

**ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)**

CHINA MACHINERY ENGINEERING CORPORATION

Applicant

-and-

**2284649 ONTARIO INC., 2270613 LIMITED PARTNERSHIP
and 2270613 ONTARIO INC.**

Respondents

Application Under Section 101 of the *Courts of Justice Act*, R.S.O. 1990,
c.C.43, as amended, and Section 243 of the *Bankruptcy and Insolvency Act*,
R.S.C. 1985, c.B-3, as amended

**FACTUM OF THE MOVING PARTIES
(Motion returnable July 26, 2018)**

July 24, 2018

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2270613 Ontario Inc.

PART I - OVERVIEW AND RELIEF SOUGHT

1. The Respondents, 2284649 Ontario Inc., 2270613 Limited Partnership and 2270613 Ontario Inc. (collectively, the “**Respondents**”), have brought a Motion for an Order lifting the stay of proceedings granted under the Order of the Honourable Mr. Justice McEwen of the Ontario Superior Court of Justice dated February 6, 2018 (the “**Receivership Order**”) to permit 2284649 Ontario Inc. (formerly known as “JD Development Phillip Street Limited”) (the “**Debtor**”) to redeem the Mortgage (as defined below).

PART II - THE FACTS

2. Pursuant to the Receivership Order, KSV Kofman Inc. was appointed as receiver and manager (in such capacity, the “**Receiver**”) of the property, assets and undertakings of the Respondents upon the Application of China Machinery Engineering Corporation (“**CMEC**”).

Reference: Affidavit of Yueqing Zhang sworn July 19, 2018 (the “Initial Zhang Affidavit”) at para 8.

3. The Debtor is part of the JD Development Group, a large organization in the business of design, construction, project financing and property management, with its head office in Markham, Ontario. JD Development Group has successfully developed and operates a number of large real estate development projects in Ontario.

Reference: Initial Zhang Affidavit at para 3.

4. JD Development Group specializes in the development and operation of student residence buildings. Prior to the commencement of this receivership proceeding, the Debtor and its

affiliates were undertaking a project (the “**Phillip Street Project**”) that contemplated development of a four (4) acre parcel of real property municipally known as 256 Phillip Street, Waterloo, Ontario into four (4) student residence buildings.

Reference: Initial Zhang Affidavit at para 4.

5. The Debtor is the registered owner of real property (the “**Real Property**”) that includes three of the four parcels that comprise the Phillip Street Project. The remaining parcel, located at the property known municipally as 254 Phillip Street, Waterloo and known as “Fergus House”, is owned by an affiliate of the Debtor, JD Development 254 Phillip Street Ltd. (“**JD 254**”).

Reference: Initial Zhang Affidavit at para 5.

6. CMEC is a construction and engineering company with its head office in Beijing, China. CMEC is a secured creditor of the Debtor. CMEC holds, among other things, a Mortgage and Charge registered against the Real Property in the maximum principal amount of U.S. \$61,380,000, as amended (the “**Mortgage**”).

Reference: Initial Zhang Affidavit at para 7.

7. Pursuant to the Order of Justice McEwen dated July 5, 2018 (the “**Sale Process Order**”), the Receiver was authorized to engage in a marketing and sales process (the “**Sale Process**”). The marketing component of the Sale Process contemplated in the Sale Process Order is scheduled to commence on July 30, 2018.

Reference: Initial Zhang Affidavit at para 9.

8. At the hearing before Justice McEwen on July 5, 2018, the Receiver and CMEC sought an Order prohibiting the Debtor from bringing a Motion to lift the stay of proceedings in order to redeem the Mortgage. Justice McEwen refused to grant the Order sought by CMEC, and scheduled the Motion to lift the stay for a hearing on July 26, 2018.

Reference: Initial Zhang Affidavit at para 10.

9. In the event that the Court grants the Motion to lift the stay to allow the Debtor to redeem the Mortgage, the amount required to do so is approximately \$95.4 million as of August 31, 2018.

Reference: Initial Zhang Affidavit at para 14.

10. The Debtor has arranged for financing in the aggregate amount of \$101.23 million to fund the proposed redemption and pay certain other amounts. The financing will be provided by Institutional Mortgage Capital Canada Inc. (“**IMC**”) pursuant to four (4) Commitment Letters (the “**Commitment Letters**”).

Reference: Affidavit of Yueqing Zhang sworn July 24, 2018 (the “Supplemental Zhang Affidavit”) at para 3.

11. The proposed lender, IMC, is a large commercial mortgage lender, loan servicer, and investment fund manager. IMC is a leader in the Canadian commercial mortgage market, including first mortgages, mezzanine loans, and commercial mortgage-backed securities. IMC and its affiliates are among the largest independent commercial mortgage loan servicers in Canada.

Reference: Initial Zhang Affidavit at paras. 16-17.

12. The funding obligations in the Commitment Letters provided by IMC are not subject to any commercially unusual or otherwise challenging conditions. In fact, a substantial portion of the conditions have already been fulfilled.

Reference: Supplemental Zhang Affidavit at paras 13-15.

13. IMC's internal credit committee has approved the proposed transactions set out in the Commitment Letters. The remaining funding conditions relate primarily to information and document delivery as well as ordinary course due diligence requirements such as, for example, with respect to corporate existence and authority.

Reference: Supplemental Zhang Affidavit at paras 10, 16.

14. The benefit to the Debtor if the stay of proceedings is lifted will substantially outweigh the prejudice, if any, that would be sustained by CMEC, the Receiver or the other stakeholders.

Reference: Initial Zhang Affidavit at para 25.

15. If the stay is lifted and the Debtor completes the redemption, the result will be optimal for all stakeholders:

- (a) CMEC will receive payment in full of all amounts owing to it, earlier than it would through the proposed Sale Process;
- (b) Lien claimants will implement a plan agreed to with the Debtor and MBCI that will see them paid in full for outstanding amounts, and recommence construction activities at the Phillip Street Project as early as September 2018;

- (c) Disruption to the approximately 425 residents of the Blair House residence will be minimized;
- (d) Construction of Hespeler House will recommence early enough that the building can be completed in time for the beginning of the 2019/2020 academic year, commencing in September 2019;
- (e) The claims of unsecured creditors will not be “vested out” through a sale process, but rather, will be paid by the Debtor in the ordinary course following the redemption and recommencement of development of the Phillip Street Project; and
- (f) The Phillip Street Project residences will continue to be managed by the Debtor’s affiliate, Rez-One Management Corp., which has more than 20 employees.

Reference: Initial Zhang Affidavit at para 26.

16. The Respondents’ motion is overwhelmingly supported by the Debtor’s key creditors and other stakeholders, including, in particular, construction lien claimants and the significant related party unsecured creditors.

Reference: Initial Zhang Affidavit at paras 33-34.

17. The Debtor will be substantially prejudiced if the Motion to lift the stay of proceedings is dismissed. If the Debtor is denied the right to exercise its redemption right, it will suffer from the following:

- (a) The Debtor will lose its equity in the Phillip Street Project;

(b) The Debtor's affiliates may not recover unsecured advances made to the Debtor in the amount of approximately \$21,735,112.92; and

(c) Even if successful in obtaining its assets back in a sale process, given the timing of the conclusion of such a transaction it will be too late to complete Hespeler House in time for September 2019, which the Debtor estimates will cost a minimum of \$5 million in gross revenue.

Reference: Initial Zhang Affidavit at paras 28-30.

18. CMEC will not sustain any undue prejudice in the event that the stay is lifted but the Debtor fails to complete the redemption. At worst, the Sale Process will be commenced in accordance with the Sale Process Order with the understanding in the market that the Debtor may redeem, but this will be resolved by August 31, 2018, almost three weeks prior to the proposed deadline for bids under the Sale Process.

Reference: Initial Zhang Affidavit at para 38.

19. The Respondents submit that, based on the highly concentrated market for the Real Property (as described in the Receiver's own evidence) and the fact that the Receiver has been marketing the Real Property since at least as early as March 2018, the suggestion by the Receiver and CMEC that any prospective purchaser would have any difficulty preparing a bid by September 19, 2018 is not credible.

Reference: Initial Zhang Affidavit at para 38.

20. The Debtor proposes that, in the event the Court lifts the stay of proceeding to allow the debtor to redeem the Mortgage, the “costs thrown away” would be \$451,643 limited to the following three (3) components:

- (a) Interest on the outstanding Receiver’s Borrowing Certificate accrued from July 16, 2018 to August 31, 2018 in the amount of CDN\$2,227;
- (b) Interest on the indebtedness claimed by CMEC from July 13, 2018 to August 31, 2018 in the amount of CDN\$324,416; and
- (c) Additional potential fees to be incurred by CMEC to August 31, 2018 in the amount of \$125,000.

Reference: Supplemental Zhang affidavit at para 23.

21. The Debtor’s Statement of Issues (the “**Statement of Issues**”) filed in connection with the hearing on July 5, 2018 makes clear that the Debtor is prepared to deliver a deposit in an amount in excess of potential costs thrown away. Debtor’s counsel advised the Court at that hearing of this position as well, and CMEC did not object to that as a basis for calculating the amount of a deposit.

Reference: Supplemental Zhang Affidavit at para 21.

22. However, in its letter dated July 24, 2018, CMEC took the position that it is entitled to a deposit in an amount in excess of potential costs thrown away, and demanded a minimum deposit of CAD \$5 million as a condition of its support for the proposed redemption.

Reference: Supplemental Zhang Affidavit at para 24.

23. CMEC has not put forth any evidence to substantiate its claim that it is facing potential damages in the amount of CAD \$5 million in the event that the Debtor fails to close the redemption. The only losses that CMEC would reasonably be faced with in the event the Debtor fails to close the redemption are those that would be covered off by the Debtor's estimate of "costs thrown away".

Reference: Supplemental Zhang Affidavit at paras 21, 23, 24.

PART III - ISSUES

24. The issues on this Application are as follows:
- (a) Should the stay of proceedings be lifted to allow the Debtor to redeem the Mortgage?
 - (b) What, if any, conditions should the Court impose on the proposed redemption process?

PART IV - THE LAW

ISSUE 1: Should the stay of proceedings be lifted to allow the Debtor to redeem the Mortgage?

25. It is respectfully submitted that the Court ought to lift the stay of proceedings to allow the Debtor to redeem the Mortgage.

(a) Redemption Rights Under the *Mortgages Act*

26. Pursuant to the *Mortgages Act* (Ontario), the Debtor has a right to redeem the Mortgage, subject only to the stay of proceedings.

Reference: *Mortgages Act*, R.S.O. 1990, c M-40, as amended.

27. Section 22(1) of the *Mortgages Act* provides as follows:

22(1) Despite any agreement to the contrary, where default has occurred in making any payment of principal or interest due under a mortgage or in the observance of any covenant in a mortgage and under the terms of the mortgage, by reason of such default, the whole principal and interest secured thereby has become due and payable,

(a) at any time before sale under the mortgage; or

(b) before the commencement of an action for the enforcement of the rights of the mortgagee or of any person claiming through or under the mortgagee, the mortgagor may perform such covenant or pay the amount due under the mortgage, exclusive of the money not payable by reason merely of lapse of time, and pay any expenses necessarily incurred by the mortgagee, and thereupon the mortgagor is relieved from the consequences of such default.

28. Section 23(1) of the *Mortgages Act* provides as follows:

23(1) Despite any agreement to the contrary, where default has occurred in making any payment of principal or interest due under a mortgage or in the observance of any covenant in a mortgage and under the terms of the mortgage, by reason of such default, the whole principal and interest secured thereby has become due and payable, in an action for enforcement of the rights of the mortgagee or of any person claiming through or under the mortgagee, the mortgagor, upon payment into court of the sum of \$100 to the credit of the action as security for costs, may apply to the court and, conditional upon performance of such covenant or upon payment of the money due under the mortgage, exclusive of the money not payable by reason merely of lapse of time, and upon payment of the costs of the action, the court,

(a) shall dismiss the action if judgment has not been recovered; or

(b) may stay proceedings in the action, if judgment has been recovered and if no sale or recovery of possession of the land or final foreclosure of the equity of redemption has taken place.

29. The redemption rights prescribed in the *Mortgages Act* are not subject to any applicable conditions or restrictions, provided that they are exercised prior to a sale under the mortgage. Even where an action has been commenced for enforcement of the mortgagee's rights, the mortgagor has an unequivocal right to redeem. However, the Respondents concede that in the case at bar, the stay of proceedings under the Receivership Order prevents the Debtor from exercising such rights.
30. The Respondents submit that the cases relied upon by the Receiver and CMEC in their respective Statements of Issues dated June 28, 2018 do not stand for the proposition that the Debtor does not have a right to redeem the Mortgage.
31. CMEC and the Receiver have both cited *Ron Handelman Investments Ltd. v. Mass Properties Inc.* as standing for the proposition that the Debtor does not have a right to redeem the Mortgage. It is respectfully submitted that CMEC and the Receiver have overstated both the relevance and meaning of the *Handelman* decision. In that case, the party seeking to redeem only did so in the face of an executed agreement of purchase and sale with a third party and a motion by the receiver for approval of same after the conclusion of a sale process. Justice Pepall found that in those circumstances, the mortgagor did not have an "automatic" right to redeem as,

A mockery would be made of the practice and procedures relating to receivership sales if redemption were permitted at this stage of the proceedings. A receiver would spend time and money securing an agreement of purchase and sale that was, as is common place, subject to Court approval, and for the benefit of all the stakeholders, only for there to be a redemption by a mortgagee at the last minute. This could act as a

potential chill on securing the best offer and be to the overall detriment of stakeholders.

Reference: *Ron Handelman Investments Ltd. v. Mass Properties Inc.*, 2009 CarswellOnt 4257 at para 22,179 ACWS (3d) 114 (Ont Sup Ct) [*Handelman*], Respondent's Book of Authorities ("BOA") at Tab 1.

32. The Respondents do not dispute the reasoning above in the circumstances of that case. However, the circumstances in the case at bar are not analogous to those in *Handelman*. Put simply, Justice Pepall did not rule that a mortgagor in a receivership loses the right to redeem.
33. In fact, all three of the "anti-redemption" cases relied upon by CMEC and the Receiver – *i.e.*, *Handelman*, as well as *Home Trust Co. v. 2122775 Ontario Inc.* and *Business Development Bank of Canada v. Marlwood Golf & Country Club Inc.* – arose in similar circumstances and were decided on similar bases.

Reference: *Home Trust Co. v 2122775 Ontario Inc.*, 2015 CarswellOnt 1888 (Ont Sup Ct) [*Home Trust*], BOA at Tab 2; *Business Development Bank of Canada v Marlwood Golf & Country Club Inc.*, 2015 CarswellOnt 9453 (Ont Sup Ct) [*Marlwood*], BOA at Tab 3.

34. None of those cases state that a mortgagor loses its right to redeem a mortgage once a receiver had been appointed. Rather, the Court in each of those cases found that by waiting until the receiver had conducted a sale process and entered a purchase agreement with a third party, it was too late in the receivership process for the debtor to be permitted to redeem the mortgage.

Reference: *Handelman*, BOA at Tab 1; *Home Trust*, BOA at Tab 2; *Marlwood*, BOA at Tab 3.

35. In the present case, the Debtor did not “lie in the weeds” as could be said for the debtors in *Handelman, supra*, and the other cases relied upon by CMEC and the Receiver, but instead came forward at its earliest opportunity to alert the parties of its intention to redeem. In fact, pursuant to the Sale Process Order the formal marketing component of the Sale Process will not commence until July 30, 2018. The Receiver has not yet commenced the bidding process, much less accepted an offer. As such, concerns regarding the need to protect the integrity of a court-supervised sale process are unfounded and inapplicable.

(b) Lifting the Stay of Proceedings

36. It is respectfully submitted that the circumstances in this case are such that the Court ought to lift the stay of proceedings.

37. In considering whether to lift a stay of proceedings, the Court should examine “...the totality of the circumstances and the relative prejudice to both sides.”

Reference: *Peoples Trust Co. v Rose of Sharon (Ontario) Retirement Community*, 2012 ONSC 7319 at para 5, 2012 CarswellOnt 16827 [*Peoples Trust*], BOA at Tab 4.

38. The Court may find guidance in the case law that has developed around requests to lift stays imposed by the *Bankruptcy and Insolvency Act (Canada)* (the “**BIA**”). In *Peoples Trust Co. v. Rose of Sharon (Ontario) Retirement Community*, Justice Brown held that under the stay provisions in Section 69.4(1) of the BIA a court may declare that a statutory stay no longer operates, subject to such qualifications as the court considers proper, where

the court is satisfied that the creditor is likely to be materially prejudiced by the continued operation of the stay or that it is otherwise equitable to make such a declaration.

Reference: *Bankruptcy and Insolvency Act*, R.S.C. 1985, c B-3, as amended.

Reference: *Peoples Trust* at para 5.

39. In the case at bar, the Debtor and its affiliates will be substantially prejudiced if the Motion to lift the stay of proceedings is dismissed. The benefit to the Debtor if the stay of proceedings is lifted will substantially outweigh the prejudice, if any, that would be sustained by CMEC, the Receiver or the other stakeholders.

Reference: Initial Zhang Affidavit at para 27.

(c) No Undue Risk to CMEC

40. The Debtor's proposed financing is credible, subject to binding Commitment Letters and there is therefore good reason to believe it will close.

41. The Debtor's confidence that the financing will close is evidenced by its conduct. The Debtor's affiliates have already paid non-refundable deposits to IMC in the aggregate amount of \$790,000 and will be paying an additional \$382,500 on July 25, 2018, which the Commitment Letters prescribe will be forfeited if the Debtor fails to close the financing.

Reference: Supplemental Zhang Affidavit at para 17.

ISSUE 2: What, if any, conditions should the Court impose on the proposed redemption process?

42. It is respectfully submitted that the Court should not impose any conditions on the Debtor's exercise of its redemption rights under the *Mortgages Act*. The right of redemption is a

fundamental proprietary interest and is thus qualitatively different than the opportunity to participate in a court-supervised sale process, and as such the “usual” requirement of a deposit in such a sale process has no application in the case at bar. As such, any conditions that may be imposed should, at most, be limited to “costs thrown away”.

(a) Fundamental Nature of Right of Redemption

43. It is respectfully submitted that the Courts ought to be reluctant to prevent a mortgagor from exercising its redemption right. The right of redemption, while codified in the *Mortgages Act*, flows from the courts of equity, which recognized that a mortgagor’s right to redemption to be jealously guarded by the courts. The Supreme Court of Canada has found there is a:

“...well-established proposition that the equitable right to redeem is more than a mere equity but is, indeed an interest in the mortgaged land which is not lightly to be put aside and which is enforceable by courts of equity.”

Reference: *Petranik v. Dale*, [1977] SCR 959 at 995, 1976 CanLii (34), BOA at Tab 5.

44. Given the well-recognized fundamental importance of the right of redemption, it is respectfully submitted that, in the event this Honourable Court determines the stay should be lifted, the Court should be hesitant to impose any conditions that would obstruct or otherwise interfere with the Debtor’s efforts to exercise that right. Such conditions would include the imposition of a requirement that the Debtor deliver a deposit in advance of exercising its redemption rights.

(b) “Costs Thrown Away”

45. Notwithstanding the above, the Debtor has confirmed that it is prepared to deliver a deposit in an amount sufficient to cover any “costs thrown away” in relation to the nascent Sale Process in the event that the redemption is not completed and the Sale Process has to then be undertaken by the Receiver.

46. In Ontario, the phrase “costs thrown away” has a specific meaning before the courts. “Costs thrown away” has been interpreted to mean costs for those steps reasonably necessary to proceed with an action or other proceeding, but which have been rendered useless by the conduct of the other party.

Reference: *Legacy Leather International Inc. v Ward*, 2007 CarswellOnt 527 (Ont Sup Ct [Commercial List]) at para 9, 2007 CanLII 2357, BOA at Tab 6.

47. In the case at bar, in the event the Court lifts the stay of proceedings to allow the Debtor to redeem in accordance with the Debtor’s proposal for same, it is respectfully submitted that the potential “costs thrown away” include only the following three components, accrued by or incurred to August 31, 2018:

- (a) Interest on outstanding Receiver’s Borrowing Certificates;
- (b) Interest on the indebtedness claimed by CMEC; and
- (c) Additional fees to be incurred by CMEC.

Reference: Supplemental Zhang Affidavit at para 23.

48. The Debtor's proposed redemption process contemplates a completion date of August 31, 2018. The Debtor estimates that the aggregate amount of exposure to "costs thrown away" faced by CMEC in the event that the Debtor fails to close in accordance with the proposed redemption is \$451,643. The Debtor has confirmed that it is prepared to pay this amount to the Receiver as a deposit against potential "costs thrown away" should this Honourable Court make this a condition to the proposed redemption.

Reference: Supplemental Zhang Affidavit at paras 21-23.

49. CMEC has taken the position that it is entitled to a deposit in an amount no less than CAD \$5 million, with vague references to "...unnecessary and largely unmitigated risks." However, CMEC has not substantiated or even articulated any such risks beyond those that would be covered off by the amount deposited in respect of potential costs thrown away.

Reference: Supplemental Zhang Affidavit at para 23 and Exhibit "A" and "C".

50. The Respondents submit that the amount of deposit funds demanded by CMEC is significantly out of proportion to the quantum of damages that it would likely suffer in the unlikely event the Debtor is unable to complete the redemption process.

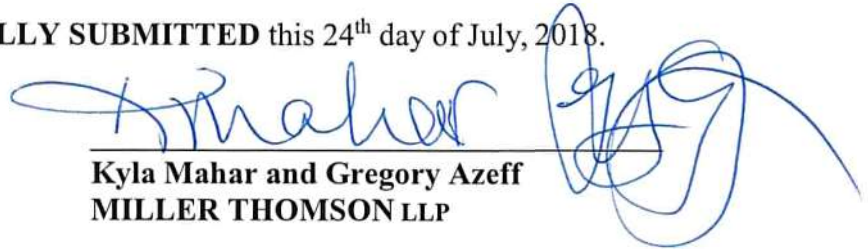
Reference: Statement of Issues at para. 9.

Reference: Supplemental Zhang Affidavit at para 24.

RELIEF REQUESTED

51. In light of the foregoing, the Respondents respectfully request that this Honourable Court issue an Order lifting the stay of proceedings to allow the Debtor to redeem the Mortgage and, upon same being completed, to discharge the Receivership Proceeding.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 24th day of July, 2018.



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Lawyers for the Moving Parties, 2284649 Ontario Inc., 2270613 Limited Partnership and 2270613 Ontario Inc.

**SCHEDULE “A”
LIST OF AUTHORITIES**

JURISPRUDENCE

1. *Ron Handelman Investments Ltd. v Mass Properties Inc.*, 2009 CarswellOnt 4257 (Ont Sup Ct).
2. *Home Trust Co. v 2122775 Ontario Inc.*, 2015 Carswell Ont 1888 (Ont Sup Ct).
3. *Business Development Bank of Canada v Marlwood Golf & Country Club Inc.*, 2015 CarswellOnt 9453 (Ont Sup Ct).
4. *Peoples Trust Co. v Rose of Sharon (Ontario) Retirement Community*, 2012 ONSC 7319, 2012 CarswellOnt 16827.
5. *Petranik v Dale*, [1977] SCR 959, 1976 CanLii (34).
6. *Legacy Leather International Inc. v Ward*, 2007 CarswellOnt 527 (Ont Sup Ct [Commercial List]), 2007 CanLII 2357.

**SCHEDULE “B”
RELEVANT STATUTES**

Mortgages Act

Relief before action

22 (1) Despite any agreement to the contrary, where default has occurred in making any payment of principal or interest due under a mortgage or in the observance of any covenant in a mortgage and under the terms of the mortgage, by reason of such default, the whole principal and interest secured thereby has become due and payable,

(a) at any time before sale under the mortgage; or

(b) before the commencement of an action for the enforcement of the rights of the mortgagee or of any person claiming through or under the mortgagee,

the mortgagor may perform such covenant or pay the amount due under the mortgage, exclusive of the money not payable by reason merely of lapse of time, and pay any expenses necessarily incurred by the mortgagee, and thereupon the mortgagor is relieved from the consequences of such default.

Relief after action commenced

23 (1) Despite any agreement to the contrary, where default has occurred in making any payment of principal or interest due under a mortgage or in the observance of any covenant in a mortgage and under the terms of the mortgage, by reason of such default, the whole principal and interest secured thereby has become due and payable, in an action for enforcement of the rights of the mortgagee or of any person claiming through or under the mortgagee, the mortgagor, upon payment into court of the sum of \$100 to the credit of the action as security for costs, may apply to the court and, conditional upon performance of such covenant or upon payment of the money due under the mortgage, exclusive of the money not payable by reason merely of lapse of time, and upon payment of the costs of the action, the court,

(a) shall dismiss the action if judgment has not been recovered; or

(b) may stay proceedings in the action, if judgment has been recovered and if no sale or recovery of possession of the land or final foreclosure of the equity of redemption has taken place.