canada)* 211 D.L.R. (4th) 193, 223 F.T.R. 137 (note), 20 C.P.C. (5th) 1, 40 Admin. L.R. (3d) 1, 2002 SCC 41, 2002 CarswellNat 822, 2002 CarswellNat 823, (sub nom. *Atomic Energy of Canada Ltd. v. Sierra Club of Canada)* 93 C.R.R. (2d) 219, [2002] 2 S.C.R. 522 (S.C.C.) — followed

Statutes considered:

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — referred to

s. 4 — considered

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

s. 5 — considered

s. 11.2 [en. 1997, c. 12, s. 124] — considered

s. 11.2(1) [en. 1997, c. 12, s. 124] — considered

s. 11.2(4) [en. 1997, c. 12, s. 124] — considered

s. 11.4 [en. 1997, c. 12, s. 124] — considered

s. 11.4(1) [en. 1997, c. 12, s. 124] — considered

s. 11.4(2) [en. 1997, c. 12, s. 124] — considered

s. 11.7(2) [en. 1997, c. 12, s. 124] — referred to

s. 11.51 [en. 2005, c. 47, s. 128] — considered

s. 11.52 [en. 2005, c. 47, s. 128] — considered

Courts of Justice Act, R.S.O. 1990, c. C.43
s. 137(2) — considered

APPLICATION by entity of company already protected under Companies' Creditors Arrangement Act for similar protection.

***Pepall J.*:**

Reasons for Decision

Introduction

1 Canwest Global Communications Corp. ("Canwest Global") is a leading Canadian media company with interests in (i) newspaper publishing and digital media; and (ii) free-to-air television stations and subscription based specialty television channels. Canwest Global, the entities in its Canadian television business (excluding CW Investments Co. and its subsidiaries) and the National Post Company (which prior to October 30, 2009 owned and published the National Post) (collectively, the "CMI Entities"), obtained protection from their creditors in a *Companies' Creditors Arrangement Act*[1] ("CCAA") proceeding on October 6, 2009.[2] Now, the Canwest Global Canadian newspaper entities with the exception of National Post Inc. seek similar protection. Specifically, Canwest Publishing Inc./Publications Canwest Inc. ("CPI"), Canwest Books Inc. ("CBI"), and Canwest (Canada) Inc. ("CCI") apply for an order pursuant to the CCAA. They also seek to have the stay of proceedings and the other benefits of the order extend to Canwest Limited Partnership/Canwest Société en Commandite (the "Limited Partnership"). The Applicants and the Limited Partnership are referred to as the "LP Entities" throughout these reasons. The term "Canwest" will be used to refer to the Canwest enterprise as a whole. It includes the LP Entities and Canwest Global's other subsidiaries which are not applicants in this proceeding.

2 All appearing on this application supported the relief requested with the exception of the Ad Hoc Committee of 9.25% Senior Subordinated Noteholders. That Committee represents certain unsecured creditors whom I will discuss more fully

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

later.

3 I granted the order requested with reasons to follow. These are my reasons.

4 I start with three observations. Firstly, Canwest Global, through its ownership interests in the LP Entities, is the largest publisher of daily English language newspapers in Canada. The LP Entities own and operate 12 daily newspapers across Canada. These newspapers are part of the Canadian heritage and landscape. The oldest, The Gazette, was established in Montreal in 1778. The others are the Vancouver Sun, The Province, the Ottawa Citizen, the Edmonton Journal, the Calgary Herald, The Windsor Star, the Times Colonist, The Star Phoenix, the Leader-Post, the Nanaimo Daily News and the Alberni Valley Times. These newspapers have an estimated average weekly readership that exceeds 4 million. The LP Entities also publish 23 non-daily newspapers and own and operate a number of digital media and online operations. The community served by the LP Entities is huge. In addition, based on August 31, 2009 figures, the LP Entities employ approximately 5,300 employees in Canada with approximately 1,300 of those employees working in Ontario. The granting of the order requested is premised on an anticipated going concern sale of the newspaper business of the LP Entities. This serves not just the interests of the LP Entities and their stakeholders but the Canadian community at large.

5 Secondly, the order requested may contain some shortcomings; it may not be perfect. That said, insolvency proceedings typically involve what is feasible, not what is flawless.

6 Lastly, although the builders of this insolvent business are no doubt unhappy with its fate, gratitude is not misplaced by acknowledging their role in its construction.

Background Facts

(i) Financial Difficulties

7 The LP Entities generate the majority of their revenues through the sale of advertising. In the fiscal year ended August 31, 2009, approximately 72% of the LP Entities' consolidated revenue derived from advertising. The LP Entities have been seriously affected by the economic downturn in Canada and their consolidated advertising revenues declined substantially in the latter half of 2008 and in 2009. In addition, they experienced increases in certain of their operating costs.

8 On May 29, 2009 the Limited Partnership failed, for the first time, to make certain interest and principal reduction payments and related interest and cross currency swap payments totaling approximately $10 million in respect of its senior secured credit facilities. On the same day, the Limited Partnership announced that, as of May 31, 2009, it would be in breach of certain financial covenants set out in the credit agreement dated as of July 10, 2007 between its predecessor, Canwest Media Works Limited Partnership, The Bank of Nova Scotia as administrative agent, a syndicate of secured lenders ("the LP Secured Lenders"), and the predecessors of CCI, CPI and CBI as guarantors. The Limited Partnership also failed to make principal, interest and fee payments due pursuant to this credit agreement on June 21, June 22, July 21, July 22 and August 21, 2009.

9 The May 29, 2009, defaults under the senior secured credit facilities triggered defaults in respect of related foreign

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

currency and interest rate swaps. The swap counterparties (the "Hedging Secured Creditors") demanded payment of $68.9 million. These unpaid amounts rank pari passu with amounts owing under the LP Secured Lenders' credit facilities.

10 On or around August 31, 2009, the Limited Partnership and certain of the LP Secured Lenders entered into a forbearance agreement in order to allow the LP Entities and the LP Secured Lenders the opportunity to negotiate a pre-packaged restructuring or reorganization of the affairs of the LP Entities. On November 9, 2009, the forbearance agreement expired and since then, the LP Secured Lenders have been in a position to demand payment of approximately $953.4 million, the amount outstanding as at August 31, 2009. Nonetheless, they continued negotiations with the LP Entities. The culmination of this process is that the LP Entities are now seeking a stay of proceedings under the CCAA in order to provide them with the necessary "breathing space" to restructure and reorganize their businesses and to preserve their enterprise value for the ultimate benefit of their broader stakeholder community.

11 The Limited Partnership released its annual consolidated financial statements for the twelve months ended August 31, 2009 and 2008 on November 26, 2009. As at August 31, 2009, the Limited Partnership had total consolidated assets with a net book value of approximately $644.9 million. This included consolidated current assets of $182.7 million and consolidated non-current assets of approximately $462.2 million. As at that date, the Limited Partnership had total consolidated liabilities of approximately $1.719 billion (increased from $1.656 billion as at August 31, 2008). These liabilities consisted of consolidated current liabilities of $1.612 billion and consolidated non-current liabilities of $107 million.

12 The Limited Partnership had been experiencing deteriorating financial results over the past year. For the year ended August 31, 2009, the Limited Partnership's consolidated revenues decreased by $181.7 million or 15% to $1.021 billion as compared to $1.203 billion for the year ended August 31, 2008. For the year ended August 31, 2009, the Limited Partnership reported a consolidated net loss of $66 million compared to consolidated net earnings of $143.5 million for fiscal 2008.

(ii) Indebtedness under the Credit Facilities

13 The indebtedness under the credit facilities of the LP Entities consists of the following.

(a) The LP senior secured credit facilities are the subject matter of the July 10, 2007 credit agreement already mentioned. They are guaranteed by CCI, CPI and CBI. The security held by the LP Secured Lenders has been reviewed by the solicitors for the proposed Monitor, FTI Consulting Canada Inc. and considered to be valid and enforceable.[3] As at August 31, 2009, the amounts owing by the LP Entities totaled $953.4 million exclusive of interest.[4]

(b) The Limited Partnership is a party to the aforementioned foreign currency and interest rate swaps with the Hedging Secured Creditors. Defaults under the LP senior secured credit facilities have triggered defaults in respect of these swap arrangements. Demand for repayment of amounts totaling $68.9 million (exclusive of unpaid interest) has been made. These obligations are secured.

(c) Pursuant to a senior subordinated credit agreement dated as of July 10, 2007, between the Limited Partnership, The Bank of Nova Scotia as administrative agent for a syndicate of lenders, and others, certain subordinated lenders agreed to provide the Limited Partnership with access to a term credit facility of up to $75 million. CCI, CPI, and CBI are guarantors. This facility is unsecured, guaranteed on an unsecured basis and currently fully drawn. On June 20, 2009, the Limited Partnership failed to make an interest payment resulting in an event of default under the credit agreement. In addition, the defaults under the senior secured credit facilities resulted in a default under this facility. The senior subordinated lenders are in a position to take steps to demand payment.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

(d) Pursuant to a note indenture between the Limited Partnership, The Bank of New York Trust Company of Canada as trustee, and others, the Limited Partnership issued 9.5% per annum senior subordinated unsecured notes due 2015 in the aggregate principal amount of US $400 million. CPI and CBI are guarantors. The notes are unsecured and guaranteed on an unsecured basis. The noteholders are in a position to take steps to demand immediate payment of all amounts outstanding under the notes as a result of events of default.

14 The LP Entities use a centralized cash management system at the Bank of Nova Scotia which they propose to continue. Obligations owed pursuant to the existing cash management arrangements are secured (the "Cash Management Creditor").

(iii) LP Entities' Response to Financial Difficulties

15 The LP Entities took a number of steps to address their circumstances with a view to improving cash flow and strengthening their balance sheet. Nonetheless, they began to experience significant tightening of credit from critical suppliers and other trade creditors. The LP Entities' debt totals approximately $1.45 billion and they do not have the liquidity required to make payment in respect of this indebtedness. They are clearly insolvent.

16 The board of directors of Canwest Global struck a special committee of directors (the "Special Committee") with a mandate to explore and consider strategic alternatives. The Special Committee has appointed Thomas Strike, the President, Corporate Development & Strategy Implementation, as Recapitalization Officer and has retained Gary Colter of CRS Inc. as Restructuring Advisor for the LP Entities (the "CRA"). The President of CPI, Dennis Skulsky, will report directly to the Special Committee.

17 Given their problems, throughout the summer and fall of 2009, the LP Entities have participated in difficult and complex negotiations with their lenders and other stakeholders to obtain forbearance and to work towards a consensual restructuring or recapitalization.

18 An ad hoc committee of the holders of the senior subordinated unsecured notes (the "Ad Hoc Committee") was formed in July, 2009 and retained Davies Ward Phillips & Vineberg as counsel. Among other things, the Limited Partnership agreed to pay the Committee's legal fees up to a maximum of $250,000. Representatives of the Limited Partnership and their advisors have had ongoing discussions with representatives of the Ad Hoc Committee and their counsel was granted access to certain confidential information following execution of a confidentiality agreement. The Ad Hoc Committee has also engaged a financial advisor who has been granted access to the LP Entities' virtual data room which contains confidential information regarding the business and affairs of the LP Entities. There is no evidence of any satisfactory proposal having been made by the noteholders. They have been in a position to demand payment since August, 2009, but they have not done so.

19 In the meantime and in order to permit the businesses of the LP Entities to continue to operate as going concerns and in an effort to preserve the greatest number of jobs and maximize value for the stakeholders of the LP Entities, the LP Entities have been engaged in negotiations with the LP Senior Lenders, the result of which is this CCAA application.

(iv) The Support Agreement, the Secured Creditors' Plan and the Solicitation Process

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

20 Since August 31, 2009, the LP Entities and the LP administrative agent for the LP Secured Lenders have worked together to negotiate terms for a consensual, prearranged restructuring, recapitalization or reorganization of the business and affairs of the LP Entities as a going concern. This is referred to by the parties as the Support Transaction.

21 As part of this Support Transaction, the LP Entities are seeking approval of a Support Agreement entered into by them and the administrative agent for the LP Secured Lenders. 48% of the LP Secured Lenders, the Hedging Secured Creditors, and the Cash Management Creditor (the "Secured Creditors") are party to the Support Agreement.

22 Three interrelated elements are contemplated by the Support Agreement and the Support Transaction: the credit acquisition, the Secured Creditors' plan (the "Plan"), and the sale and investor solicitation process which the parties refer to as SISP.

23 The Support Agreement contains various milestones with which the LP Entities are to comply and, subject to a successful bid arising from the solicitation process (an important caveat in my view), commits them to support a credit acquisition. The credit acquisition involves an acquisition by an entity capitalized by the Secured Creditors and described as AcquireCo. AcquireCo. would acquire substantially all of the assets of the LP Entities (including the shares in National Post Inc.) and assume certain of the liabilities of the LP Entities. It is contemplated that AcquireCo. would offer employment to all or substantially all of the employees of the LP Entities and would assume all of the LP Entities' existing pension plans and existing post-retirement and post-employment benefit plans subject to a right by AcquireCo., acting commercially reasonably and after consultation with the operational management of the LP Entities, to exclude certain specified liabilities. The credit acquisition would be the subject matter of a Plan to be voted on by the Secured Creditors on or before January 31, 2010. There would only be one class. The Plan would only compromise the LP Entities' secured claims and would not affect or compromise any other claims against any of the LP Entities ("unaffected claims"). No holders of the unaffected claims would be entitled to vote on or receive any distributions of their claims. The Secured Creditors would exchange their outstanding secured claims against the LP Entities under the LP credit agreement and the swap obligations respectively for their *pro rata* shares of the debt and equity to be issued by AcquireCo. All of the LP Entities' obligations under the LP secured claims calculated as of the date of closing less $25 million would be deemed to be satisfied following the closing of the Acquisition Agreement. LP secured claims in the amount of $25 million would continue to be held by AcquireCo. and constitute an outstanding unsecured claim against the LP Entities.

24 The Support Agreement contemplates that the Financial Advisor, namely RBC Dominion Securities Inc., under the supervision of the Monitor, will conduct the solicitation process. Completion of the credit acquisition process is subject to a successful bid arising from the solicitation process. In general terms, the objective of the solicitation process is to obtain a better offer (with some limitations described below) than that reflected in the credit acquisition. If none is obtained in that process, the LP Entities intend for the credit acquisition to proceed assuming approval of the Plan. Court sanction would also be required.

25 In more detailed terms, Phase I of the solicitation process is expected to last approximately 7 weeks and qualified interested parties may submit non-binding proposals to the Financial Advisor on or before February 26, 2010. Thereafter, the Monitor will assess the proposals to determine whether there is a reasonable prospect of obtaining a Superior Offer. This is in essence a cash offer that is equal to or higher than that represented by the credit acquisition. If there is such a prospect, the Monitor will recommend that the process continue into Phase II. If there is no such prospect, the Monitor will then determine whether there is a Superior Alternative Offer, that is, an offer that is not a Superior Offer but which might nonetheless receive approval from the Secured Creditors. If so, to proceed into Phase II, the Superior Alternative Offer must be supported by Secured Creditors holding more than at least 33.3% of the secured claims. If it is not so supported, the process would be terminated and the LP Entities would then apply for court sanction of the Plan.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

26 Phase II is expected to last approximately 7 weeks as well. This period allows for due diligence and the submission of final binding proposals. The Monitor will then conduct an assessment akin to the Phase 1 process with somewhat similar attendant outcomes if there are no Superior Offers and no acceptable Alternative Superior Offers. If there were a Superior Offer or an acceptable Alternative Superior Offer, an agreement would be negotiated and the requisite approvals sought.

27 The solicitation process is designed to allow the LP Entities to test the market. One concern is that a Superior Offer that benefits the secured lenders might operate to preclude a Superior Alternative Offer that could provide a better result for the unsecured creditors. That said, the LP Entities are of the view that the solicitation process and the support transaction present the best opportunity for the businesses of the LP Entities to continue as going concerns, thereby preserving jobs as well as the economic and social benefits of their continued operation. At this stage, the alternative is a bankruptcy or liquidation which would result in significant detriment not only to the creditors and employees of the LP Entities but to the broader community that benefits from the continued operation of the LP Entities' business. I also take some comfort from the position of the Monitor which is best captured in an excerpt from its preliminary Report:

> The terms of the Support Agreement and SISP were the subject of lengthy and intense arm's length negotiations between the LP Entities and the LP Administrative Agent. The Proposed Monitor supports approval of the process contemplated therein and of the approval of those documents, but without in any way fettering the various powers and discretions of the Monitor.

28 It goes without saying that the Monitor, being a court appointed officer, may apply to the court for advice and directions and also owes reporting obligations to the court.

29 As to the objection of the Ad Hoc Committee, I make the following observations. Firstly, they represent unsecured subordinated debt. They have been in a position to take action since August, 2009. Furthermore, the LP Entities have provided up to $250,000 for them to retain legal counsel. Meanwhile, the LP Secured Lenders have been in a position to enforce their rights through a non-consensual court proceeding and have advised the LP Entities of their abilities in that regard in the event that the LP Entities did not move forward as contemplated by the Support Agreement. With the Support Agreement and the solicitation process, there is an enhanced likelihood of the continuation of going concern operations, the preservation of jobs and the maximization of value for stakeholders of the LP Entities. It seemed to me that in the face of these facts and given that the Support Agreement expired on January 8, 2010, adjourning the proceeding was not merited in the circumstances. The Committee did receive very short notice. Without being taken as encouraging or discouraging the use of the comeback clause in the order, I disagree with the submission of counsel to the Ad Hoc Committee to the effect that it is very difficult if not impossible to stop a process relying on that provision. That provision in the order is a meaningful one as is clear from the decision in *Muscletech Research & Development Inc., Re*[5]. On a come back motion, although the positions of parties who have relied bona fide on an Initial Order should not be prejudiced, the onus is on the applicants for an Initial Order to satisfy the court that the existing terms should be upheld.

Proposed Monitor

30 The Applicants propose that FTI Consulting Canada Inc. serve as the Monitor. It currently serves as the Monitor in the CMI Entities' CCAA proceeding. It is desirable for FTI to act; it is qualified to act; and it has consented to act. It has not served in any of the incompatible capacities described in section 11.7(2) of the CCAA. The proposed Monitor has an enhanced role that is reflected in the order and which is acceptable.

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

Proposed Order

31 As mentioned, I granted the order requested. It is clear that the LP Entities need protection under the CCAA. The order requested will provide stability and enable the LP Entities to pursue their restructuring and preserve enterprise value for their stakeholders. Without the benefit of a stay, the LP Entities would be required to pay approximately $1.45 billion and would be unable to continue operating their businesses.

(a) Threshold Issues

32 The chief place of business of the Applicants is Ontario. They qualify as debtor companies under the CCAA. They are affiliated companies with total claims against them that far exceed $5 million. Demand for payment of the swap indebtedness has been made and the Applicants are in default under all of the other facilities outlined in these reasons. They do not have sufficient liquidity to satisfy their obligations. They are clearly insolvent.

(b) Limited Partnership

33 The Applicants seek to extend the stay of proceedings and the other relief requested to the Limited Partnership. The CCAA definition of a company does not include a partnership or a limited partnership but courts have exercised their inherent jurisdiction to extend the protections of an Initial CCAA Order to partnerships when it was just and convenient to do so. The relief has been held to be appropriate where the operations of the partnership are so intertwined with those of the debtor companies that irreparable harm would ensue if the requested stay were not granted: *Canwest Global Communications Corp., Re*[6] and *Lehndorff General Partner Ltd., Re*[7].

34 In this case, the Limited Partnership is the administrative backbone of the LP Entities and is integral to and intertwined with the Applicants' ongoing operations. It owns all shared information technology assets; it provides hosting services for all Canwest properties; it holds all software licences used by the LP Entities; it is party to many of the shared services agreements involving other Canwest entities; and employs approximately 390 full-time equivalent employees who work in Canwest's shared services area. The Applicants state that failure to extend the stay to the Limited Partnership would have a profoundly negative impact on the value of the Applicants, the Limited Partnership and the Canwest Global enterprise as a whole. In addition, exposing the assets of the Limited Partnership to the demands of creditors would make it impossible for the LP Entities to successfully restructure. I am persuaded that under these circumstances it is just and convenient to grant the request.

(c) Filing of the Secured Creditors' Plan

35 The LP Entities propose to present the Plan only to the Secured Creditors. Claims of unsecured creditors will not be addressed.

36 The CCAA seems to contemplate a single creditor-class plan. Sections 4 and 5 state:

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> s.4 Where a compromise or an arrangement is proposed between a debtor company and its unsecured creditors or any class of them, the court may, on the application in a summary way of the company or of any such creditor or of the trustee in bankruptcy or liquidator of the company, order a meeting of the creditors or class of creditors and, it the court so determines, of the shareholders of the company, to be summoned in such manner as the court directs.
>
> s.5 Where a compromise or an arrangement is proposed between a debtor company and its secured creditors or any class of them, the court may, on the application in a summary way of the company or of any such creditor or of the trustee in bankruptcy or liquidator of the company, order a meeting of the creditors or class of creditors and, if the court so determines, of the shareholders of the company, to be summoned in such manner as the court directs.

37 Case law has interpreted these provisions as authorizing a single creditor-class plan. For instance, Blair J. (as he then was) stated in *Philip Services Corp., Re*[8] : " There is no doubt that a debtor is at liberty, under the terms of sections 4 and 5 of the CCAA, to make a proposal to secured creditors or to unsecured creditors or to both groups."[9] Similarly, in *Anvil Range Mining Corp., Re*[10], the Court of Appeal stated: "It may also be noted that s. 5 of the CCAA contemplates a plan which is a compromise between a debtor company and its secured creditors and that by the terms of s. 6 of the Act, applied to the facts of this case, the plan is binding only on the secured creditors and the company and not on the unsecured creditors."[11]

38 Based on the foregoing, it is clear that a debtor has the statutory authority to present a plan to a single class of creditors. In *Anvil Range Mining Corp., Re*, the issue was raised in the context of the plan's sanction by the court and a consideration of whether the plan was fair and reasonable as it eliminated the opportunity for unsecured creditors to realize anything. The basis of the argument was that the motions judge had erred in not requiring a more complete and in depth valuation of the company's assets relative to the claims of the secured creditors.

39 In this case, I am not being asked to sanction the Plan at this stage. Furthermore, the Monitor will supervise a vigorous and lengthy solicitation process to thoroughly canvass the market for alternative transactions. The solicitation should provide a good indication of market value. In addition, as counsel for the LP Entities observed, the noteholders and the LP Entities never had any forbearance agreement. The noteholders have been in a position to take action since last summer but chose not to do so. One would expect some action on their part if they themselves believed that they "were in the money". While the process is not perfect, it is subject to the supervision of the court and the Monitor is obliged to report on its results to the court.

40 In my view it is appropriate in the circumstances to authorize the LP Entities to file and present a Plan only to the Secured Creditors.

(D) DIP Financing

41 The Applicants seek approval of a DIP facility in the amount of $25 million which would be secured by a charge over all of the assets of the LP Entities and rank ahead of all other charges except the Administration Charge, and ahead of all other existing security interests except validly perfected purchase money security interests and certain specific statutory encumbrances.

42 Section 11.2 of the CCAA provides the statutory jurisdiction to grant a DIP charge. In *Canwest Global Communications Corp., Re*[12], I addressed this provision. Firstly, an applicant should address the requirements contained in section 11.2 (1) and then address the enumerated factors found in section 11.2(4) of the CCAA. As that list is not exhaustive,

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

it may be appropriate to consider other factors as well.

43 Applying these principles to this case and dealing firstly with section 11.2(1) of the CCAA, notice either has been given to secured creditors likely to be affected by the security or charge or alternatively they are not affected by the DIP charge. While funds are not anticipated to be immediately necessary, the cash flow statements project a good likelihood that the LP Entities will require the additional liquidity afforded by the $25 million. The ability to borrow funds that are secured by a charge will help retain the confidence of the LP Entities' trade creditors, employees and suppliers. It is expected that the DIP facility will permit the LP Entities to conduct the solicitation process and consummate a recapitalization transaction of a sale of all or some of its assets. The charge does not secure any amounts that were owing prior to the filing. As such, there has been compliance with the provisions of section 11.2 (1).

44 Turning then to a consideration of the factors found in section 11.2(4) of the Act, the LP Entities are expected to be subject to these CCAA proceedings until July 31, 2010. Their business and financial affairs will be amply managed during the proceedings. This is a consensual filing which is reflective of the confidence of the major creditors in the current management configuration. All of these factors favour the granting of the charge. The DIP loan would enhance the prospects of a viable compromise or arrangement and would ensure the necessary stability during the CCAA process. I have already touched upon the issue of value. That said, in relative terms, the quantum of the DIP financing is not large and there is no readily apparent material prejudice to any creditor arising from the granting of the charge and approval of the financing. I also note that it is endorsed by the proposed Monitor in its report.

45 Other factors to consider in assessing whether to approve a DIP charge include the reasonableness of the financing terms and more particularly the associated fees. Ideally there should be some evidence on this issue. Prior to entering into the forbearance agreement, the LP Entities sought proposals from other third party lenders for a DIP facility. In this case, some but not all of the Secured Creditors are participating in the financing of the DIP loan. Therefore, only some would benefit from the DIP while others could bear the burden of it. While they may have opted not to participate in the DIP financing for various reasons, the concurrence of the non participating Secured Creditors is some market indicator of the appropriateness of the terms of the DIP financing.

46 Lastly, I note that the DIP lenders have indicated that they would not provide a DIP facility if the charge was not approved. In all of these circumstances, I was prepared to approve the DIP facility and grant the DIP charge.

(e) Critical Suppliers

47 The LP Entities ask that they be authorized but not required to pay pre-filing amounts owing in arrears to certain suppliers if the supplier is critical to the business and ongoing operations of the LP Entities or the potential future benefit of the payments is considerable and of value to the LP Entities as a whole. Such payments could only be made with the consent of the proposed Monitor. At present, it is contemplated that such suppliers would consist of certain newspaper suppliers, newspaper distributors, logistic suppliers and the Amex Bank of Canada. The LP Entities do not seek a charge to secure payments to any of its critical suppliers.

48 Section 11.4 of the CCAA addresses critical suppliers. It states:

WestlawNext CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

> 11.4(1) On application by a debtor company and on notice to the secured creditors who are likely to be affected by the security or charge, the court may make an order declaring a person to be a critical supplier to the company if the court is satisfied that the person is a supplier of goods and services to the company and that the goods or services that are supplied are critical to the company's continued operation.
>
> (2) If the court declares the person to be a critical supplier, the court may make an order requiring the person to supply any goods or services specified by the court to the company on any terms and conditions that are consistent with the supply relationship or that the court considers appropriate.
>
> (3) If the court makes an order under subsection (2), the court shall, in the order, declare that all or part of the property of the company is subject to a security or charge in favour of the person declared to be a critical supplier, in an amount equal to the value of the goods or services supplied upon the terms of the order.
>
> (4) The court may order that the security or charge rank in priority over the claim of any secured creditor of the company.

49 Mr. Byers, who is counsel for the Monitor, submits that the court has always had discretion to authorize the payment of critical suppliers and that section 11.4 is not intended to address that issue. Rather, it is intended to respond to a post-filing situation where a debtor company wishes to compel a supplier to supply. In those circumstances, the court may declare a person to be a critical supplier and require the person to supply. If the court chooses to compel a person to supply, it must authorize a charge as security for the supplier. Mr. Barnes, who is counsel for the LP Entities, submits that section 11.4 is not so limited. Section 11.4 (1) gives the court general jurisdiction to declare a supplier to be a "critical supplier" where the supplier provides goods or services that are essential to the ongoing business of the debtor company. The permissive as opposed to mandatory language of section 11.4 (2) supports this interpretation.

50 Section 11.4 is not very clear. As a matter of principle, one would expect the purpose of section 11.4 to be twofold: (i) to codify the authority to permit suppliers who are critical to the continued operation of the company to be paid and (ii) to require the granting of a charge in circumstances where the court is compelling a person to supply. If no charge is proposed to be granted, there is no need to give notice to the secured creditors. I am not certain that the distinction between Mr. Byers and Mr. Barnes' interpretation is of any real significance for the purposes of this case. Either section 11.4(1) does not oust the court's inherent jurisdiction to make provision for the payment of critical suppliers where no charge is requested or it provides authority to the court to declare persons to be critical suppliers. Section 11.4(1) requires the person to be a supplier of goods and services that are critical to the companies' operation but does not impose any additional conditions or limitations.

51 The LP Entities do not seek a charge but ask that they be authorized but not required to make payments for the pre-filing provision of goods and services to certain third parties who are critical and integral to their businesses. This includes newsprint and ink suppliers. The LP Entities are dependent upon a continuous and uninterrupted supply of newsprint and ink and they have insufficient inventory on hand to meet their needs. It also includes newspaper distributors who are required to distribute the newspapers of the LP Entities; American Express whose corporate card programme and accounts are used by LP Entities employees for business related expenses; and royalty fees accrued and owing to content providers for the subscription-based online service provided by FPinfomart.ca, one of the businesses of the LP Entities. The LP Entities believe that it would be damaging to both their ongoing operations and their ability to restructure if they are unable to pay their critical suppliers. I am satisfied that the LP Entities may treat these parties and those described in Mr. Strike's affidavit as critical suppliers but none will be paid without the consent of the Monitor.

(f) Administration Charge and Financial Advisor Charge

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

52 The Applicants also seek a charge in the amount of $3 million to secure the fees of the Monitor, its counsel, the LP Entities' counsel, the Special Committee's financial advisor and counsel to the Special Committee, the CRA and counsel to the CRA. These are professionals whose services are critical to the successful restructuring of the LP Entities' business. This charge is to rank in priority to all other security interests in the LP Entities' assets, with the exception of purchase money security interests and specific statutory encumbrances as provided for in the proposed order.[13] The LP Entities also request a $10 million charge in favour of the Financial Advisor, RBC Dominion Securities Inc. The Financial Advisor is providing investment banking services to the LP Entities and is essential to the solicitation process. This charge would rank in third place, subsequent to the administration charge and the DIP charge.

53 In the past, an administration charge was granted pursuant to the inherent jurisdiction of the court. Section 11.52 of the amended CCAA now provides statutory jurisdiction to grant an administration charge. Section 11.52 states:

> On notice to the secured creditors who are likely to be affected by the security or charge, the court may make an order declaring that all or part of the property of the debtor company is subject to a security or charge - in an amount that the court considers appropriate - in respect of the fees and expenses of
>
> > (a) the monitor, including the fees and expenses of any financial, legal or other experts engaged by the monitor in the performance of the monitor's duties;
> >
> > (b) any financial, legal or other experts engaged by the company for the purpose of proceedings under this Act; and
> >
> > (c) any financial, legal or other experts engaged by any other interested person if the court is satisfied that the security or charge is necessary for their effective participation in proceedings under this Act.
>
> (2) The court may order that the security or charge rank in priority over the claim of any secured creditor of the company.

54 I am satisfied that the issue of notice has been appropriately addressed by the LP Entities. As to whether the amounts are appropriate and whether the charges should extend to the proposed beneficiaries, the section does not contain any specific criteria for a court to consider in its assessment. It seems to me that factors that might be considered would include:

> (a) the size and complexity of the businesses being restructured;
>
> (b) the proposed role of the beneficiaries of the charge;
>
> (c) whether there is an unwarranted duplication of roles;
>
> (d) whether the quantum of the proposed charge appears to be fair and reasonable;
>
> (e) the position of the secured creditors likely to be affected by the charge; and
>
> (f) the position of the Monitor.

This is not an exhaustive list and no doubt other relevant factors will be developed in the jurisprudence.

55 There is no question that the restructuring of the LP Entities is large and highly complex and it is reasonable to expect

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

extensive involvement by professional advisors. Each of the professionals whose fees are to be secured has played a critical role in the LP Entities restructuring activities to date and each will continue to be integral to the solicitation and restructuring process. Furthermore, there is no unwarranted duplication of roles. As to quantum of both proposed charges, I accept the Applicants' submissions that the business of the LP Entities and the tasks associated with their restructuring are of a magnitude and complexity that justify the amounts. I also take some comfort from the fact that the administrative agent for the LP Secured Lenders has agreed to them. In addition, the Monitor supports the charges requested. The quantum of the administration charge appears to be fair and reasonable. As to the quantum of the charge in favour of the Financial Advisor, it is more unusual as it involves an incentive payment but I note that the Monitor conducted its own due diligence and, as mentioned, is supportive of the request. The quantum reflects an appropriate incentive to secure a desirable alternative offer. Based on all of these factors, I concluded that the two charges should be approved.

(g) Directors and Officers

56 The Applicants also seek a directors and officers charge ("D & O charge") in the amount of $35 million as security for their indemnification obligations for liabilities imposed upon the Applicants' directors and officers. The D & O charge will rank after the Financial Advisor charge and will rank pari passu with the MIP charge discussed subsequently. Section 11.51 of the CCAA addresses a D & O charge. I have already discussed section 11.51 in *Canwest Global Communications Corp., Re*[14] as it related to the request by the CMI Entities for a D & O charge. Firstly, the charge is essential to the successful restructuring of the LP Entities. The continued participation of the experienced Boards of Directors, management and employees of the LP Entities is critical to the restructuring. Retaining the current officers and directors will also avoid destabilization. Furthermore, a CCAA restructuring creates new risks and potential liabilities for the directors and officers. The amount of the charge appears to be appropriate in light of the obligations and liabilities that may be incurred by the directors and officers. The charge will not cover all of the directors' and officers' liabilities in a worse case scenario. While Canwest Global maintains D & O liability insurance, it has only been extended to February 28, 2009 and further extensions are unavailable. As of the date of the Initial Order, Canwest Global had been unable to obtain additional or replacement insurance coverage.

57 Understandably in my view, the directors have indicated that due to the potential for significant personal liability, they cannot continue their service and involvement in the restructuring absent a D & O charge. The charge also provides assurances to the employees of the LP Entities that obligations for accrued wages and termination and severance pay will be satisfied. All secured creditors have either been given notice or are unaffected by the D & O charge. Lastly, the Monitor supports the charge and I was satisfied that the charge should be granted as requested.

(h) Management Incentive Plan and Special Arrangements

58 The LP Entities have made amendments to employment agreements with 2 key employees and have developed certain Management Incentive Plans for 24 participants (collectively the "MIPs"). They seek a charge in the amount of $3 million to secure these obligations. It would be subsequent to the D & O charge.

59 The CCAA is silent on charges in support of Key Employee Retention Plans ("KERPs") but they have been approved in numerous CCAA proceedings. Most recently, in *Canwest Global Communications Corp., Re*[15], I approved the KERP requested on the basis of the factors enumerated in *Grant Forest Products Inc., Re*[16] and given that the Monitor had carefully reviewed the charge and was supportive of the request as were the Board of Directors, the Special Committee of the Board of Directors, the Human Resources Committee of Canwest Global and the Adhoc Committee of Noteholders.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

60 The MIPs in this case are designed to facilitate and encourage the continued participation of certain senior executives and other key employees who are required to guide the LP Entities through a successful restructuring. The participants are critical to the successful restructuring of the LP Entities. They are experienced executives and have played critical roles in the restructuring initiatives to date. They are integral to the continued operation of the business during the restructuring and the successful completion of a plan of restructuring, reorganization, compromise or arrangement.

61 In addition, it is probable that they would consider other employment opportunities in the absence of a charge securing their payments. The departure of senior management would distract from and undermine the restructuring process that is underway and it would be extremely difficult to find replacements for these employees. The MIPs provide appropriate incentives for the participants to remain in their current positions and ensures that they are properly compensated for their assistance in the reorganization process.

62 In this case, the MIPs and the MIP charge have been approved in form and substance by the Board of Directors and the Special Committee of Canwest Global. The proposed Monitor has also expressed its support for the MIPs and the MIP charge in its pre-filing report. In my view, the charge should be granted as requested.

(i) Confidential Information

63 The LP Entities request that the court seal the confidential supplement which contains individually identifiable information and compensation information including sensitive salary information about the individuals who are covered by the MIPs. It also contains an unredacted copy of the Financial Advisor's agreement. I have discretion pursuant to Section 137(2) of the *Courts of Justice Act*[17] to order that any document filed in a civil proceeding be treated as confidential, sealed and not form part of the public record. That said, public access in an important tenet of our system of justice.

64 The threshold test for sealing orders is found in the Supreme Court of Canada decision of *Sierra Club of Canada v. Canada (Minister of Finance)*[18]. In that case, Iacobucci J. stated that an order should only be granted when: (i) it is necessary in order to prevent a serious risk to an important interest, including a commercial interest, in the context of litigation because reasonable alternative measures will not prevent the risk; and (ii) the salutary effects of the confidentiality order, including the effects on the right of civil litigants to a fair trial, outweigh its deleterious effects, including the effects on the right to free expression, which in this context includes the public interest in open and accessible court proceedings.

65 In *Canwest Global Communications Corp., Re*[19] I applied the *Sierra Club* test and approved a similar request by the Applicants for the sealing of a confidential supplement containing unredacted copies of KERPs for the employees of the CMI Entities. Here, with respect to the first branch of the *Sierra Club* test, the confidential supplement contains unredacted copies of the MIPs. Protecting the disclosure of sensitive personal and compensation information of this nature, the disclosure of which would cause harm to both the LP Entities and the MIP participants, is an important commercial interest that should be protected. The information would be of obvious strategic advantage to competitors. Moreover, there are legitimate personal privacy concerns in issue. The MIP participants have a reasonable expectation that their names and their salary information will be kept confidential. With respect to the second branch of the *Sierra Club* test, keeping the information confidential will not have any deleterious effects. As in the *Canwest Global Communications Corp., Re* case, the aggregate amount of the MIP charge has been disclosed and the individual personal information adds nothing. The salutary effects of sealing the confidential supplement outweigh any conceivable deleterious effects. In the normal course, outside of the context of a CCAA proceeding, confidential personal and salary information would be kept confidential by an employer and would not find its way into the public domain. With respect to the unredacted Financial Advisor agreement, it contains commercially sensitive information the disclosure of which could be harmful to the solicitation process and the salutary effects of sealing it

 Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

outweigh any deleterious effects. The confidential supplements should be sealed and not form part of the public record at least at this stage of the proceedings.

Conclusion

66 For all of these reasons, I was prepared to grant the order requested.

Application granted.

Footnotes

1 R.S.C. 1985, c. C. 36, as amended.

2 On October 30, 2009, substantially all of the assets and business of the National Post Company were transferred to the company now known as National Post Inc.

3 Subject to certain assumptions and qualifications.

4 Although not formally in evidence before the court, counsel for the LP Secured Lenders advised the court that currently $382,889,000 in principal in Canadian dollars is outstanding along with $458,042,000 in principal in American dollars.

5 2006 CarswellOnt 264 (Ont. S.C.J. [Commercial List]).

6 2009 CarswellOnt 6184 (Ont. S.C.J. [Commercial List]) at para. 29.

7 (1993), 9 B.L.R. (2d) 275 (Ont. Gen. Div. [Commercial List]).

8 1999 CarswellOnt 4673 (Ont. S.C.J. [Commercial List]).

9 Ibid at para. 16.

10 (2002), 34 C.B.R. (4th) 157 (Ont. C.A.), leave to appeal to S.C.C. refused (March 6,2003) [2003 CarswellOnt 730 (S.C.C.)].

11 Ibid at para. 34.

12 Supra, note 7 at paras. 31-35.

13 This exception also applies to the other charges granted.

14 Supra note 7 at paras. 44-48.

15 Supra note 7.

16 [2009] O.J. No. 3344 (Ont. S.C.J. [Commercial List]).

17 R.S.O. 1990, c. C.43, as amended.

18 [2002] 2 S.C.R. 522 (S.C.C.).

19 Supra, note 7 at para. 52.

WestlawNext. CANADA Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

End of Document

Copyright © Thomson Reuters Canada Limited or its licensors (excluding individual court documents). All rights reserved.

IN THE MATTER OF THE *COMPANIES CREDITORS' ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED AND IN THE MATTER OF A PLAN OR COMPROMISE OR ARRANGEMENT OF CASH STORE FINANCIAL SERVICES INC. et al

Court File No. CV-14-10518-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

Proceedings commenced in Toronto

BOOK OF AUTHORITIES OF 0678786 B.C. LTD.

VOLUME 2 OF 2

BENNETT JONES LLP
One First Canadian Place
Suite 3400, P.O. Box 130
Toronto, Ontario
M5X 1A4

Robert W. Staley (LSUC #27115J)
Raj Sahni (LSUC #42942U)
Gannon Beaulne (LSUC #63948V)

Tel: 416-777-4856
Fax: 416-863-1716

Lawyers for 0678786 B.C. Ltd.