Court File No.: CV-13-10280-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

B E T W E E N :

DBDC SPADINA LTD.
AND THOSE CORPORATIONS LISTED ON SCHEDULE A HERETO

Applicants

- and -

NORMA WALTON, RONAULD WALTON,
THE ROSE & THISTLE GROUP LTD. and EGLINTON CASTLE INC.

Respondents

- and -

THOSE CORPORATIONS LISTED ON SCHEDULE B HERETO,
TO BE BOUND BY THE RESULT

BOOK OF AUTHORITIES OF THE MOVING PARTY

December 18, 2013

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I N D E X

TAB #	DOCUMENT
7.	*Peoples Trust Company v. Rose of Sharon (Ontario) Retirement Community*, 2012 ONSC 7319
8.	*Re Francisco*, 1995 CanLII 7371 (ON S.C.), aff'd 1996 CanLII 10233 (ON C.A.)
9.	*Re Ma*, 2001 CanLII 24076 (ON C.A.)

TAB 1

Arnold v. Bronstein et al.

[1971] 1 O.R. 467-470

ONTARIO
[HIGH COURT OF JUSTICE]

LACOURCIERE, J.

24th NOVEMBER 1970.

Mortgages -- Remedies of mortgagee -- Power of sale -- Mortgagor seeking interim injunction to restrain exercise of power -- Applicable principles in determining when injunctions should be granted.

Except in the most extreme and exceptional cases, a mortgagee, acting in good faith and without fraud, will not be restrained from a proper exercise of his power of sale except upon tender by the mortgagor of the principal moneys due, interest and costs. Accordingly, postponement of a sale on a mortgagor's vague and indefinite hope of finding new financial backing would be an unwarranted interference with the contractual rights of the mortgagee, even if the mortgaged property is ample security for the loan.

[Standard Realty Co. v. Nicholson (1911), 24 O.L.R. 46; Macleod v. Jones (1883), 24 Ch.D. 289; Yandt v. Sparling (1927), 32 O.W.N. 318; Hoskins v. Johnston (1875), 6 P.R. (Ont.) 257, refd to]

APPLICATION by a mortgagor for an interim injunction to restrain the mortgagee from selling under the power of sale contained in the mortgage.

A. Wellenreiter, for plaintiff.

M.A. Catzman, for defendants.

LACOURCIERE, J.:-- The plaintiff, a mortgagor in possession of property known as the Norfolk Hotel, in the Town of Simcoe, brings this application for an interim injunction to restrain the defendant Bronstein, a first mortgagee, from selling under a power of sale contained in his mortgage.

In very brief summary, the principal amount owing under the mortgage became due on July 10, 1969; more than six months before the said date, the first mortgageee advised the plaintiff, by letter, that the mortgage would not be renewed, although a short term renewal might be considered if the principal was reduced by $50,000 and the taxes paid in full. The principal was not so reduced, although monthly payments were accepted by the mortgagee providing very slight reduction on a large mortgage. Following the notice, the mortgagor made three abortive attempts to refinance. He was unable to arrange funds on a solid commitment basis. The efforts are fully set out in the applicant's extensive affidavit. He blames the general economic conditions for his inability to refinance. He refers to the deteriorating state of his health and argues that a postponement of the sale by injunction will not prejudice the mortgagee, whose security is said to be ample. It is clear that different considerations apply where the sale is made by a mortgagee under a power of sale in contrast to a sale after final order of foreclosure. As pointed out by Riddell, J., in Standard Realty Co. v. Nicholson (1911), 24 O.L.R. 46 at pp. 56-7:

> The difference is manifest -- on a sale after final order for foreclosure the mortgagee has a chance of making a gain -- he has not to account to the mortgagor; and, if he does not make enough to pay the amount of the debt, he cannot sue for the balance. Where the property is sold under power of sale, the mortgagee cannot make a gain; he must account for the surplus over his debt, but he can sue if there be a deficiency: Burnham v. Galt (1869), 16 Gr. 417, at p. 419; Pegg v. Hobson (1887), 14 O.R. 272; Rudge v. Richens, L.R. 8 C.P. 358.

> Again, there is a marked difference in the power of the Court to interfere where it is a question of rights arising under its own decree, and where it is a question of rights arising from a contract. Where a person, to support his claim to land, must rely upon a judgment of the Court, the Court may well have the power to vary such judgment and the rights arising under it -- but whence comes the power of the Courts to interfere with rights arising under contract and independently of any Court proceeding?

It appears that Courts have refused to interfere with the proper exercise of a power of sale in all but the most extreme and exceptional cases. In fact, the learned author of Kerr on Injunctions, 5th ed., p. 538, in a chapter dealing with injunctions between mortgagor and mortgagee, goes so far as to assert that:

> The Court has no jurisdiction to restrain a mortgagee from selling under a power of sale, provided he keep within the terms of the power and no case of fraud be made out.

The proposition is well supported by cases referred to in footnote (e). The general rule developed from numerous cases is that a mortgagee, acting in good faith and without fraud, will not be restrained from a proper exercise of his power of sale, except upon tender by the mortgagor of the principal moneys due, interest and costs. This is of course subject to the statutory relief provided by s. 20 [rep. & sub. 1970, c. 54, s. 1] of the Mortgages Act, R.S.O. 1960, c. 245, which is not here invoked. The institution of a redemption action per se does not affect the mortgagee's power of sale: Kerr on Injunctions, supra, p. 540; Halsbury's Laws of England, 3rd ed., vol. 27, para. 566, p. 301.

The rule is stated thus in Macleod v. Jones (1883), 24 Ch.D. 289 at pp. 299-300, per Cotton, L.J.:

> This is an application to restrain a mortgagee from exercising his power of sale. Now under ordinary circumstances the Court never interferes unless there is something very strong; it does not interfere on any suggested case without requiring the Plaintiff applying to pay into Court not what the Judge or the Court on hearing the evidence is satisfied will probably be the amount due, but what the mortgagee, the accounts not having been yet taken, swears is due to him on his security. And that is perfectly right, because we ought not to prevent mortgagees from exercising the powers given to them by their security without seeing that they are perfectly safe.

See Yandt v. Sparling (1927), 32 O.W.N. 318.

I am far from satisfied, on the material before me, that the applicant has shown extreme or exceptional circumstances which would justify a departure from the prevailing practice; nor has it been established that the plaintiff would probably be entitled to redeem, following the granting of an interlocutory injunction.

On the contrary, the plaintiff was given every consideration, and every reasonable opportunity, to make arrangements. In the light of the plaintiff's poor record of payment, allowing taxes on the property to accumulate in an amount in excess of $22,000 for the years 1969 and 1970, previous abortive attempts to refinance, the mortgagee was not unreasonable in advising the plaintiff that his instructions to proceed with the sale of the property were peremptory.

The date fixed for sale is November 27th next, 11 days following the return of this motion. In preparation for the sale, the mortgagee obtained appraisals, inserted advertisements in three publications, posted the formal advertisements in prominent places in the County of Norfolk, sent copies thereof to 34 different law firms in surrounding municipalities, and as a result of these efforts received some 30 inquiries from interested parties who plan to attend the sale and to enter bids. Postponement of the sale at this time on the plaintiff's vague and indefinite hope of finding new financial backing would, in my opinion, constitute an unwarranted interference with the mortgagee's contractual rights.

Speaking of a judicial sale, Blake, V.C., had this to say in Hoskins v. Johnston (1875), 6 P.R. (Ont.) 257 at p. 259:

> Only in an extreme case should a sale be postponed. Where an application is made, some time before the day appointed for the auction, so that a postponement can be had before bidders have arranged to attend and, to become purchasers, then it may not, at times, be unreasonable to allow an adjournment, as no injury need thereby be done; but where the application is made but a few days before the time appointed for the sale, then it is out of the question to grant a postponement unless there be some fraud or evil practice, or some omission which will plainly cause damage to parties interested. Here by a postponement the proposed sale would be damped, and general discredit will be cast upon all the sales of the Court. The sale in question is to take place tomorrow; already those who intend to purchase have made their arrangements for so doing. No postponement can now take place, except in the auction room. The annoyance caused by dispersing in this manner the intending purchasers will put persons out of the whim or intention of purchasing, and deter them from attending any future sale of the kind.

These words are equally applicable to a private sale where a postponement could deter potential purchasers.

Upon payment into Court of the principal amount, accumulated interest and costs, the proposed sale will be restrained. Otherwise, this application will be dismissed with costs to be paid by the applicant to the respondent David Bronstein in any event of the cause.

Order Accordingly.

TAB 2

COURT FILE NO.: CV-0800007922-00CL
DATE: 20091006

SUPERIOR COURT OF JUSTICE – ONTARIO
COMMERCIAL LIST

RE: TURBO LOGISTICS CANADA INC., 2163960 ONTARIO INC., GEORGE PERLIN, ALEX BER and 2192370 ONTARIO LIMITED

Plaintiffs

- And -

HSBC BANK CANADA

Defendant

A N D B E T W E E N:

HSBC BANK OF CANADA

Plaintiff by Counterclaim

- And -

GEORGE PERLIN, ALEX BER, 2086611 ONTARIO INC., ARI YAKOBSON, VLADIMIR BOTVINNIK and BORIS SHTEIMAN

Defendants to the Counterclaim

A N D B E T W E E N:

2086611 ONTARIO INC.

Plaintiff by Counterclaim

- And -

HSBC BANK CANADA and DELOITTE AND TOUCHE INC.

Defendants to the Counterclaim

BEFORE: Justice Newbould

COUNSEL: *Melvyn L. Solmon* and *Cameron J. Wetmore*, for the plaintiffs Turbo Logistics Canada Inc., George Perlin, Alex Ber and 2192370 Ontario Limited

J. Brian Casey, for the defendant HSBC Bank Canada

DATE HEARD: October 1, 2009

E N D O R S E M E N T

[1] The plaintiffs[1] moved for an order removing the law firm of Baker & McKenzie LLP ("Baker") as solicitors of record in this matter for the defendant HSBC Bank Canada ("HSBC") and for an order extending the time of delivery of their reply and statement of defence to counterclaim. The motion was heard on October 1, 2009. At the conclusion of the motion I dismissed the motion to remove Baker as solicitors for HSBC for reasons to follow and ordered that the plaintiffs' reply to the statement of defence to the counterclaim be delivered within thirty days. These are my reasons.

Factual Background

[2] The plaintiffs Turbo Logistics Canada Inc. ("Turbo") and 2163960 Ontario Inc. ("216") are companies previously controlled by the plaintiffs George Perlin and Alex Ber. HSBC is the secured creditor of Turbo and 216. Turbo is indebted to HSBC for approximately $9 million and 216 is indebted to HSBC for approximately $2 million. Messrs. Ber and Perlin are guarantors.

[3] In November 2008 Baker was retained by HSBC to act in connection with the enforcement of the credit facilities extended by HSBC to Turbo and 216. On December 22, 2008 the plaintiffs commenced this action against HSBC seeking, among other things, declarations relieving Messrs. Perlin and Ber of their guarantee obligations to HSBC for the loans of Turbo and 216. Subsequently HSBC counterclaimed against Messrs. Perlin and Ber and others for alleged fraud and conspiracy.

[4] On December 24, 2009, shortly after the commencement of the action, HSBC brought an application to have Deloitte and Touche LLP appointed as receiver of Turbo and 216. Turbo and 216 opposed the application. On January 28, 2009 Cumming J. appointed Deloitte and Touche Inc. as receiver of Turbo and 216. Paragraph 5 of the receivership order provided that the

[1] The action by the plaintiffs Turbo Logistics Canada Inc. and 2163960 Ontario Inc. has been stayed by the receiving order of Cumming J. of January 28, 2009. My reference to the plaintiffs in these reasons is to the remaining plaintiffs George Perlin, Alex Ber and 2192370 Ontario Limited.

receiver could retain Baker to represent and advise the receiver in respect of any matter where there is no conflict of interest.

[5] The plaintiffs contend that as a result of what they say is a refusal by Baker to produce documents of the receiver in the civil action, Baker should be removed as solicitors for HSBC in the civil action on the grounds that there is a conflict in Baker's obligations to HSBC and to the receiver. The plaintiffs say that the receiver and Baker each owe a duty of fairness to the plaintiffs and to treat them like other creditors, which duty is said to have been breached. The plaintiffs have not moved to remove Baker from acting as solicitors for the receiver.

Request for Documents

[6] On April 7, 2000 Mr. Solmon wrote on behalf of the plaintiffs to Baker and made a request to attend at Baker's office to review "all files (including without limitation all written or electronic documents) in the possession of [Baker] that are in anyway related to [Turbo] or [216] or relevant to the issues raised in the [civil action]." On April 16, 2009 Baker replied that Mr. Solmon's clients were not entitled to documentary discovery prior to the close of pleadings and that all documents produceable by HSBC which are relevant to the proceeding and not subject to claims of privilege would be produced in its affidavit of documents.

[7] On March 15, 2009 Ari Yakobson, one of the defendants to the counterclaim, served a demand for particulars and request to inspect which requested copies of all documents that HSBC was relying on in the civil action in support of its allegations against the defendants to the counterclaim. On April 24, 2009 HSBC responded to the solicitors for Mr. Yakobson and stated that a CD with the requested documents would be sent, which it was. The letter was copied to other counsel, including Mr. Solmon, and stated that if other counsel would like a copy of the CD, it would be provided. The plaintiffs, represented by Mr. Solmon, did not request a copy of the CD's or the documents contained in it. The CD contained all of the documents relevant to the allegations made by HSBC in the counterclaim that were in the hands of HSBC or the receiver.

[8] Mr. Solmon did not respond to the offer contained in the Baker letter of April 16, 2009 to provide the CD to other counsel. Instead, on May 12, 2009, Mr. Solmon on behalf of the plaintiffs brought a motion in the civil action for an order removing Baker as solicitors for HSBC or for the receiver, an order restraining Baker from acting for HSBC in the civil action, an order compelling Baker to provide access to a comprehensive list of various documents in its possession, power or control in any way related to Turbo or 216 or relevant to the issues raised in the civil action. Subsequently on May 22, 2009, Mr. Solmon delivered an amended notice of motion which removed the request for an order removing Baker from acting for the receiver and removed the request for an order that Baker produce the documents requested in the original notice of motion. Thus the amended notice of motion simply seeks an order removing Baker as solicitors for HSBC in the civil action and an order restraining Baker from acting for HSBC in that action.

[9] On May 25 Baker wrote to Mr. Solmon and enquired whether his clients were prepared to restrict their request to all non-privileged information and to pay the costs of the receiver in assembling and preparing it. Baker pointed out that the plaintiffs' request was not limited to documents relevant to the civil action and that there were many documents s in the hands of the receiver that had not been provided to Baker or HSBC. Mr. Solmon did not respond to that letter.

[10] On May 29, 2009 Baker wrote to Mr. Solmon and enclosed a copy of the CD that had previously been provided and offered to him.

Legal Principles

[11] The general rule is that a lawyer may not represent one client whose interests are directly adverse to the immediate interest of another current client, even if the two mandates are unrelated, unless both clients consent after receiving full disclosure and the lawyer reasonably believes that he or she is able to represent each client without adversely affecting the other. See *R. v. Neil*, [2002] 3 S.C.R. 631.

[12] In determining the presence of a conflict of interest, a court must balance three factors, being i) the maintenance of the high standards of the legal profession and the integrity of the judicial system, ii) the right of litigants not to be deprived of their counsel without good cause and iii) the desirability of permitting reasonable mobility in the legal profession. See *Macdonald Estate v. Martin*, [1990] 3 S.C.R. 1235.

[13] A court appointed receiver is an officer of the court and acts in a fiduciary capacity with respect to all parties interested in the assets under the control of the receiver. See *Canadian Imperial of Commerce v. Isobord Enterprises Inc.* (2002), 36 C.B.R. (4th) 19 (Man. C.A.); *Ostrander v. Niagara Helicopters Ltd.* (1993), 1 O.R. (2nd) 281; *Royal Bank v. Vista Homes Ltd.* (1984), 54 C.B.R. (N.S.) 124.

[14] It is asserted on behalf of the plaintiffs that the obligations of a court-appointed receiver to treat creditors equally is an obligation that applies equally to the solicitors for the receiver and relies upon the followings statements of Wilson J. in *Engels v. Richard Killen & Associates Ltd.* (2002), 60 O.R. (3rd), 572 at paras. 49 and 54:

> [49] The trustee and his or her counsel must be neutral and evenhanded with all classes of creditors, and with the bankrupt.
>
> [54] The duties and obligations of trustees in bankruptcy apply equally to their counsel. Counsel, too, are officers of the court. They are not ordinary counsel representing one litigant entitled to wage war with the bankrupt, or to prefer one creditor over another utilizing all of the artillery of the adversary system. They are obliged to act neutrally and fairly throughout, to all creditors and to the bankrupt.

[15] In *Re Dugas* (2003), 41 CBR (4th) 168 these statements of Wilson J. were adopted.

[16] I cannot agree with the notion that counsel for a trustee in bankruptcy, or for a court-appointed receiver, normally owes any duty to the creditors of the bankrupt or debtor under a court-appointed receiver. The obligation of a solicitor is to his or her client. The fact that the solicitor is an officer of the court does not change that. It is the trustee in bankruptcy or the court-appointed receiver that owes a fiduciary duty to the creditors or other stakeholders. To suggest that the lawyer advising the trustee in bankruptcy or the court-appointed receiver owes a

duty to those creditors or other stakeholders would, amongst other things, lay the solicitor open to actions at the hands of the creditors of the trustee in bankruptcy or court-appointed receiver for failure to properly carry out the lawyer's obligations to those creditors or stakeholders. This is not the law and would make no sense. A solicitor giving advice to a client, whether the client is a trustee in bankruptcy or court-appointed receiver or otherwise, is responsible to the client to give proper advice to the client. It is the client, and not the solicitor, that owes duties to creditors and other stakeholders in the case of a trustee in bankruptcy or court-appointed receiver.

[17] With respect to the requirement to produce privileged documents, a court-appointed receiver is in no different position than any other person seeking legal advice and advice given by the solicitor to the receiver in confidence is entitled to solicitor and client privilege. The fact that a receiver has a fiduciary relationship with the creditors does not give the creditors the right to have access to all documents that come into the hands of a receiver manager. See *Houlden & Morawetz, Bankruptcy and Insolvency Analysis, L§39*; *SLP Resources Inc. v. Sorrel Resources Ltd.* (1987), 65 C.B.R. (N.S.) 288.

[18] The fact that a receiver owes fiduciary duties to the stakeholders does not entitle a stakeholder to go on a fishing expedition for documents. See *Re Battery Plus Inc.*, (2002), 31 C.B.R. (4th) 196 at para. 21.

Analysis

[19] I do not see any conflict between HSBC and the receiver of Turbo and 216. The action by Turbo and 216 was stayed in the order of Cumming J. of January 28, 2009 appointing the receiver, and no one has moved to seek leave to continue the action on their behalf. The litigation is essentially amongst HSBC and the guarantors of the loans made by HSBC and others who are alleged to have engaged in fraudulent activities harming HSBC. The receiver is not involved in the civil action and the issues involved in the action relate to matters that took place prior to the appointment of the receiver. Thus this is not a situation in which Baker has divided loyalties between HSBC and the receiver in relation to the civil action, nor is it a situation in which the interests of HSBC and the receiver's duties to the stakeholders of Turbo and 216 are potentially adverse.

[20] It seems to me, moreover, that even if there were a conflict between the positions of HSBC and the receiver, the appropriate step would be to remove Baker from acting for the receiver in connection with that conflict. The plaintiff's assertion of a conflict between HSBC and the receiver is founded on the duty of a receiver to deal evenly with all creditors, which it says has been breached because of the failure of Baker to produce documents. If that assertion of a conflict were correct, the logical step, and one that would be consistent with the order of Cumming J. authorizing Baker to act for the receiver where there is no conflict of interest, would be to move to have Baker removed from acting for the receiver rather than for HSBC. A litigant is not to be deprived of the counsel of its choosing without good cause – See *Macdonald Estate v. Martin, supra.*

[21] With respect to the issue of the production of documents that has been raised by Mr. Solmon, his request for documents on behalf of Messrs. Perlin and Ber and 2192370 Ontario Ltd. was directed to Baker to produce all of the requested documents in the possession of Baker. The request appears to have been purely tactical. The request was not made to have the documents in the possession of the receiver produced. Ordinarily, if Mr. Solmon's clients were looking for documents relating to the litigation, a request would be made to HSBC's solicitors to have those documents produced by HSBC. Mr. Solmon asserted in his letter of request that his clients were creditors of Turbo and that Baker as solicitors for the receiver owed a fiduciary duty to them. Presumably that was stated to support the request for all written or electronic documents in the possession of Baker in any way related to Turbo or 216. One would have thought that if it was a request for documents in the possession of the receiver, the request would have been made to Baker to have the receiver produce such documents. It appears to me clear that Mr. Solmon was in the process of setting up a motion to remove Baker as solicitors and that this letter was the opening salvo. Removal litigation brought to remove solicitors in order to gain a tactical advantage by delaying delivery of pleadings should not be permitted.

[22] In argument, Mr. Solmon contended that in response to his letter Baker should have responded by saying that as the solicitor for the receiver he was providing everything the receiver knows about HSBC's case against Mr. Solmon's clients. As a practical matter, Mr. Solmon has received those documents. He has been provided with all documents relevant in the

civil litigation that were in the possession of HSBC or the receiver. Baker sent the CD containing these documents to Mr. Solmon on May 29, 2009 in the correspondence relating to production in the civil litigation. If Mr. Solmon's clients wanted to take the position that there were other documents that should be produced, or that for some reason privileged documents should be produced, the appropriate step would have been for a motion requiring their production. No such motion has been brought.

[23] Mr. Solmon asserted in argument that the receiver has given privileged documents to Baker in Baker's capacity as solicitor for the receiver and that as Baker acts for HSBC, the privilege has been lost. Therefore he asserts such documents should be delivered by Baker to his clients. One problem with this argument is that Mr. Solmon readily acknowledges that he has no knowledge of what HSBC has received from the receiver. Another is that no motion for production of any documents has been made. Even if Mr. Solmon were right in his contention, his clients would be able to move for documents in the possession of Baker even if Baker were removed as solicitors for HSBC. It would be no basis to remove Baker from acting for HSBC.

[24] With respect to the broad request that Baker produce all of the documents in its possession relating to Turbo or 216, there is no principled reason provided as to why Messrs. Perlin and Ber and their company 2192370 Ontario Limited, even if they are creditors of Turbo or 216, would be entitled to all such documents. It appears to be a fishing expedition in the extreme. Baker acts for the receiver in connection with a number of matters typical in a receivership involving attempts by the receiver to obtain assets of various kinds. If there is any legitimate reason for creditors to have access to documents in the hands of a court-appointed receiver, one would expect a request to be made to the receiver and to identify what documents were being sought. I agree with the following statement of Greer J. in *Re Battery Plus Inc. supra,* that a creditor is not entitled to go on a fishing expedition with a receiver. She stated:

> Further, in *SLP Resources Inc. v. Sorrel Resources Ltd.* (1987), 65 C.B.R. (N.S.) 288 (Alta. Q.B.), the Court pointed out that the fiduciary relationship created in such situation between the receiver-manager and with the people involved in the receivership:

> ... does not in my view automatically entitle creditors or people in the position of SLP Resources and Societe Generale access to all of the documents which come into the hands of the receiver-manager and, in particular, legal opinions relating to the receiver's position and the validity, or otherwise, of various securities.
>
> To allow all people involved in this Interim Receivership to automatically be entitled to access to all of the documents which came into the Interim Receiver's hands could cause the interim receivership to waste untold hours for no purpose. I am satisfied that, while there is a right of an interested party to certain relevant documents, these documents must relate to a specific purpose. That right does not entitle Badr to go on a fishing expedition.

[25] In summary, I find that there is no conflict between Baker's duty to HSBC and to the receiver that would require the removal of Baker from acting as solicitor for HSBC.

Extending time for delivery of pleading

[26] In the plaintiffs' motion they requested an order extending the time for delivery of a reply and defence to counter-claim for 30 days after final determination of whether Baker should be removed as solicitors for HSBC. Neither in their factum nor in oral argument was any reason given why the pleading should be delayed until the motion to remove Baker was finally determined, nor is any reason apparent why that should be. In the circumstances I ordered at the conclusion of the motion that the pleading be delivered within 30 days.

_____

Newbould J.

DATE: October 6, 2009

TAB 3

3 of 3 DOCUMENTS

Robert F. Kowal Investments Ltd. et al. v. Deeder Electric Ltd.

[1975] O.J. No. 2363

9 O.R. (2d) 84

59 D.L.R. (3d) 492

21 C.B.R. (N.S.) 201

Ontario
Court of Appeal
Jessup, Lacourciere

and Houlden, JJ.A.

May 5, 1975

H. Lorne Morphy and Sheila R. Block, for appellant, Monte Denaburg.

John G. Reid, Q.C., for plaintiffs, respondents.

Leon Klug, for receiver, respondent, Jerry Friedman.

The judgment of the Court was delivered by

1 HOULDEN, J.A.:-- This is an appeal from an order of the Honourable Mr. Justice Holland dated December 13, 1974, which declared that Jerry Friedman was entitled, on his discharge as receiver, to priority for $24,043.26 over a land titles charge held by the appellant, the sum of $24,043.26 being the total of payments of principal and interest made by the receiver to the appellant on his charge during the period of the receivership.

2 On November 30, 1971, a charge under the Land Titles Act, R.S.O. 1970, c. 234, was given on

the property municipally known at 2010 Jane St. in the Borough of North York. The charge was in the principal sum of $400,000. It was registered in the Office of Land Titles at Toronto on December 1, 1971, as instrument No. B-306317. By transfer of charge dated December 31, 1971, and registered in the Office of Land Titles at Toronto on January 17, 1972, as instrument No. B-310301, the charge was transferred to the appellant Monte Denaburg.

3 In February, 1972, the premises at 2010 Jane St. were purchased by Robert F. Kowal Investments Limited, Randy Construction Company Limited and Deeder Electric Limited in partnership. On the property, there was located a car wash. At the time of the purchase, the three limited companies entered into a partnership agreement with respect to the operation of the car wash.

4 In January, 1974, serious differences arose between the partners concerning the management of the business. On January 17, 1974, the defendant Deeder Electric Limited gave notice to the plaintiffs of its desire to terminate the partnership. On February 7, 1974, the plaintiffs issued a writ against Deeder Electric Limited claiming, inter alia, the dissolution of the partnership, the appointment of a receiver and an accounting.

5 By a consent judgment dated March 13, 1974, the Honourable Mr. Justice Wright made an order dissolving the partnership and appointing Jerry Friedman as receiver of the partnership affairs. Prior to accepting the appointment, Friedman obtained from the plaintiffs an agreement to be responsible for his fees, costs, charges and expenses in acting as receiver in so far as he was unable to recover them from the assets of the partnership.

6 On May 9, 1974, the Honourable Mr. Justice Goodman made a consent order varying the judgment of March 13, 1974. Paragraph 13 of the order of May 9, 1974, provided:

> 13. AND THIS COURT DOTH FURTHER ORDER that the said receiver and manager be at liberty and he is hereby empowered to borrow monies from time to time as he may consider necessary, not exceeding the principal amount of Twenty-Five Thousand Dollars ($25,000.00), including money already expended, at an interest rate not to exceed prime plus 3 per cent, for the purpose of protecting and preserving and selling the undertaking, property and assets of the partnership and carrying on the business and undertaking of the said partnership and for the purposes of paying presently existing mortgage payments as they fall due, and that as security therefor and for every part thereof, the whole of the undertaking, property and assets of the partnership together with all assets and property which may hereafter be in the custody and control of the receiver and manager as such, do stand charged with the payment of the monies so borrowed by the receiver and manager.

Although para. 13 referred to the "receiver and manager", the original judgment and the amending order appointed Friedman as receiver only of the partnership assets. Pursuant to the authority given

by para. 13, the receiver borrowed $25,000.

7 The appellant was not served with notice of any of the foregoing proceedings in the partnership action. However, there is no doubt that shortly after March 13, 1974, the appellant was aware of the appointment of the receiver. From March to September, 1974, the appellant received payments on his charge from the receiver in the total amount of $24,043.26.

8 By notice of motion dated October 18, 1974, the receiver applied to the Court for permission to borrow a further $15,000 on the same terms as in para. 13 of the order of May 9, 1974, and for an order that the sum so borrowed and the $25,000 already borrowed, should be a first charge on the whole of the undertaking, property and assets of the partnership in priority to the appellant's charge. The appellant was served with notice of this application. On October 24, 1974, Holland, J., dismissed the application without written reasons.

9 By notice of motion dated December 9, 1974, the receiver applied to the Court for an order discharging him as receiver. In addition, he asked for an order granting him priority over the appellant's charge for his remuneration and legal costs and for expenditures made, and obligations incurred, by him. The appellant received notice of this application. On December 13, 1974, Holland, J., made an order discharging the receiver and granting him priority over the appellant's charge for the mortgage payment of $24,043.26. It is the order granting priority to the receiver over the appellant's charge which is attacked in this appeal.

10 The mortgage payments made by the receiver to the appellant were proper payments for the receiver to have made. If they had not been made, the appellant would likely have taken steps to enforce his security and if this had occurred, the potential recovery of the partners and the unsecured creditors could have been seriously affected. The receiver was, therefore, clearly entitled to priority over the claims of the partners and the unsecured creditors for the moneys he had borrowed to make the payments on the appellant's charge. However, the issue that we are called on to decide is whether the receiver should receive priority over the secured claim of the appellant for the borrowed moneys.

11 The receiver of a partnership business must look to the assets under his control for payment of his charges and expenses. In Boehm v. Goodall, [1911] 1 Ch. 155, a receiver and payments which the assets of the firm were insufficient to satisfy in full; he brought an application for an order that the partners should personally indemnify him for the balance owing to him. In dismissing the application, Warrington, J., said (at p. 161):

> I think it is of the utmost importance that receivers and managers in this position should know that they must look for their indemnity to the assets which are under the control of the Court. The Court itself cannot indemnify receivers, but it can, and will, do so out of the assets, so far as they extend, for expenses properly incurred; but it cannot go further. It would be an extreme hardship in most cases to parties to an action if they were to be held personally liable for expenses

incurred by receivers and managers over which they have no control.

12 Not only is the receiver's right to indemnity restricted to the assets under his control, but it is also confined to the equity of the partnership in those assets. As a general rule, the receiver of a partnership will have no power to subject the security of secured creditors of the partnership to liability for disbursements made by him. Clark On Receivers, 3rd ed., by Ralph Ewing Clark of the Cincinnati Bar, vol. 2, s. 638, pp. 1070-1, sums up the position regarding general receivers (a general receiver being "a receiver who takes custody of all the property of an individual or corporation for the purpose not only of preserving it and making it available to satisfy a judgment of the plaintiff in the case, but also that the assets and property of the defendant may be collected, administered and distributed to all claimants who may present their claims to the receiver": Clark, op. cit., vol. 1, s. 22, p. 25, in this way:

> When a court appoints a general receiver of the property of an individual or a corporation, at the instance of a creditor other than a mortgage lienholder, part or all of this property may be covered by liens or mortgages. The general purpose of a general receivership is to preserve and realize the property for the benefit of the creditors in general. No receivership may be necessary to protect or realize the interests of lienholders. In such cases the mortgagees and lienholders cannot be deprived of their property nor of their property rights and the receivership property cannot as a rule be used nor the business carried on and operated by the receiver in such a way as to subject the mortgagees and lienholders to the charges and expenses of the receivership. A court under such circumstances has no power to authorize expenses for improving or making additions to the property or carrying on the business of the defendant at the expense of prior mortgagees or lienholders without the sanction of such mortgagees or lienholders.

13 There are certain exceptions to the general rule. (I do not propose to give an exhaustive list of such exceptions but to refer only to the exceptions which, in my opinion, have some relevance for the facts of this case.) The first exception is this: If a receiver has been appointed at the request, or with the consent or approval, of the holders of security, the receiver will be given priority over the security holders. One would ordinarily expect that in these circumstances the order permitting the receiver to borrow would clearly provide that the security given by the receiver for his borrowings would have priority over the claims of secured creditors. However, even if the order failed to so provide, if the secured creditors have applied for, consented to, or approved of, his appointment, the receiver will have priority for charges and expenses properly incurred by him.

14 The priority which is given to a receiver in this type of situation is illustrated by Strapp v. Bull, Sons & Co.; Shaw v. School Board of London, [1895] 2 Ch. 1. In that case, a building company became involved in serious financial difficulties. Receivers and managers were appointed at the request of debenture holders of the company. The receivers and managers obtained permission to borrow 5,000 pounds by way of a first charge in priority to the security of the

debenture holders. Certain proceedings were then taken by unsecured creditors as a result of which an agreement was made whereby unsecured creditors agreed to advance two-thirds and the plaintiff Strapp, who was a debenture holder, agreed to advance one-third of the moneys that the receivers and managers wished to borrow. In due course, the receivers and managers borrowed 1,750 pounds from Strapp and 2,500 pounds from the unsecured creditors. The receivership worked out badly, and in completing certain contracts, the receivers and managers used up all the moneys they had borrowed and, in addition, incurred substantial further indebtedness. The receivers and managers applied for an order that they were entitled to priority for the debts they had incurred not only over the security of the debenture holders, but also over the security held by Strapp and the unsecured creditors for the 4,250 pounds that the receivers and managers had borrowed. This application was dismissed by Vaughan Williams, J., but on appeal, his decision was reversed and the receivers and managers were granted the priority they had requested. With reference to the position of the persons who had advanced the 4,250 pounds, A.L. Smith, L.J., said (at p. 11):

> Under these circumstances it seems to me that these people who have advanced the money stand in the same position as second debenture-holders. They have acquiesced in this form of carrying on the business by their receivers and managers, and I think, therefore, the law as laid down by Pearson J. and the Master of the Rolls, Sir George Jessel, in the two cases to which I have referred, applies, and consequently they [the receivers and managers] are are entitled to be paid their charges.

15 However, the exception to the general rule enunciated in Strapp v. Bull has no application to this case. Here, there was no acquiescence by the appellant in the appointment of the receiver. As has been pointed out, the appellant was given notice of the proceedings which led to the appointment of Jerry Friedman as receiver. It was not until after the indebtedness was incurred that the receiver sought an order giving him priority over the appellant's charge. The first exception to the general rule has, therefore, no application to the facts of this case.

16 The second exception is this: If a receiver has been appointed to preserve and realize assets for the benefit of all interested parties, including secured creditors, the receiver will be given priority over the secured creditors for charges and expenses properly incurred by him. In such a case, also, one would expect that an order permitting borrowing by the receiver would make it clear before the fact, not after the fact (as was attempted in the present case), that the receiver could give as security for his borrowing a charge upon all the assets in priority to the security of secured creditors:

> Greenwood v. Algesiras (Gibraltar) R. Co., [1894] 2 Ch. 205. When an order is sought for this type of borrowing, notice will ordinarily be given to the secured creditors whose rights will be affected: Greenwood v. Algesiras (Gibraltar) R. Co.; and it will require compelling and urgent reasons for the Court to grant its approval if the secured creditors oppose the making of the order: Re Thames Ironworks, Shipbuilding & Engineering Co. Ltd.; Farrer v. The Company, [1912]

W.N. 66.

17 The appointment of a receiver in these circumstances is illustrated by Braid Builders Supply & Fuel Ltd. et al. v. Genevieve Mortgage Corp. Ltd. (1972), 29 D.L.R. (3d) 373, 17 C.B.R. (N.S.) 305. In that case, a receiver was appointed of all the undertaking, property and assets of a building company which was in the course of construction of an apartment block. There was a first mortgage on the premises of $1,100,000. Unfortunately, the sale of the building by the receiver did not realize sufficient to pay the first mortgage in full. While admitting that certain disbursements of the receiver were in order and entitled to be paid in priority to its mortgage, the first mortgagee claimed that the balance of the disbursements and the fees of the receiver should not be given priority over the mortgage.

18 Although the judgment makes no mention of whether or not the first mortgagee was served with the motion to appoint the receiver, it would seem that service must have been made on the mortgagee, since Dickson, J.A. (as he then was), who delivered the judgment of the Manitoba Court of Appeal, pointed out that the first mortgagee did not appeal the order appointing the receiver. The report does not indicate, either, whether the secured creditor consented to or approved of the appointment of the receiver. The Court of Appeal for Manitoba held that, the appointment having been made for the benefit of all creditors, including secured creditors, for the purpose of preserving the property, the receiver should be given priority for all his fees and disbursements over the secured creditor. Dickson, J.A., said (at pp. 375-6):

> The Court itself has no funds from which to pay a receiver. If his fees cannot be paid from assets under administration of the Court the receiver would be in the untenable position of having to seek recovery from the creditor who, on behalf of all creditors, asked for the appointment. This could work a grave injustice on the receiver and on the petitioning creditor. Why should the latter bear all of the costs in respect of an appointment made for the benefit of all creditors, including secured creditors, for the purpose of preserving the property?

19 The second exception to the general rule likewise has no application to the facts of this case. Paragraph 13 of the order of Goodman, J., of May 9, 1974, supra, created a charge on the whole of the undertaking, property and assets of the partnership. This could have referred only to the equity that the partnership had in the undertaking, property and assets. Prior to the appointment of the receiver, the partners had, of course, no power to create a security having priority to the registered charge of the appellant. Although the Court appears to have power to create such a charge if it is necessary for the preservation of the property for the benefit of all parties, certainly, notice would have to be given to the appellant of such an application and likely the appellant would have to be made a party to the proceedings: Allan v. Manitoba and North Western R. Co. (1894), 10 Man. R. 143.

20 The third exception which should be noted is this: If the receiver has expended money for the

necessary preservation or improvement of the property, he may be given priority for such an expenditure over secured creditors. The boundaries of what constitute "necessary costs of preservation" have not been clearly defined in English and Canadian jurisprudence. In Re Oriental Hotels Co.; Perry v. Oriental Hotels Co. (1871), L.R. 12 Eq. 126, a receiver was given priority for "costs of preservation", but the report of the case does not set out what was included in those words. In the subsequent decision in Re Regent's Canal Ironworks Co., Ex p. Grissell (1875), 3 Ch. D. 411, James, L.J., in dealing with a liquidator's claim for priority over debenture holders for moneys paid for preservation of properties said (at p. 427):

> The only costs for the preservation of the property would be such things as have been stated, the repairing of the property, paying rates and taxes, which would be necessary to prevent any forfeiture, or putting a person in to take care of the property.

21 In Clark On Receivers, vol. 2, s. 640, p. 1078, the law on the point is stated in this way:

> By the great weight of authority the claims against, and the indebtedness incurred by a receiver as a result of his administering the affairs, and even conducting the business of an insolvent concern of a private nature, except where absolutely essential to the preservation of its property, cannot be given priority over the claims of mortgagees or lienholders to the corpus of the property in the absence of consent or estoppel affecting said lienees.
>
> However, preservation costs may be absolutely necessary and be allowed against the lienholders. Preservation of the property from destruction, waste or loss, with or without the mortgagee's consent may include putting a person in charge of the property, as a watchman or otherwise, paying necessary repairs on the property and taxes which would prevent a forfeiture, and necessary insurance.

22 Counsel for the respondents and for the receiver argued strenuously that the moneys paid by the receiver to the appellant were necessary costs of preservation of the property and hence should be given priority over the appellant's charge. However, in my opinion, the payments cannot be regarded as a necessary cost of preserving the property. In order to be payments made for preserving property, the payments must be made for the benefit of all parties including secured creditors. The payments in the present case were made primarily for the benefit of the partners, and incidentally for the benefit of the unsecured creditors, but not for the benefit of the appellant. It is true that the appellant received payments on his charge, but the payments were made not to benefit the appellant; rather, they were made to prevent him from taking action to enforce his security.

23 The payments mentioned in the Regent's Canal case are the type of payments that in my opinion fall within the scope of payments necessary for the preservation of property for the benefit of all interested parties. If, for example, the wind had blown off the roof of the car wash so that the

premises were exposed to the elements, the repair of the roof by the receiver to prevent damage to the interior of the premises would have been for the benefit of all parties; and the receiver would have been entitled to priority over the appellant's charge for moneys expended for this purpose. Again, if the receiver had been obligated to pay taxes to prevent a tax seizure, that would have been for the benefit of all parties, including the appellant. But a payment to a mortgagee of sums to which he was legally entitled under his charge, in my judgment, falls in a different category; it is not made to preserve the property for all interested parties but only to preserve the property for a certain group of interested parties; namely, the partners and the unsecured creditors. If the order under appeal is allowed to stand, the appellant will receive little or no benefit from the payments that were made, since the receiver will have priority over his charge for those payments. I do not think, therefore, that the third exception to the general rule has any application to the facts of this case.

24 To sum up, I can see no basis for granting the receiver priority over the appellant's charge for the sum of $24,043.26 paid by the receiver to the appellant.

25 The appeal should be allowed with costs, and the order of Holland, J., of December 13, 1974, should be varied by striking out para. 2 thereof.

Appeal allowed.

TAB 4

IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation: ***Terra Nova Management Ltd. v. Halcyon Health Spa Ltd. et al,***
2005 BCSC 1017

Date: 20050705
Docket: 8894
Registry: Nelson

Between:

Terra Nova Management Ltd.

Petitioner

And

Halcyon Health Spa Ltd., Ulf Matthias Burmeister, Sabine Christa Burmeister, Community Futures Development Corporation of Central Kootenay, J & M Industries Ltd., Emco Limited, E.B. Horseman & Son Ltd., Hans-Peter Mayr, Roman Pacific Imports Ltd., 452702 B.C. Ltd. and Her Majesty the Queen in Right of the Province of British Columbia

Respondents

Before: The Honourable Madam Justice Stromberg-Stein

Reasons for Judgment

Counsel for D. Manning & Associates Inc.: G.A. Cuttler

Counsel for Arthur Andersen Inc.: W.E.J. Skelly

Date and Place of Trial/Hearing: June 9 and 10, 2005
Vancouver, B.C.

Introduction

[1] This is an application by the Receiver Manager of Halcyon Health Spa Ltd. ("Halcyon"), D. Manning & Associates Inc. ("Manning"), to determine whether the previous Receiver Manager, Arthur Andersen Inc. ("Andersen"), was entitled to use a forfeited $200,000 deposit received in consideration for a sale of Halcyon's assets, in priority to the Federal Business Development Bank ("BDC"), the first mortgagee.

Position of the Parties

[2] It is the position of Andersen that BDC knew of and approved of the appointment of Andersen as it was necessary to take control of Halcyon because the business was out of control. Andersen asserts that BDC knew at the time of the Andersen appointment that there was no guarantee BDC would be paid in full and the appointment of a receiver manager would enhance the value of Halcyon and the chance of BDC getting paid in full. Andersen argues it obtained priority for its fees, costs and expenses pursuant to the court order appointing it Receiver Manager and as of September 22, 2000 BDC knew this and took no steps to vary, alter or amend the court order. Further, Andersen argues it is entitled to retain the priority granted to it in respect of its fees, costs and expenses incurred in relation to Halcyon since its administration of the receivership was for the benefit of everyone, including BDC.

[3] It is the position of Manning that the court order appointing Andersen was not binding on BDC because the order was granted without notice to BDC. Manning asserts that at no time did BDC acquiesce or consent to, or approve of, a reordering of priorities giving Andersen priority over BDC. Manning argues Andersen assumed the risk of recovering its costs, expenses and fees from the equity remaining in

Halcyon's assets after payment to BDC. Further, Manning argues the forfeited $200,000 deposit constitutes proceeds from the sale of Halcyon's assets over which BDC held a first charge, and that Andersen's use of the deposit and failure to deliver it up to Manning constitutes a contravention of court orders made on April 14, 2001, and May 27, 2002.

Issues

1. Was the July 31, 2000 order of Metzger J, appointing Andersen Receiver Manager of Halcyon, binding on BDC?

2. Did BDC agree that Andersen would have priority over BDC?

3. Did Andersen assume the risk of recovering its costs, expenses and fees from the equity remaining in Halcyon's assets after payment to BDC?

4. Did the $200,000 non-refundable deposit for the sale Halcyon's assets of constitute proceeds from the sale of Halcyon's assets over which BDC held a first charge?

5. Did Andersen contravene the order of April 14, 2001 when it used the $200,000 deposit to pay its fees, costs and expenses in priority to BDC?

6. Did Andersen contravene the order of May 27, 2002 by failing to deliver up to Manning funds it held on deposit?

[4] In the result I conclude issues 1 and 2 are answered “No”. Issues 3, 4, and 6 are answered “Yes”. I do not have to address issue 5.

Facts

[5] Halcyon operated a resort near Nakusp, British Columbia. BDC held a first mortgage over all of Halcyon’s assets; Terra Nova Management Ltd. (“Terra Nova”) held second mortgage security. In May 2000 Halcyon was experiencing extreme financial difficulties and the health spa facilities were in a state of disarray. Halcyon defaulted on its loans to BDC and to Terra Nova. Without objection from BDC, Terra Nova privately appointed Mender Property Services Ltd. (“Mender”) as Receiver Manager of Halcyon. This appointment was short-lived due to lack of cooperation from the operational manager of Halcyon and the fact Mender was not qualified to act as a receiver manager. Mender was removed and paid in full for its fees and services.

[6] In June 2000 Terra Nova commenced the underlying proceedings against Halcyon seeking the court appointment of Andersen as Receiver Manager over Halcyon’s assets. Although BDC was aware of Terra Nova’s action, BDC was not named as a respondent and was not served. BDC did not participate in the application.

[7] On July 31, 2000, Terra Nova obtained an order from Metzger J appointing Andersen Receiver Manager over Halcyon. Metzger J ordered that Andersen could borrow up to $5,000 without leave of the court for the purpose of preserving the assets or carrying on the business of Halcyon. The order of Metzger J provided that:

> any expenditure which shall be properly made and incurred by the Receiver Manager including its fees, which shall be subject to taxation, **shall form a charge** on the undertaking, property and assets of Halcyon and the undertaking, property and assets **in priority to all charges** save those imposed by statute which cannot be postponed to the charge thus created. [Emphasis added].

[8] Andersen did not obtain an indemnity for its fees and disbursements from Terra Nova.

[9] On September 22, 2000, BDC's legal counsel received a copy of the July 31, 2000 order. BDC did not apply to set aside, vary or appeal this order, or subsequent orders that adopted the priority granted to Andersen.

[10] There is a conflict on the evidence, affidavits and cross-examination on affidavits, as to whether BDC supported the appointment of Andersen as Receiver Manager over Halcyon, or did not object to the appointment, and as to whether BDC agreed to give priority to the Receiver Manager for its fees, costs and expenses.

[11] The evidence reveals BDC was not prepared to appoint a receiver manager as sought by Terra Nova; nor was it prepared to fund the appointment of a receiver manager. When Terra Nova was considering appointing a receiver manager, BDC was considering enforcing BDC's security. Given its priority position, BDC did not consider it necessary for BDC to appoint a receiver manager to protect its security interest. At the time BDC believed there was sufficient equity in the property to cover BDC's mortgage. Although BDC did not object to Terra Nova seeking the appointment of a receiver manager and did not interfere with Terra Nova's installation of Mender or Andersen, there is no evidence that BDC ever agreed to

give up its priority to Andersen. In fact, BDC's internal reports reveal it agreed with the appointment of Andersen as Receiver Manager on the condition that the cost of the receivership would rank behind BDC's mortgage.

[12] I find, after reviewing the evidence and considering it in its entirety, that while BDC supported, or did not object to, the appointment of Andersen as Receiver Manager, at no time did BDC agree to pay Andersen's fees, costs and expenses or grant Andersen priority for its fees, costs and expenses.

[13] In the course of the receivership, Andersen made significant changes and improvements to Halcyon. Throughout the receivership, Anderson prepared receivership reports. Anderson did not provide a copy of its first receivership report, which was prepared in August, 2000, to BDC. On March 2, 2001 Anderson provided its second and third receivership reports to BDC. In the third report, Andersen requested the power to borrow up to $150,000 in priority to BDC, a request which BDC refused. Andersen applied to the court for permission to borrow $150,000. BDC had notice of this proceeding and received materials in support of Andersen's application but did not appear at the application.

[14] On April 4, 2001, Andersen obtained an order from Humphries J increasing the amount of Andersen's permitted borrowing to $150,000. The order also provided that borrowed funds in excess of $5,000 would rank "**in priority immediately behind the Business Development Bank of Canada charge and** the reasonable fees, costs and expenses **charge of the Receiver Manager** (the "Receiver Manager Charge") **created by the Metzger Order**, but in priority to all other charges against

the undertaking, property and assets of Halcyon save those imposed by statute which cannot be postponed as a matter of law to the charge thus created".

[15] Despite securing the power to borrow additional funds, no one would lend Andersen funds. Andersen threatened to cease operations of Halcyon but carried on. As of April 2001 all parties believed there was sufficient equity in Halcyon to at least pay out BDC. Andersen had an appraisal indicating a value of $2.6 million for Halcyon's assets. BDC was owed about $1.5 to $1.7 million.

[16] On April 26, 2001, Andersen asked BDC to agree to a priority charge for $60,000, for specific items such as insurance costs, asserting the appraisal made it "clear BDC's equity is secure", and suggesting Andersen would be forced to shut down Halcyon's operation. BDC did not respond to Andersen's request for a priority charge for $60,000.

[17] On October 23, 2001, BDC commenced foreclosure proceedings but took no further steps until Andersen's attempt to sell the property fell through in the spring of 2002.

[18] Anderson had been authorized to offer the Halcyon property for sale as October 23, 2000 and on December 24, 2001, Andersen received an offer to purchase Halcyon's assets for $2.49 million. Pursuant to that offer, Andersen received non-refundable deposits totalling $200,000. On April 11, 2001, the offer was approved by the court. The interests of BDC were not affected by the court order as BDC was a permitted encumbrance and its mortgage would be discharged on payment of the debt owing it.

[19] The court was not informed that Andersen would claim priority over the $200,000 deposit in priority if the sale did not complete.

[20] The purchasers sought an extension of the closing date, which extension Andersen refused. BDC was not consulted. The sale did not complete. On May 16, 2002, Andersen took the position that the purchasers were in breach of their obligations and the $200,000 deposit was forfeited to Andersen. Andersen advised BDC it would take steps to be discharged as Receiver Manager and informed BDC to take immediate steps as deemed appropriate to preserve and protect their security interest in Halcyon.

[21] Andersen never requested BDC to pay its fees and had never received any fees from BDC. Andersen intended to claim priority over the $200,000 deposit to pay its fees, costs, and expenses, but did not tell BDC of this intention.

[22] BDC entered into an interim agreement with Andersen whereby Andersen would remain Receiver Manager until BDC could arrange for the appointment for another Receiver Manager. On May 27, 2002, Martinson J ordered Andersen discharged and Manning appointed as Receiver Manager of Halcyon. The order of Martinson J required Andersen to protect and preserve Halcyon's assets and to deliver any property or assets to Manning. Andersen's solicitor was present. There was no mention of the $200,000 deposit.

[23] On May 27, 2002, Manning asked Andersen to deliver up the $200,000 deposit. Andersen did not respond. On May 29, 2002, Andersen's lawyer wrote BDC's lawyer stating "should the proceeds of sale of the Halcyon property exceed

what Business Development Bank of Canada is owed, payment should first be made to Arthur Andersen Inc. in the amount it is owed before any further distribution is made". This is a clear indication, as supported by all the evidence, that Andersen never claimed a priority over BDC for its fees, costs and expenses and never thought it had any priority.

[24] Andersen used the $200,000 deposit to pay its fees, costs and expenses. These have yet to be taxed.

[25] On February 3, 2003 Halcyon's assets were sold for $1.37 million. By this time BDC was owed about $2,075,000 by Halcyon.

Analysis

1. Was the July 31, 2000 order of Metzger J, appointing Andersen Receiver Manager of Halcyon, binding on BDC?

[26] It is fundamental that a court order is not binding on a person who has no notice of it and a court has no power to authorize charges and expenses of a receivership in priority to a prior mortgagee without the sanction of such mortgagee. This general rule was described by Mr. Justice Houlden in ***Kowal Investments et al.*** **v.** ***Deeder Electric Ltd.*** (1975), 9 O.R. (2d) 84, 59 D.L.R. (3d) 492 at 496 (C.A.) [hereinafter ***Kowal*** cited to D.L.R], by reference to the following passage from *Clark on Receivers*, 3rd ed. by Ralph Ewing Clark of the Cincinnati Bar, vol. 2, s. 638, pp.1070-1:

> No receivership may be necessary to protect or realize the interests of lienholders. In such cases the mortgagees and lienholders cannot be

> deprived of their property nor of their property rights and the receivership property cannot as a rule be used nor the business carried on and operated by the receiver in such a way as to subject the mortgagees and lienholders to the charges and expenses of the receivership. A court under such circumstances has no power to authorize expenses for improving or making additions to the property or carrying on the business of the defendant at the expense of prior mortgagees or lienholders without the sanction of such mortgagees or lienholders.

[27] This passage was subsequently quoted with approval by the British Columbia Court of Appeal in ***Lochson Holdings Ltd*****. v. *****Eaton Mechanical Inc*****.** (1984), 33 R.P.R. 100, 55 B.C.L.R. 54 at 57 (C.A.).

[28] In the present case, BDC was not named as a respondent and was not served with notice of the proceedings. BCD was not served with the court order and did not receive notice of the terms of the order impacting on its priority position. BCD's lawyer received the order September 22, 2000. However, in the circumstances, knowledge of the contents of the order affecting BDC's priority position cannot be imputed to BDC.

[29] I conclude that BDC did not have notice of the court order and therefore the court order appointing Andersen was not binding on BDC.

2. Did BDC agree that Andersen would have priority over BDC?

[30] Although a secured creditor in a priority position may not be bound by a court order granting priority to another party, as held in ***Kowal,*** a creditor in a superior priority position may nevertheless forgo that priority position by some other means. For example, three exceptions to the general rule that a receiver has no priority for

his expenses over a prior secured creditor were recognized by the Ontario Court of Appeal in ***Kowal***, and by the British Columbia Court of Appeal in ***Lochson***. The three exceptions as provided in ***Kowal*** at 496, 497, and 499, respectively, are:

> 1. If a receiver has been appointed at the request, or with the consent or approval, of the holders of security, the receiver will be given priority over the security holders;
>
> 2. If a receiver has been appointed to preserve and realize assets for the benefit of all interested parties, including secured creditors, the receiver will be given priority over the secured creditors for charges and expenses properly incurred by him; and
>
> 3. If the receiver has expended money for the necessary preservation or improvement of the property he may be given priority for such expenditure over secured creditors.

[31] Andersen asserts that the first two exceptions apply to the circumstances of this case.

[32] Before considering the exceptions, a preliminary issue appears to be whether a receivership was in fact, necessary. This requirement was made clear in ***Deloitte, Haskins &Sells Ltd*. v. *P.R.D. Travel Investments Inc*.** (1984), 10 D.L.R. (4th) 572, (sub nom. Re ***Winmil Holidays Co.***) 55 B.C.L.R. 38 at 46 (C.A.) ("*P.R.D.*"), where Esson J.A. rephrased the general rule set out in ***Kowal*** as follows:

> if a receivership is not necessary to protect or realize interests of mortgagees and lien holders, the court cannot authorize expenses for improving or making additions to the property or carrying on the business of the defendant at the expense of prior mortgagees without their agreement.

[33] Thus the exceptions only apply where the receivership is not necessary. In the present case, there is no evidence that the appointment of a receiver manager

was a necessity. In fact, the evidence suggests BDC did not consider the appointment of a receiver manager necessary in light of its belief that the amount of equity remaining in the property was sufficient.

[34] In any event, I will consider whether the exceptions apply to entitle Andersen to priority over the secured creditors for its fees and expenses.

[35] The first exception is if a receiver has been appointed at the request, or with the consent or approval, of the holders of security, the receiver will be given priority over the security holders. The onus is on Andersen, in claiming priority over BDC's first charge, to prove BDC consented to, approved of, or acquiesced to, Anderson's appointment.

[36] There is no evidence that BDC consented Andersen's appointment. The fact that BDC did not object to the appointment of Andersen as Receiver Manager, without direct evidence to the contrary, cannot supplant BDC's priority position, particularly in light of Mr. Lougheed's evidence (the BDC representative on the file) that in his dealings with Mr. Gilchrist, Andersen's representative, it was clear that BDC would not give up its priority position to fund a receiver manager and BDC did not need a receiver manager as it could simply foreclose on Halcyon's assets to realize its indebtedness. These are sophisticated parties. There is no written document evidencing BDC's consent or approval to give up priority.

[37] In my view, there is no evidence of the conduct of BDC which would suggest it approved or consented to the appointment of Andersen. Andersen relies on ***Federal Business Development Bank* v. *Persic*** (1981), 32 B.C.L.R. 75, [1981]

B.C.J. No. 1443 (QL) (C.A.), for the proposition that the conduct of a prior security holder subsequent to the appointment of a receiver can be a basis for a receiver to assert that its fees, costs and expenses should take priority over that prior security holder, even where the prior security holder did not consent to the order establishing such priority.

[38] I find ***Persic*** distinguishable from the case at bar. In ***Persic*****,** Anderson J. A. found, at paragraph 20, that the prior security holder "not only acquiesced in his dealing with all of the assets … but actively encouraged the receiver-manager to continue his efforts". The evidence in the case at bar establishes that while BDC did not object to the appointment of Andersen as Receiver Manager, it did not actively encourage Andersen. In ***Persic***, the prior security holder, guaranteed, in writing, the receiver managers fees and arranged for a line a credit to be granted to the receiver manager. Anderson J. A. found that by this conduct the prior security holder had made all the assets subject to a charge in favour of the receiver manager. There is no evidence that BDC acted in a similar fashion in the present case.

[39] In my view, there is also no evidence that BDC acquiesced to the appointment of Andersen. Andersen relies on ***Darby House Mortgage Corp.*** **v. *Atherton Realty Company Ltd*****.** (1986), 9 B.C.L.R. (2d) 198, [1986] B.C.J. No. 1404 (QL) (C.A.), for the proposition that the acquiescence of a prior security holder by the appointment and conduct of a receiver will later bar that prior security holder from asserting a priority to proceeds of sale over the fees, costs, and expenses of the receiver.

[40] In ***Darby House***, a receiver manager was appointed by the court without notice to the first mortgagee. The Court of Appeal upheld the trial judge's decision to allow all of the receiver manager's proper expenses to rank in priority to the first charge. The circumstances constituting acquiescence were not clear in either judgment. With respect, I find that ***Darby House*** is of little assistance to Andersen in regard to the acquiescence argument under the first exception to the general rule.

[41] The second exception is if a receiver has been appointed to preserve and realize assets for the benefit of all interested parties, including secured creditors, the receiver will be given priority over the secured creditors for charges and expenses properly incurred by him.

[42] Andersen argues it falls within the second exception and relies on ***Stenner Financial Services Ltd. (Re)***, [1988] B.C.J. No.965 (QL) (S.C.), and ***P.R.D****, supra*. In ***Stenner***, the Securities Commission obtained an ex parte order appointing a receiver over all property of Stenner, whose ability to function had been paralyzed by a freezing order of the Securities Commission for alleged violations of the ***Securities Act***. The Court, in finding that the Receiver's expenses and fees constituted a first charge against Stenner's assets in priority of all other claims, stated "the appointment of the receiver herein was an imperative given the situation of Stenner; its license had expired; it undertaking was frozen. Under the circumstances the interests of all the creditors were at risk". In the present case, Halcyon was experiencing financial difficulties, the spa facilities were in disarray and the appointment of a receiver manager may have been desirable from Terra Nova's

perspective; however, there is no objective evidence to suggest that the appointment of the receiver manager was imperative, as in ***Stenner***.

[43] In ***P.R.D.***, a receiver had been appointed by the court ex parte and the Court found that the receiver's fees and expenses enjoyed priority over P.R.D., which held prior security. Counsel for Andersen recognized that ***P.R.D.*** was somewhat factually dissimilar from the case at bar, in that in ***P.R.D.***, the prior security holder attended the initial hearing and raised some objections to the order, whereas BDC did not attend Terra Nova's application seeking Andersen's appointment. This, in addition to the fact that P.R.D. applied to have a receiver of its choice appointed in place of the court appointed receiver, make ***P.R.D.*** factually distinguishable from the case at bar.

[44] I agree with counsel for Manning that priority cannot be removed by stealth or suggestion. For a reordering of priorities to occur in these circumstances where a receivership was not necessary, one of the exceptions must apply. Andersen bears the onus of proving it fits within one of the exceptions. I find that Anderson has not discharged this onus.

3. Did Andersen assume the risk of recovering its costs, expenses and fees from the equity, if any, remaining in Halcyon's assets after payment to BDC?

[45] Andersen never requested BDC to pay its fees and had never received any fees from BDC. The evidence establishes Andersen took a calculated business risk in carrying on Halcyon's operation and incurring further liabilities, and in advancing its own funds from its parent company and obtaining credit from suppliers, in the

belief there was equity in Halcyon behind BDC if the property were sold to recover its fees, costs and expenses. I find Andersen knowingly assumed the risk that there would be sufficient equity in Halcyon's assets after BDC was paid to recover its fees, costs and expenses.

> 4. Did the $200,000 non-refundable deposit for the sale Halcyon's assets constitute proceeds from the sale of Halcyon's assets over which BDC held a first charge?

[46] There is no real issue about the characterization of the $200,000 deposit in light of the concession made by Andersen's counsel in argument. I am satisfied the deposit received was toward the purchase price of Halcyon's assets and BDC's security applied over this money: ***Alma College* v. *United Church of Canada*** (1997), 42 O.T.C. 331, [1997] O.J. No. 4129, aff'd [1998] O.J. No. 4896 (C.A.).

> 6. Did Andersen contravene the order of May 27, 2002 by failing to deliver up to Manning funds it held on deposit?

[47] Having found the deposit received was toward the purchase price of Halcyon's assets, it follows that Andersen was required to deliver up the deposit to Manning in accordance with the order of May 27, 2002. Andersen knew the order required payment of funds under its control to Manning. Andersen could not unilaterally claim the deposit funds and pay itself, its parent company and its various suppliers as it did.

[48] Andersen submits that it fulfilled its responsibilities as a receiver under its court appointment as an officer of the court. The importance of remunerating receivers appointed by the court was noted in ***Braid Builders Supply & Fuel Ltd*. v.**

Genevieve Mortgage Corp Ltd. (1972), 29 D.L.R. (3d) 373, [1972] M.J. No.31 (Man C.A.). In ***Braid***, Dickson J.A. (as he then was), noted at p. 373 that "the receiver's remuneration must come out of the assets under the control of the Court, and not from the pocket of those who sought his appointment". This was in fact what the Order of Metzger J sought to achieve by the terms giving Andersen a priority charge over all other charges for its fees and expenses. However, as is made clear in ***Kowal*** this principle cannot apply where the order granting priority to the assets was made without notice to prior security holders.

[49] Andersen also submits that it fulfilled its responsibilities as receiver in reliance of the terms of the order of Metzger J giving it priority over all other charges and encumbrances for its fees and expenses. The evidence of Andersen's repeated requests of BDC for additional funding suggest that Andersen may have had some inclination that BDC did not support a reordering of priorities. Although Andersen may have incurred some expense in reliance of the order of Metzger J, as between the parties, BDC should not be visited with this loss.

Conclusion

[50] Andersen is ordered to pay the $200,000 deposit to Manning, as Receiver Manager, together with Court Order interest. Manning is entitled to its costs of this application. The order arising from this application may be entered in the Vancouver Registry.

"S.S. Stromberg-Stein, J."
The Honourable Madam Justice S.S. Stromberg-Stein

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COURT OF APPEAL FOR BRITISH COLUMBIA

Citation: ***Re Halcyon Health Spa Ltd. (Receiver-Manager of),*** 2006 BCCA 458

Date: 20061006
Docket: CA033217

Between:

D. Manning & Associates, Inc., in its capacity as Receiver-Manager of Halcyon Health Spa Ltd.

Respondent
(Applicant)

And

Arthur Andersen Inc.

Appellant
(Respondent)

Before: The Honourable Madam Justice Ryan
The Honourable Mr. Justice Donald
The Honourable Mr. Justice Smith

Oral Reasons for Judgment

W.E.J. Skelly
B.R.H. Johnston — Counsel for the Appellant

G.A. Cuttler — Counsel for the Respondent

Place and Date: Vancouver, British Columbia
6 October 2006

[1] **DONALD, J.A.**: This is an appeal from the order of Madam Justice Stromberg-Stein pronounced 5 July 2005, that Arthur Andersen Inc. ("Andersen") pay $200,000.00 to D. Manning & Associates Inc. ("Manning") plus court order interest and costs. The neutral citation for the judgment is 2005 BCSC 1017 and can also be found at (2005), 13 C.B.R. (5th) 273.

[2] The order proceeded from the finding that Andersen's fees and expenses as receiver-manager of Halcyon Health Spa Ltd. ("Halcyon") do not take priority over first mortgage security.

[3] Halcyon operated a resort facility near Nakusp, British Columbia. It granted a first mortgage over the resort and a general security agreement over all of its assets to the Business Development Bank of Canada (“BDC”), a second mortgage and a general security agreement over all of its assets to Terra Nova Management Ltd. (“Terra Nova”), and a third mortgage to another party.

[4] In the spring of 2000, Halcyon suffered extreme financial problems, causing it to default on payments to BDC and Terra Nova. In June 2000, Terra Nova commenced proceedings against Halcyon and sought the appointment of Andersen as receiver-manager over Halcyon’s assets. While BDC was aware of Terra Nova’s action, it was not named as a respondent, was not served, and did not participate in the application.

[5] On 31 July 2000, Metzger J. granted an order appointing Andersen receiver-manager over Halcyon. Under the terms of the order, Andersen could borrow up to $5,000.00 without leave for the purpose of preserving assets and carrying on the

business of Halcyon. The order also provided that any properly incurred expenditure, including Andersen's fees, will form a charge on Halcyon's assets in priority to non-statutory charges. Andersen did not obtain indemnity for fees from Terra Nova.

[6] BDC's solicitor received a copy of the order, but BDC did not apply to set aside, vary or appeal this order or subsequent orders that adopted its terms. The trial judge found there was no evidence, however, that it agreed to grant Andersen priority or to pay Andersen's fees.

[7] On 23 October 2001, BDC commenced foreclosure proceedings. On 24 December 2001, Andersen received an offer to purchase Halcyon's assets for $2.49 million. Andersen received $200,000.00 in non-refundable deposits pursuant to the offer. On 11 April 2002, the offer was approved by the court. The supporting affidavit filed by Andersen shows that BDC was to be paid in full from the proceeds. At that point, Andersen did not indicate to the court that it would claim priority to the deposit if the sale did not complete. The purchasers sought an extension of the closing date and Andersen refused, without consulting BDC. On 16 May 2002, Andersen retained the deposit on the basis that the purchasers were in breach of the contract. Although the purchasers indicated they would bring an action to recover the deposit, no proceedings were commenced.

[8] Andersen then advised BDC that it would seek to be discharged as receiver-manager. It did not indicate to BDC that it would claim priority to the deposit for its

fees and expenses. On 27 May 2002, Andersen was discharged and Manning was appointed receiver-manager by an order of Martinson J.

[9] The trial judge found that there was ample equity in the property securing BDC's mortgage debt at the time of Andersen's appointment, and so the appointment was not necessary to protect BDC's interest. That being so, the trial judge went on to find that since the order of Metzger J. was granted without notice to BDC, it was not bound by the priority term, subject to certain exceptions. They are outlined in the reasons for judgment, 2005 BCSC 1017, in this way:

> [30] Although a secured creditor in a priority position may not be bound by a court order granting priority to another party, as held in *Kowal* [*Kowal Investments et al. v. Deeder Electric Ltd.* (1975), 9 O.R. (2d) 84, 59 D.L.R. (3d) 492 (C.A.)], a creditor in a superior priority position may nevertheless forgo that priority position by some other means. For example, three exceptions to the general rule that a receiver has no priority for his expenses over a prior secured creditor were recognized by the Ontario Court of Appeal in *Kowal*, and by the British Columbia Court of Appeal in *Lochson* [*Lochson Holdings Ltd. v. Eaton Mechanical Inc.* (1984), 33 R.P.R. 100, 55 B.C.L.R. 54 (C.A.)]. The three exceptions as provided in *Kowal* at 496, 497, and 499, respectively, are:
>
> 1. If a receiver has been appointed at the request, or with the consent or approval, of the holders of security, the receiver will be given priority over the security holders;
>
> 2. If a receiver has been appointed to preserve and realize assets for the benefit of all interested parties, including secured creditors, the receiver will be given priority over the secured creditors for charges and expenses properly incurred by him; and
>
> 3. If the receiver has expended money for the necessary preservation or improvement of the property he may be given priority for such expenditure over secured creditors.
>
> [31] Andersen asserts that the first two exceptions apply to the circumstances of this case.

> [32] Before considering the exceptions, a preliminary issue appears to be whether a receivership was in fact, necessary. This requirement was made clear in *Deloitte, Haskins &Sells Ltd*. v. *P.R.D. Travel Investments Inc*. (1984), 10 D.L.R. (4th) 572, (sub nom. Re *Winmil Holidays Co.*) 55 B.C.L.R. 38 at 46 (C.A.) ("*P.R.D.*"), where Esson J.A. rephrased the general rule set out in *Kowal* as follows:
>
> > if a receivership is not necessary to protect or realize interests of mortgagees and lien holders, the court cannot authorize expenses for improving or making additions to the property or carrying on the business of the defendant at the expense of prior mortgagees without their agreement.
>
> [33] Thus the exceptions only apply where the receivership is not necessary. In the present case, there is no evidence that the appointment of a receiver manager was a necessity. In fact, the evidence suggests BDC did not consider the appointment of a receiver manager necessary in light of its belief that the amount of equity remaining in the property was sufficient.
>
> [34] In any event, I will consider whether the exceptions apply to entitle Andersen to priority over the secured creditors for its fees and expenses.

[10] Andersen accepts that the trial judge applied the correct legal principles. I set out the errors in judgment as alleged in the appellant's factum:

> 36. In particular, the Chambers Judge erred in law or in mixed law and fact:
>
> i) In concluding that a receivership was not necessary to protect the secured creditors' interests; and
>
> ii) Alternatively, if a receivership was not necessary to protect the secured creditors' interest, in concluding that:
>
> a. the BDC had not acquiesced in the Appellant's appointment as receiver-manager; and,
>
> b. that the Appellant's appointment as receiver-manager was not for the benefit of all interested parties.

[11] As to the facts, the trial judge found that there is:

1. "... no evidence that BDC consented [to] Andersen's appointment." [Reasons for judgment, para. 36.]

2. "... no evidence of the conduct of BDC which would suggest it approved or consented to the appointment of Andersen." [Reasons for judgment, para. 37.]

3. "... no evidence that BDC acquiesced to the appointment of Andersen." [Reasons for judgment, para. 39.]

4. "... no objective evidence to suggest that the appointment of the receiver-manager was imperative...." [Reasons for judgment, para. 42]

[12] But for one matter, the record fully supports these findings. The matter relates to the trial judge's statement at paragraph 28 of her reasons that even though BDC's lawyer received a copy of the order, the knowledge of the contents of the order cannot be imputed to BDC. Without actual proof that the lawyer withheld the order from his client, I do not see how BDC can avoid being fixed with the knowledge of the order. However, I do not think this is a significant error.

[13] Appellate review of inferences from facts must be on the standard of palpable and overriding error: ***Housen v. Nikolaisen***, [2002] 2 S.C.R. 235 ¶ 22. The inference that BDC did not acquiesce is supportable on the evidentiary findings that are not open to question.

[14] In the circumstances of this case, BDC did not have a positive duty to apply to vary the order of Metzger J. in order to preserve its priority. Thus, BDC was entitled to wait until realization to deal with the difficulty created by the order. Having taken the order without naming BDC as a party, giving notice of the application, or securing its consent, Andersen took the risk of a shortfall.

[15] I would dismiss the appeal.

[16] **RYAN, J.A.**: I agree.

[17] **SMITH, J.A.**: I agree.

[18] **RYAN, J.A.**: The appeal is dismissed.

"The Honourable Mr. Justice Donald"

TAB 5

2 of 2 DOCUMENTS

Indexed as:

Alma College v. United Church of Canada

Between
Alma College, (applicant/respondent in appeal), and
United Church of Canada and Office of the Public Trustee of Ontario and Canadian Imperial Bank of Commerce and Ronald Falck and Joan Ferrier Giles, (respondents/appellants in appeal)

[1996] O.J. No. 1309

62 A.C.W.S. (3d) 710

No. C20569

Ontario Court of Appeal
Toronto, Ontario

Robins, McKinlay and Rosenberg JJ.A.

Heard: April 15, 1996.
Judgment: April 18, 1996.

(4 pp.)

Mortgages -- Priorities -- Between mortgagees and receiver.

This was an appeal by second and third mortgagees, supported by the first mortgagee, relating to parts of the order appealed from that rendered the mortgage creditors subject in priority to fees and disbursements incurred by the court-appointed receiver of the mortgagor.

HELD: The appeal succeeded and the order appealed from was varied. The general rule was that the security of a prior secured creditor was not to be subjected to liability for fees or disbursements of a receiver. The circumstances of this case were not such as to bring it outside that general rule.

Counsel:

Thomas F. Delorey, for the appellants.
Thomas Robson, for CIBC.
A. Duncan Grace, for Price Waterhouse.
R.F. Leach, for the Public Trustee.
John Sanders, for Alma College.
Nancy Swartz, in person.

The following judgment was delivered by

1 THE COURT (endorsement):-- This is an appeal from the order of Browne J. dated November 25, 1994. The appeal is brought by Ronald Falck and Joan Ferrier Giles, the holders of the second and third mortgages registered against the property of Alma College, and is supported by the Canadian Imperial Bank of Commerce, the first mortgagee. The appeal relates to those parts of the order (paras. 3(j), 4(f), 5, 8, 9, 12, 14 and 18) that render the mortgages creditors subject in priority to fees and disbursements incurred by Price Waterhouse Limited, the receiver of Alma College appointed pursuant to the order of Browne J.

2 We are of the opinion that the appeal must succeed. The general rule that the security of a prior secured creditor is not to be subjected to liability for fees and disbursements of a receiver governs the situation at hand. The receiver's right to indemnity in so far as the subject property is concerned is concerned to the debtor's equity in the property. The circumstances of this case are not such as to bring it within any of the exceptions to the general rule, entitling a receiver to priority over the secured interests of mortgagees. See Kowal Investments Limited v. Deeder Electric Limited (1975), 9 O.R. (2d) 84.

3 The mortgages in question have long been in default and notices exercising power of sale were served prior to the appointment of the receiver. The appellants are entitled to enforce their security; there is no reason to stay their right to do so. They have no interest in the investigation that has been or that may be conducted by the receiver into the affairs of Alma College or into assets that may be held by it in trust for restricted charitable purposes. As matters presently stand, on the figures presented to the court the appellants would be required to pay the entire costs of the receivership. Their recovery on the realization of their security cannot be subjected to charges relating to matters which are of no concern to them as mortgagees.

4 Accordingly, the order of Browne J. will be varied in the following respects:

1. Re Paragraphs 3(j) and 4(f)

5 The costs and expenses of the receiver and the interim receiver as provided for in these

paragraphs shall be subject and not in priority to the mortgage encumbrances save in the following respect. Since the date of the order the receiver has taken steps and made efforts to sell the mortgaged property and to preserve and protect the property. The mortgagees acknowledge that these actions have to some extent enured to their benefit and that the receiver is entitled to be reimbursed for the disbursements and fees that it has reasonably incurred for these purposes. Such reimbursement shall be payable in priority to the claims of the mortgagees but shall not exceed the sum of $50,000 exclusive of the amounts for which the receiver has already been reimbursed by the first mortgagee. If the parties are unable to agree on the amount of the fees or disbursements properly payable for such purposes, the receiver may have its account assessed.

2. Re Paragraph 5

6 Any costs incurred by the receiver in conducting the investigation contemplated in this paragraph shall be subject and not in priority to the mortgage encumbrances.

3. Re Paragraph 8

7 Any costs incurred by the receiver pursuant to the terms of this paragraph shall be subject ad not in priority to the mortgage encumbrances.

4. Re Paragraph 9

8 The provisions of this paragraph shall not be applicable to any action taken by the mortgagees to enforce their security.

5. Re Paragraphs 12 and 14

9 Any borrowings made by the receiver or monies received by it in regard to the mortgaged property pursuant to the provisions of these paragraphs shall be subject to the claims of the mortgagees.

6. Re Paragraph 18

10 The costs of the parties (other than the mortgagees) payable pursuant to this paragraph shall be subject in priority to the mortgage encumbrances.

11 An order may issue accordingly. There will be no order as to the costs of this appeal or the motion before Laskin J.A.

ROBINS J.A.
McKINLAY J.A.
ROSENBERG J.A.

qp/s/lmm/DRS/DRS/DRS

TAB 6

British Columbia Court of Appeal
Lochson Hldg. Ltd. v. Eaton Mech. Inc.
Date: 1984-06-06

D.I. Knowles, for Federal Business Development Bank.

C.D. Skillings, for receiver, Jamieson.

R.J. Meyer, for Canadian Imperial Bank of Commerce.

(Victoria Nos. 125/82, 1170/78, 2513/79 & 504/79)

6th June 1984. Excerpt from the transcript.

[1] HINKSON J.A.:– This is an appeal in mortgage foreclosure proceedings from the decision of a judge fixing priorities. The circumstances giving rise to the foreclosure proceedings were that in September 1977 Lochson Holdings Ltd. sold a hotel and the land it was situated on to Eaton Mechanical Inc., taking a mortgage back. Eaton then sold the land and hotel to Marrick Development Corporation. The Federal Business Development Bank had first and second mortgages over the land. Lochson's mortgage was thus a third mortgage.

[2] In 1978 Lochson began foreclosure proceedings pursuant to its mortgage. On 10th August 1978 Stewart L.J.S.C. granted an order nisi and appointed a Mr. Jamieson, who was an officer of Lochson, as receiver of the lands and premises. Contained in the order were a number of provisions with respect to the powers of the receiver and the priorities in the event a sale occurred.

[3] At the time that order was made, the Federal Business Development Bank not only had no notice of the application, but had no knowledge of Lochson's foreclosure proceedings. Subsequent to the making of that order Mr. Jamieson, in his capacity as receiver, borrowed approximately $36,000 from the Canadian Imperial Bank of Commerce. He spent that amount on renovations of the hotel. On 23rd February 1979 the Federal Business Development Bank began foreclosure proceedings under its mortgages. Lochson was named as a party. On 14th March 1979 an-order nisi of foreclosure was granted. Counsel for Lochson approved the form of that order. On 5th October 1979 the Canadian Imperial Bank of Commerce moved to be joined as a party in the foreclosure proceedings of both Lochson and the Federal Business Development Bank. Those motions were granted.

[4] On 14th March 1980 the hotel premises and the lands were sold for $150,000. The court granted approval of the sale. Ultimately an application came before Tyrwhitt-Drake

L.J.S.C. and on 23rd June 1982 he made an order on the application of Mr. Jamieson as receiver, fixing the priorities with respect to those entitled to share in the funds realized on the sale of the hotel [reported at 43 C.B.R. (N.S.) 179]. It is from that order that the present appeal is taken.

[5] It is fundamental that a person is not to be bound by a court order of which he has no notice. In the Lochson foreclosure proceedings the Federal Business Development Bank was not named as a respondent nor, as I have indicated, did it have notice of the application, That, then, is the starting point in these proceedings, namely, that the Federal Business Development Bank cannot be bound by the order made by Stewart L.J.S.C.

[6] The position of Mr. Jamieson and the Canadian Imperial Bank of Commerce is that the priority fixed by Tyrwhitt-Drake L.J.S.C. should be upheld, By his order the first mortgage of Federal Business Development Bank ranks second in priority after the Crown Provincial for taxes, and ahead of Mr. Jamieson as receiver for his charges, costs and disbursements. Thus Mr. Jamieson, as receiver, would come in priority ahead of the second mortgage of the Federal Business Development Bank, but after its first mortgage. As the receiver and the Canadian Imperial Bank of Commerce are unable to rely upon the order made by Stewart L.J.S.C. on 10th August 1978, it has been necessary to fall back on the position at common law in order to sustain the priority granted by Tyrwhitt-Drake L.J.S.C.

[7] Counsel referred to the decision in Oberman v. Mannahugh Hotels Ltd.; Mannahugh Hotels Ltd. v. Oberman; Assiniboine Credit Union Ltd. v. Mannahugh Hotels Ltd., 34 C.B.R. (N.S.) 181, [1980] 5 W.W.R. 487 at 493-97, 4 Man. R. (2d) 312, and to the decision in *Re Br. Power Traction & Lighting Co.; Halifax Joint Stock Banking Co. v. Br. Power Traction & Lighting Co.,* [1906] 1 Ch. 497, but in my opinion those cases only touch peripherally upon the problem we are here concerned with, and really do not resolve the issue with which we are faced, namely, whether the charges and expenses of the receiver take priority over the second mortgage held by the Federal Business Development Bank.

[8] In my opinion, the issue is to be resolved on the basis of the decision of the Ontario Court of Appeal in *Robert F. Kowal Invt. Ltd. v. Deeder Elec. Ltd.* (1975), 9 O.R. (2d) 84, 21 C.B.R. (N.S.) 201, 59 D.L.R. (3d) 492 (C.A.). In that case a secured creditor received no notice of the application to appoint a receiver and the issue arose as to whether or not and upon what basis the secured creditor could become bound by the acts of the receiver so that the receiver would be entitled to priority over the secured creditor, Houlden J.A., in

delivering the judgment of the court, made reference to Clark on Receivers, 3rd ed. (1959), and quoted from that text at p. 88 of the judgment, as follows:

> "When a court appoints a general receiver of the property of an individual or a corporation, at the isntance of a creditor other than a mortgage lienholder, part or all of this property may be covered by liens or mortgages. The general purpose of a general receivership is to preserve and realize the property for the benefit of the creditors in general. No receivership may be necessary to protect or realize the interests of lienholders. In such cases the mortgagees and lienholders cannot be deprived of their property nor of their property rights and the receivership property cannot as a rule be used nor the business carried on and operated by the receiver in such a way as to subject the mortgagees and lienholders to the charges and expenses of the receivership. A court under such circumstances has no power to authorize expenses for improving or making additions to the property or carrying on the business of the defendant at the expense of prior mortgagees or lienholders without the sanction of such mortagees or lienholders."

I understand that statement to express the position at law.

[9] Then, Houlden J.A. continued at p. 88:

> There are certain exceptions to the general rule. (I do not propose to give an exhaustive list of such exceptions but to refer only to the exceptions which, in my opinion, have some relevance for the facts of this case.) The first exception is this: If a receiver has been appointed at the request, or with the consent or approval, of the holders of security, the receiver will be given priority over the security holders. One would ordinarily expect that in these circumstances the order permitting the receiver to borrow would clearly provide that the security given by the receiver for his borrowings would have priority over the claims of secured creditors. However, even if the order failed to so provide, if the secured creditors have applied for, consented to, or approved of, his appointment, the receiver will have priority for charges and expenses properly incurred by him.

Pausing there for a moment, in my opinion the receiver and thus the Canadian Imperial Bank of Commerce do not fall within the first exception.

[10] Then Houlden J.A. continued to discuss a second exception and he said this at p. 89:

> The second exception is this: If a receiver has been appointed to preserve and realize assets for the benefit of all interested parties, including secured creditors, the receiver will be given priority over the secured creditors for charges and expenses properly incurred by him.

Mr. Meyer, on behalf of the Canadian Imperial Bank of Commerce, sought to come within that second exception. But Houlden J.A., after stating that to be a second exception, said this at p. 91 in discussing it:

> Although the Court appears to have power to create such a charge if it is necessary for the preservation of the property for the benefit of all parties, certainly, notice

> would have to be given to the appellant [I interpolate – the secured creditor] of such an application and likely the appellant would have to be made a party to the proceedings,

[11] Now, on the facts of the present case, if that be the situation, then clearly the second exception has no application because no notice was given to the Federal Business Development Bank nor was it made a party to the proceedings.

[12] The third exception discussed by Houlden J.A. is'the situation where the receiver has expended money for necessary preservation or improvement of the property. Houlden J.A. says at p. 91:

> If the receiver has expended money for the necessary preservation or improvement of the property, he may be given priority for such an expenditure over secured creditors.

And then he discusses two cases dealing with the meaning of “necessary costs of preservation”. One of the cases he refers to is *Re Regent's Canal Ironwks. Co.; Ex parte Grissell* (1875), 3 Ch. D. 411 (C.A.), where James L.J. said at p. 427:

> The only costs for the preservation of the property would be such things as have been stated, the repairing of the property, paying rates and taxes, which would be necessary to prevent any forfeiture, or putting a person in to take care of the property.

He also refers to a passage from Clark on Receivers, 3rd ed. (1959), and then he gives some illustrations of his appreciation of steps taken to preserve the property, and he says at p. 92:

> If, for example, the wind had blown off the roof of the car wash so that the premises were exposed to the elements, the repair of the roof by the receiver to prevent damage to the interior of the premises would have been for the benefit of all parties; and the receiver would have been entitled to priority over the appellant's charge for moneys expended for this purpose.

[13] An analysis of the three exceptions indicates that with regard to the first and second, the secured creditor must either apply for, consent to, or approve of, the appointment of a receiver or have notice under the second exception. The third exception, it seems to me, deals with a different type of situation, really one where there are circumstances which require the receiver to do something to preserve the property in an emergency situation where there is no time to come to the court beforehand and give notice to the creditors beforehand of what he intends to do, and thus obtain the approval of the court, and so he comes to the court after the event and in appropriate circumstances the court will approve the action of the receiver in those circumstances.

[14] In my opinion, on the facts of the present case the receiver does not come within the third exception.

[15] So, I go hack to what Houlden J.A. said with respect to the common law position, namely, that a court under such circumstances has no power to authorize expenses for improving or making additions to the property for carrying on the business of the defendant at the expense of prior mortgagees or lienholders without the sanction of such mortgagees or lienholders. It seems to me that that is the principle that applies in these circumstances.

[16] In the result, I would allow the appeal and set aside the priorities as fixed by Tyrwhitt-Drake L.J.S.C. and conclude that the receiver is not entitled to priority ahead of the second mortgage held by the Federal Business Development Bank. For those reasons I would allow the appeal.

[17] SEATON J.A.:– I agree.

[18] MACFARLANE J.A.:– I agree.

[19] SEATON J.A.: The appeal is allowed. Costs should go against the receiver and the Canadian Imperial Bank of Commerce.

Appeal allowed.

TAB 7

CITATION: Peoples Trust Company v. Rose of Sharon (Ontario) Retirement Community, 2012 ONSC 7319
COURT FILE NO.: CV-11-9399-00CL
DATE: 20121227

SUPERIOR COURT OF JUSTICE – ONTARIO

COMMERCIAL LIST

RE: Peoples Trust Company, Applicant

AND:

Rose of Sharon (Ontario) Retirement Community, Respondent

BEFORE: D. M. Brown J.

COUNSEL: C. Prophet and C. Stanek, for the Receiver, Deloitte & Touche Inc.

R. Jaipargas, for Trisura Guarantee Insurance Company

HEARD: December 21, 2012

REASONS FOR DECISION (corrected)

I. Motion to lift stay in a receivership in order to set down for trial a construction lien action

[1] On September 27, 2011, C. Campbell J. appointed Deloitte & Touche Inc. receiver and manager of all the assets, undertakings and properties of Rose of Sharon (Ontario) Retirement Community. Paragraph 8 of the Appointment Order contained the standard clause staying proceedings against the debtor.

[2] Rose of Sharon owned a long-term care condominium located on Maplewood Avenue, Toronto. Prior to the appointment of the Receiver construction lien litigation had broken out over the condominium project and the general contractor, Mikal-Calladan Construction Inc., had initiated lien proceedings. On January 30, 2012, Trisura Guarantee Insurance Company obtained an assignment of Mikal-Calladan's lien. On November 26, 2012, Trisura obtained an order to continue the construction lien action. As required by the terms of section 37 of the *Construction Lien Act*, R.S.O. 1990, c. C.30, Trisura must set the construction lien action down for trial by December 31, 2012, failing which its lien will expire.

[3] Trisura therefore moved for an order lifting the stay of proceedings to allow it to pursue the construction lien action so that it can set the action down for trial.

[4] The Receiver did not oppose the lifting of the stay, but it sought certain terms for the order. Trisura has agreed to all the terms, but one – whether as a condition of lifting the stay this Court should set aside a default judgment granted against Rose of Sharon some two days after the Appointment Order was made and the earlier noting in default of Rose of Sharon.

II. Governing legal principles governing the lifting of stays

[5] On a motion to lift a stay of proceedings in a receivership the moving party bears the onus of convincing the court that the relief should be granted, and in considering such a request the court should look at the totality of the circumstances and the relative prejudice to both sides.[1] The parties agreed that the court may find guidance in the jurisprudence which has developed around requests to lift stays imposed by the *Bankruptcy and Insolvency Act*. Section 69.4(1) of the *BIA* provides that a court may declare that the statutory stays no longer operate, "subject to any qualifications that the court considers proper", where the court is satisfied that the creditor is likely to be materially prejudiced by the continued operation of the stays or that it is equitable on other grounds to make such a declaration. In *Re Ma*[2] the Court of Appeal set out the basic considerations on a request to lift a stay under *BIA* s. 69.4:

> Under s. 69.4 the court may make a declaration lifting the automatic stay if it is satisfied (a) that the creditor is "likely to be materially prejudiced by [its] continued operation" or (b) "that it is equitable on other grounds to make such a declaration." The approach to be taken on s. 69.4 application was considered by Adams J. in *Re Francisco* (1995), 32 C.B.R. (3d) 29 at 29-30 (Ont. Gen. Div.), a decision affirmed by this court (1996), 40 C.B.R. (3d) 77 (Ont. C.A.):
>
> > In considering an application for leave, the function of a bankruptcy court is not to inquire into the merits of the action sought to be commenced or continued. Instead, the role is one of ensuring that sound reasons, consistent with the scheme of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, exist for relieving against the otherwise automatic stay of proceedings.
>
> As this passage makes clear, lifting the automatic stay is far from a routine matter. There is an onus on the applicant to establish a basis for the order within the meaning of s. 69.4. As stated in *Re Francisco*, the role of the court is to ensure that there are "sound reasons, consistent with the scheme of the *Bankruptcy and Insolvency Act*" to relieve against the automatic stay. While the test is not whether there is a prima facie case, that does not, in our view, preclude any consideration of the merits of the proposed action where relevant to the issue of whether there are "sound reasons" for lifting the stay. For example, if it were apparent that the proposed action had little prospect of success, it would be difficult to find that there were sound reasons for lifting the stay.

---

[1] *Ford Credit Canada Ltd. v. Welcome Ford Sales Ltd.*, 2010 ABQB 199, paras. 13 and 14.
[2] (2001), 24 C.B.R. (4th) 68 (Ont. C.A.), paras. 2 and 3.

III. The basic chronology

[6] Mikal-Calladan preserved a Claim for Lien on November 19, 2010 against title to the Project. It perfected its lien by commencing the construction lien action – CV-10-417426 – on December 31, 2010. On July 21, 2011, Peoples Trust served a statement of defence in the Lien Action. Rose of Sharon was noted in default in the Lien Action; exactly when, the materials did not disclose.

[7] On August 31, 2011, with the consent of Peoples Trust, the parties agreed to refer the Lien Action to a construction lien master in Toronto for a trial. MacDonald J. made a standard Reference Order on that day which provided that "the Master determine all questions arising in this action on the reference".

[8] Then, less than a month later, at the suit of Peoples Trust, the Appointment Order was made.

[9] On September 12, 2011, before the Appointment Order was made, Mikal-Calladan had requisitioned default judgment against Rose of Sharon. On September 29, two days after the Appointment Order was made, the Registrar signed default judgment against Rose of Sharon for $4,195,768.64, plus costs of $1,350.00 (the "Default Judgment").

[10] As mentioned, earlier this year Trisura took an assignment of Mikal-Calladan's Lien Claim and obtained an order to continue the Lien Action about a month ago.

[11] With the December 31 deadline looming to set down the Lien Action or face the expiry of its lien, on November 7, 2012 Trisura's counsel wrote to the Receiver's requesting that the Receiver consent to a lifting of the stay so it could set the Lien Action down for trial. Trisura's counsel indicated that "the main issue in the lien action relates to the priority of the lien over the People's Trust mortgage".

[12] Receiver's counsel responded on November 22, 2012 advising that the Receiver was prepared to consent to lifting the stay on the following terms:

> Condition 1: Trisura obtained an order to continue in the Lien Action;
>
> Condition 2: Trisura agreed to set aside the noting in default of Rose of Sharon and the Default Judgment so that the Receiver could defend the Lien Action;
>
> Condition 3: Issues of liability, timeliness and quantum in the Lien Action would be determined in a Reference before a Master; and,
>
> Condition 4: The issue of the priorities of the construction lien vis-à-vis any other encumbrance would be determined by a judge of the Commercial List.

[13] Mr. Edouard Chassé, a claims adjuster retained by Trisura, in his affidavit stated that Trisura had obtained an order to continue and it agreed to Conditions 3 and 4. Trisura opposed Condition 2 "as the Receiver has had notice of the default for 14 months and has taken no steps" to set aside the noting in default and default judgment.

IV. Analysis

[14] There is no doubt that if the stay is not lifted, Trisura would be prejudiced materially by losing its ability to advance its lien claim. Section 37(1) of the *Construction Lien Act* provides that a perfected lien, such as that assigned to Trisura, expires immediately after the second anniversary of the commencement of the lien action unless either (i) an order is made for the trial of an action in which the lien may be enforced or (ii) an action in which the lien may be enforced is set down for trial. December 31, 2012 is the second anniversary of the commencement of the Lien Action, so unless the stay is lifted, Trisura's lien claim will expire. As mentioned, the Receiver has consented to the lifting of the stay, so the remaining dispute centres only around Condition 2 – the Receiver's requirement that the noting of default and Default Judgment against Rose be set aside.

[15] Trisura advanced two arguments why no setting aside should occur. First, Trisura argued that because the August 31, 2011 Reference Order of MacDonald J. stipulated that "the Master determine all questions arising in this action on the reference and all questions arising under the *Construction Lien Act*", it was not open to the court supervising the receivership proceedings to set aside a noting of default which had occurred in the Lien Action.

[16] I disagree, for two reasons. First, the Default Judgment was made two days after the Appointment Order. No doubt that occurred because the papers requisitioning the Default Judgment were moving through the court's administrative office and the Registrar was unaware of the Appointment Order. Nonetheless, given the stay of proceedings ordered in the Appointment Order, the Default Judgment contravened the Appointment Order and therefore was of no force or effect.

[17] Second, Trisura's submission ignored what occurred less than one month after MacDonald J. made his Reference Order – this receivership came about. As a result of the Appointment Order, the court supervising the receivership considers all issues relating to or touching upon the receivership and therefore is the proper court to determine whether, as a condition of lifting a stay of proceedings, certain relief should be granted to the receiver as part of the process of balancing the respective interests at stake on the lift-stay motion.

[18] Which brings me to the second argument made by Trisura: it contended that the appropriate test for considering whether to set aside a noting in default in a construction lien action is that set out in the *Construction Lien Act* and the related jurisprudence and, in the circumstances of this case, the Receiver could not meet that test. Section 54(3) of the *CLA* provides that where a defendant has been noted in default, it shall not be permitted to contest the claim "except with leave of the court, to be given only where the court is satisfied that there is evidence to support a defence". Section 67(3) of the *CLA* states that "except where inconsistent

with this Act…the *Courts of Justice Act* and the rules of court apply to pleadings and proceedings under this Act."

[19] In *M.J. Dixon Construction Ltd. v. Hakim Optical Laboratory Ltd.*, Master Polika held that Rule 19.03(1) of the *Rules of Civil Procedure* dealing with the setting aside of notings in default was inconsistent with *CLA* s. 54(3) because it was less stringent than the test under the *CLA* by reason of granting the court a discretion to set aside a noting of default on such terms as were just. Master Polika stated that the sole test a party moving to set aside the noting of default in a construction lien action needed to meet was that set out in *CLA* s. 54(3) – i.e. to satisfy the court that there existed evidence to support a defence.[3] In *A1 Equipment Rental Ltd. v. Borkowski* Lederer J. stated that a party moving to set aside a noting in default under the *CLA* must not only demonstrate that evidence existed to support a defence, it also had to move promptly to set aside the noting in default.[4]

[20] Whether, when a lien claimant seeks leave of the court supervising a receivership to lift the stay of proceedings and the receiver seeks a condition that a noting of default be set aside, the court must apply the test under *CLA* s. 54(3) or may proceed on a less stringent basis as part of its discretion in lifting the stay, is a question I need not determine for the simple reason that on the facts of this case the Receiver meets the test under the *CLA*.

[21] Trisura submitted that the Receiver cannot now attempt to impose a condition setting aside the noting of default when over a year has passed since that event. The evidence does not support that contention. First, just over a week after the making of the Appointment Order, counsel for Mikal-Calladan wrote to Receiver's counsel advising of the Default Judgment and stating:

> Under the circumstances, we will not take any steps to enforce our client's judgment in the absence of obtaining the necessary leave from the Court.

In light of that position taken by the lien claimant, it is not surprising that the Receiver took no immediate steps to set aside the Default Judgment or the noting in default.

[22] In its First Report dated December 12, 2011 the Receiver reported:

> While there may be setoffs against Mikail's claim that may be asserted by the Receiver, pending disposition of the Property, the Receiver does not intend to take any action in connection with any of the above-noted lien claims at this time.

Again, this constitutes evidence of a reasonable explanation by the Receiver about why it did not take steps at the time in the Lien Action.

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[3] (2009), 79 C.L.R. (3d) 144 (S.C.J.), para. 24.
[4] (2008), 70 C.L.R. (3d) 274 (S.C.J.), para. 51.

[23] On February 29, 2012, Trisura advised the Receiver of the assignment of the Lien Claim, but then took no further steps to move the Lien Action along until October 24, 2012 when it informed the Receiver that it wished to obtain a trial date. Further emails between counsel ultimately resulted in the Receiver's November 22, 2012 letter setting out the terms for lifting the stay of proceedings. In those circumstances, I see no argument that the Receiver failed to take steps promptly to set aside the noting in default once it became aware of Trisura's intention to proceed with the Lien Action. I also would note, by way of chronology, that on September 14, 2012, a month before Trisura approached the Receiver about further steps in the Lien Action, the Receiver had commenced a claim against Trisura under the performance bond for the Project.

[24] As to whether the Receiver has filed evidence to support a defence, it has. Although the Receiver has not filed a draft Statement of Defence, the Receiver provided Trisura with ample details of its defence through its July 10, 2012 letter to Trisura's counsel, in particular the sections entitled "Set-Offs" and "Deficiencies", as well as in portions of its Statement of Claim in the performance bond action, specifically paragraphs 42 and 62 of the claim.

[25] In balancing the interests of Trisura and the Receiver on this motion to lift the stay of proceedings, I conclude that it is fair and appropriate to require, as a term of lifting the stay, that both the noting of default of Rose of Sharon and the Default Judgment be set aside, and that the Receiver be permitted to file a Statement of Defence in the Lien Action within 20 days.

V. Summary and costs

[26] By way of summary, I grant the motion of Trisura to lift the stay of proceedings contained in the Appointment Order to allow it to pursue the Lien Action, including allowing Trisura to set the Lien Action down for trial. Out of an abundance of caution, given the proximity of the December 31 deadline, I also order the trial of the Lien Action. As conditions for lifting the stay I order as follows:

(i) the noting in default of Rose of Sharon and the Default Judgment against it are set aside so that the Receiver can defend the Lien Action;

(ii) the Receiver may file a Statement of Defence in the Lien Action within 20 days;

(iii) the issues of liability, timeliness and quantum in the Lien Action shall be determined in a Reference before a Master; and,

(iv) the issue of the priorities of the construction lien vis-à-vis any other encumbrance shall be determined by a judge of the Commercial List in these receivership proceedings.

As to costs, the conditions sought by the Receiver in its November 22, 2012 letter were reasonable. There really was no need for a contested motion. Accordingly, I grant the Receiver its costs of this motion fixed at $4,000.00 payable by Trisura within 20 days of the date of this Order. I am available at a 9:30 appointment tomorrow, Friday, December 28, 2012, to issue this order, if required.

D. M. Brown J.

Date: December 27, 2012

TAB 8

Ontario Supreme Court
Francisco, Re
Date: 1995-03-31

Re bankruptcy of Casimiro Almeida Francisco

Ontario Court of Justice (General Division) [In Bankruptcy] Adams J.

Judgment-March 31, 1995.

Pauline Bosman, for appellant BPCO, a division of EMCO Limited.

Craig Colraine, for respondent bankrupt Casimiro Almeida Francisco.

(Doc. No. 31-292784)

[1] March 31, 1995. ADAMS J.: – This is an appeal from an order of Registrar Ferron dismissing an application for leave to continue with an action against a bankrupt. In considering an application for leave, the function of a bankruptcy court is not to inquire into the merits of the action sought to be commenced or continued. Instead, the role is one of ensuring that sound reasons, consistent with the scheme of the *Bankruptcy and Insolvency Act,* R.S.C. 1985, c. B-3, exist for relieving against the otherwise automatic stay of proceedings. See *Re Cravit* (1984), 54 C.B.R. (N.S.) 214 (Ont. S.C.); and *Re Advocate Mines Ltd.* (1984), 52 C.B.R. (N.S.) 277 (Ont. S.C.). On appeal, the reviewing court cannot substitute its opinion for that of the court of first instance given the discretionary nature of the decision appealed from. But such discretion must be exercised in accordance with legal principle.

[2] The appellant BPCO sold and delivered roofing materials to Caldense Roofing and Insulation Limited (“Caldense”) between August 23, 1988 and October 31, 1989 for installation at construction projects on which Caldense was working. The amount due to BPCO was $120,159.06. Casimiro Francisco, Carlos Santos and Antonio Santos were shareholders, officers and directors of Caldense at various times. On February 16, 1990, BPCO commenced an action against Caldense and Francisco for these unpaid invoices and for breach of trust pursuant to the *Construction Lien Act,* R.S.O. 1990, c. C.30, as amended. Ultimately, Carlos Santos was added as a defendant, and Carlos Santos and Antonio Santos were added as Third Parties. Section 8 and ss. 13(1) and 13(2) of that statute provide:

8.–(1) All amounts,

(*a*) owing to a contractor or subcontractor, whether or not due or payable; or

(*b*) received by a contractor or subcontractor,

on account of the contract or subcontract price of an improvement constitute a trust fund for the benefit of the subcontractors and other persons who have supplied services or materials to the improvement who are owed amounts by the contractor or subcontractor.

(2) The contractor or subcontractor is the trustee of the trust fund created by subsection (1) and the contractor or subcontractor shall not appropriate or convert any part of the fraud to the contractor's or subcontractor's own use or to any use inconsistent with the trust until all subcontractors and other persons who supply services or materials to the improvement are paid all amounts related to the improvement owed to them by the contractor or subcontractor.

[R.S.O. 1990, c. C.30, s. 8]

…

13.–(1) In addition to the persons who are otherwise liable in an action for breach of trust under this Part,

(*a*) every director or officer of a corporation; and

(*b*) any person, including an employee or agent of the corporation, who has effective control of a corporation or its relevant activities,

who assents to, or acquiesces in, conduct that he or she knows or reasonably ought to know amounts to breach of trust by the corporation is liable for the breach of trust.

(2) The question of whether a person has effective control of a corporation or its relevant activities is one of fact and in determining this the court may disregard the form of any transaction and the separate corporate existence of any participant.

[3] It would appear the funds received by Caldense from construction projects were all deposited into one bank account without differentiating the various jobs and payments were made out of these funds on a running account basis.

[4] In his Third Party claim, Francisco alleges he was out of the country from July 1, 1989 to August 17, 1989 and further alleges that, in his absence and without his consent, the Third Parties caused Caldense to pay $100,000 to Antonio Santos from its general account comprised of monies paid to Caldense on account of the projects subject to BPCO's claim. The Third Parties deny that payment was made without Francisco's knowledge and assure that the monies paid were not from the projects subject to BPCO's action.

[5] Caldense consented to summary judgment against it by order of Hoilett J. dated May 9, 1990 in the amount of $117,000. Paragraph 2 of that order provides:

> 2. This Court ORDERS that this judgment against the Defendant, Caldense Roofing and Insulation Limited is without prejudice to the Plaintiff continuing its claim against the Defendant, Casimiro Francisco.

Paragraphs 4, 9 and 10 of BPCO's claim alleges:

> 4. The Defendant, Casimiro Francisco resides in the Province of Ontario and was at all material times an officer, director and person having effective control of Caldense.
>
> 9. The Plaintiff further alleges that Caldense, in breach of the Construction Lien Act, 1983 appropriated or converted to its own use or a use not authorized by the trust the funds received on the projects referred to in paragraph 8 hereof and thereby caused the Plaintiff damages thereby to the extent of its claim herein.
>
> 10. The Plaintiff further alleges that the Defendant, Casimiro Francisco was and is an officer, director and person with the effective control of the affairs of the Corporation and assented to and/or ac-
>
> quiesced in conduct which he knew or ought to reasonably have known amounts to a breach of trust by the Corporation and is personally liable to the Plaintiff herein for such breach pursuant to Section 13 of the said Act.

[6] BPCO was unable to collect its judgment against Caldense, and the trial of the action against Francisco commenced on September 26, 1994 before Davidson J. After three days of hearing, however, the trial was adjourned to a date to be fixed in order to permit BPCO further discovery of Francisco on documents produced by him at trial and not previously produced. Costs were also awarded against Francisco.

[7] On October 28, 1994, Francisco made an assignment in bankruptcy, and on November 14, 1994 BPCO filed a proof of claim in the bankruptcy proceeding. BPCO, however, also took the position that Francisco's liability to BPCO survives his bankruptcy because it is a "liability arising out of fraud, embezzlement, misappropriation or defalcation while acting in a fiduciary capacity" within the meaning of s. 178(1)(*d*) of the *Bankruptcy and Insolvency Act.* The argument is that the failure to pay BPCO out of project funds received by Caldense made Francisco liable for misappropriation or defalcation while he was acting in a fiduciary capacity given that the funds were impressed with a statutory trust, the breach of which Francisco was made liable by s. 13(1) of the *Construction Lien Act.*

[8] Section 178(1)(*d*) of the *Bankruptcy and Insolvency Act* provides:

> 178. (1) An order of discharge does not release the bankrupt from
>
> …
>
> (*d*) any debt or liability arising out of fraud, embezzlement, misappropriation or defalcation while acting in a fiduciary capacity.

[9] Master Ferron refused leave to continue the action. His endorsement took the following summary form:

> January 5, 1995
>
> – None of the items described in subparas, (*d*) or (*e*) of s. 178 have been pleaded against the Bankrupt.
>
> – Further, the reasons for lifting the stay which I listed in *Re Advocate Mines* are not present.
>
> – The action against the company of which the Bankrupt was an officer has been concluded and Judgment rendered.
>
> In that action and in the Judgment there was no finding of fraud, misrepresentation, etc., against the company.
>
> The Bankrupt liability, if any, must be established through the company, that is, his liability is vicarious.
>
> It must follow that if the company has been adjudicated not to be liable on any grounds except breaching a simple contract, no liability under the *Construction Lien Act* can be attributed to the Bankrupt. It is not sufficient to suggest that the breaching the trust provisions [sic] of the Act can be established against the company in an action against the principal.
>
> This is not an appropriate case for lifting the s. 69 stay.

[10] With the greatest of respect, I have come to the conclusion that Registrar Ferron erred in principle in rejecting the application. Therefore, this appeal must be allowed. Consent to the action continuing is granted.

[11] Without intending to usurp the role of the trial judge to decide otherwise on the facts established before him, I am satisfied BPCO has pleaded sufficient allegations to bring its claim, at least arguably, within s. 178(1)(*d*). Francisco is alleged to have been a director or officer of a corporation who assented to or acquiesced in conduct he knew or should have known amounted to breach of trust by the corporation. Section 13(1) of the *Construction Lien Act* makes such a person “liable to the breach of trust.” Thus, it is reasonably arguable that a director acts in a fiduciary capacity with respect to the beneficiaries of this trust relationship. For very similar fact situations see, for example, *J.B. Allen & Co. v. D.E. Witmer Plumbing & Heating Ltd.* (1992), 12 C.B.R. (3d) 272 (Ont. Bktcy.), and *Smith v. Henderson* (1992), 10 C.B.R. (3d) 153 (B.C. C.A.).

[12] It should be understood that *Re Advocate Mines Ltd.,* supra, is not an exhaustive codification of the policy underlying the *Bankruptcy and Insolvency Act.* It is but one thoughtful decision attempting to articulate the type of grounds which may provoke the exercise of a

judicial discretion. To view *Advocate Mines* as a limiting or exhaustive instrument is an error in principle. Moreover, I am satisfied the action in question is one in respect of which a discharge may not be a defence and, further, that the action had progressed to a point where logic dictated the action be permitted to continue to judgment.

[13] While the action against Caldense had culminated in a consent summary judgment, the fact that there had been “no finding of fraud, misrepresentation etc. against the company” was not material to issue before the learned registrar. The words “misappropriate” and “defalcation” are not used in a pejorative or accusatory sense and are applicable simply where there has been a failure to properly account for funds. See *Abstainer’s Insurance Co. v. Pellegrino* (1989), 77 C.B.R. (N.S.) 108 (Ont. Dist. Ct.), and *Turner v. Midland Doherty Ltd.* (1992), 13 C.B.R. (3d) 16 (B.C. S.C.).

[14] Further, it was not for the registrar to determine that the liability of a director under s. 13(1) of the *Construction Lien Act* is merely “vicarious.” I personally have difficulty with this conclusion given the wording of that subsection. But this is for the trial judge to determine. The consent judgment against Caldense was made expressly subject to the right of the plaintiff to proceed against Francisco. I do not appreciate the existence of any a priori legal principle precluding BPCO from establishing facts which demonstrate Caldense’s conduct as a background to establishing Francisco’s independent liability for breach of trust. In any event, this too is a matter for the trial judge.

[15] Accordingly, the appeal is allowed and the s. 69 stay is lifted. BPCO may continue its action against the bankrupt and in respect of which the applicability of s. 178(1)(*d*) can be definitively determined. See *Turner v. Midland Doherty Ltd.,* supra.

[16] I may be spoken to concerning costs on appointment.

Appeal allowed.

[BLANK]

Court of Appeal for Ontario
Francisco (Re)
Date: 1996-06-06

Craig R. Colraine, for appellant.

Chris Reed, for respondent.

(Doc. CA C21510)

June 6, 1996. The judgment of the court was delivered by

[1] McMURTRY C.J.O.: – We agree with the conclusion of Adams J. and his reasons for reaching that conclusion. The appeal is therefore dismissed. The costs of the appeal (including the motion to qualify the appeal) are reserved for disposition by the Judge presiding at the trial of the action.

Appeal dismissed.

TAB 9

DATE: 20010404
DOCKET: C34958

COURT OF APPEAL FOR ONTARIO

IN THE MATTER OF THE BANKRUPTCY OF JAMES HOI-PANG MA, OF THE CITY OF MISSISSAUGA, IN THE REGIONAL MUNCIPALITY OF PEEL, IN THE PROVINCE OF ONTARIO

RE: JAMES HOI-PANG MA (Bankrupt (Appellant)) and TORONTO DOMINION BANK (Applicant (Respondent))

BEFORE: ABELLA, CHARRON and SHARPE JJ.A.

COUNSEL: Chi-Kun Shi
For the appellant

Bruce S. Batist
For the respondent

William J. Meyer, Q.C.
For the Trustee in Bankruptcy

HEARD: March 23, 2001

E N D O R S E M E N T

Released orally March 23, 2001

[1] The appellant argues that when considering an application to lift a stay under s. 69.4 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c.B-3, the applicant is required to establish a *prima facie* case for the proposed action. *Bowles v. Barber* (1985), 60 C.B.R. 311 (Man. C.A.) is cited in support of this proposition. It is argued that to the extent Ontario cases such as *Arrojo Investments v. Cardamone* (1995), 33 C.B.R. (3d) 46 (Ont. Gen. Div.) apply a more lenient standard, they are inconsistent with decisions from other provinces.

[2] In our view there is no requirement to establish a *prima facie* case and no inconsistency in the case law. We do not agree that *Bowles v. Barber* imposes a *prima facie* case requirement. More importantly, that requirement is not imposed by the statute. Under s. 69.4 the court may make a declaration lifting the automatic stay if it is satisfied (a) that the creditor is "likely to be materially prejudiced by [its] continued operation" or (b) "that it is equitable on other grounds to make such a declaration." The approach to be taken on s. 69.4 application was considered by Adams J. in *Re Francisco* (1995), 32 C.B.R. (3d) 29 at 29-30 (Ont. Gen. Div.), a decision affirmed by this court (1996), 40 C.B.R. (3d) 77 (Ont. C.A.):

> In considering an application for leave, the function of a bankruptcy court is not to inquire into the merits of the action sought to be commenced or continued. Instead, the role is one of ensuring that sound reasons, consistent with the scheme of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c.B-3, exist for relieving against the otherwise automatic stay of proceedings.

[3] As this passage makes clear, lifting the automatic stay is far from a routine matter. There is an onus on the applicant to establish a basis for the order within the meaning of s. 69.4. As stated in *Re Francisco*, the role of the court is to ensure that there are "sound reasons, consistent with the scheme of the *Bankruptcy and Insolvency Act*" to relieve against the automatic stay. While the test is not whether there is a *prima facie* case, that does not, in our view, preclude any consideration of the merits of the proposed action where relevant to the issue of whether there are "sound reasons" for lifting the stay. For example, if it were apparent that the proposed action had little prospect of success, it would be difficult to find that there were sound reasons for lifting the stay.

[4] In the case before us, Justice Lane found that the Deputy Registrar was correct in finding that the applicant would suffer sufficient prejudice to justify an order lifting the stay. This finding accords with s. 69.4 and is supported by the record. We see no basis for interfering with his conclusion. The appeal is therefore dismissed with costs.

"R. S. Abella J.A."
"Louise Charron J.A."
"Robert J. Sharpe J.A."

DBDC SPADINA LTD. et al. and NORMA WALTON, et al. And THOSE CORPORATIONS LISTED ON SCHEDULE B HERETO

Court File No: CV-13-10280-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE - COMMERCIAL LIST

Proceeding commenced at Toronto

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