COURT FILE NO.: 08-CL-7840
DATE: 20091014

ONTARIO

SUPERIOR COURT OF JUSTICE

IN THE MATTER OF an Application under section 47(1) of the *Bankruptcy and Insolvency Act,* R.S.C. 1985, c. B-3, as amended

AND IN THE MATTER OF Section 101 of the *Courts of Justice Act*, R.S.O. 1990, c.43, as amended

B E T W E E N:	
BANK OF MONTREAL, as agent for BANK OF MONTREAL, THE BANK OF NOVA SCOTIA and ALBERTA TREASURY BRANCHES Applicant	**Douglas O. Smith**, for the Applicant **Jonathan F. Lancaster**, for ADP Canada Co.
- and -	
GRAFIKOM LIMITED PARTNERSHIP, GRAFIKOM GENERAL PARTNER INC., GRAFIKOM SPEEDFAST LIMITED and GRAFIKOM GRENVILLE LIMITED Respondents	**John A. MacDonald** for the Interim Receiver
	HEARD: June 8, 2009 and October 1, 2009

Hoy J.

REASONS FOR DECISION

[1] Within hours after RSM Richter Inc. (the "Receiver") was appointed by the court as interim receiver and receiver manager of all of the assets and undertakings of Grafikom. Speedfast Limited ("Speedfast") at the behest of Bank of Montreal ("BMO"), Phillip Healey, a former Speedfast employee retained by the Receiver to perform a specified task, triggered the payment of Speedfast's payroll by ADP Canada Co. ("ADP"), Speedfast's payroll services provider. Pursuant to the payroll services agreement made between ADP and

Speedfast, ADP paid Speedfast's employees, and immediately sent a corresponding debit instruction to Speedfast's bank. Speedfast was unable to pay ADP as required by that agreement.

[2] Mr. Healey had not been retained, authorized or directed, by the Receiver to trigger the payment and the Receiver was unaware that he had done so.

[3] ADP seeks an order requiring the Receiver to pay it the amount that it is out-of-pocket as a result of ADP's breach of the agreement, allegedly $118,593.20. Such a payment would reduce the distribution to BMO, Speedfast's first secured creditor, by a corresponding amount. BMO opposes ADP's motion. It is not disputed that if ADP had not paid Speedfast's employees, the Receiver would have been required to pay each of the employees up to $2,000 out of Speedfast's current assets before paying any other creditors, secured or unsecured, pursuant to s. 81.4 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, as amended (the "BIA"). The amounts available for distribution to BMO would have been reduced accordingly.

[4] At my request, the Receiver provided a report regarding its dealings with Speedfast's employees and containing additional background information. The Receiver's position is that the payroll payment by ADP partially discharged its obligation to pay employee claims under the Wage Earner Protection Program (the "WEPP").

[5] There are two[1] issues:

1. Did Mr. Healey triggering payment of the payroll after the Receiver was appointed amount to an implied affirmation by the Receiver of the agreement between Speedfast and ADP, with the result that the Receiver is obligated to pay ADP, and the amount at issue forms part of the Receiver's charge?

2. If not, does the rule in *Ex Parte James* apply, and should the Receiver nonetheless be required to make payment to ADP out of the funds in its hands, in priority to BMO?

[6] For the reasons that follow, the answer to both of these questions is "no".

The Background

[7] Under the agreement effective October 24, 2005 between ADP and Speedfast, ADP paid Speedfast's employees out of ADP's own funds, either by direct deposit into their respective bank accounts or by cheque issued by ADP. Speedfast agreed to maintain sufficient cleared funds in its bank account to cover the amount paid to its employees, and authorized ADP to debit Speedfast's account at BMO to fund payroll payments. The agreement required Speedfast to notify ADP if it would not have sufficient funds to satisfy its obligations to ADP and of any material adverse change in its financial position.

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[1] ADP specifically confirmed that contrary to what appears to be suggested in its factum it does not argue that it may assert the Speedfast employees' claims under section 81.4 of the *Bankruptcy and Insolvency Act* by subrogation. Nor does it advance a claim of unjust enrichment.

[8] The agreement provided that, "Upon notice, ADP may, in its discretion, modify the required funding method for Payment Services." ADP did not modify this funding method.

[9] ADP administers payrolls through its web-hosted payroll application. As part of the normal payroll processing activity, an employer's designated payroll contact(s) logs-in and inputs their payroll data, including employees' names, payroll amounts and bank account data. These changes are recorded by ADP and are presented to the employer in a payroll preview report.

[10] Once the employer has reviewed the payroll preview report, it then submits the payroll to "run" status. Once this occurs, debit instructions are sent by ADP to its bank, and to the employer's bank. Employees in turn are paid, either by direct deposit into their respective bank accounts or by cheque issued by ADP, as applicable.

[11] Speedfast designated one of its employees, Phillip Healey, as ADP's primary payroll contact. He was issued a unique digital certificate, a confidential user name and a password.

[12] Speedfast began experiencing financial difficulties. By August of 2008, it had retained the Receiver as a restructuring consultant. Speedfast did not advise ADP of its financial difficulties.

[13] On the morning of November 10, 2008, the Receiver was appointed by order of this Court (the "Order") pursuant to section 47(1) of the BIA and section 101 of the *Courts of Justice Act*, R.S.O. 1990 c. C. 43, in respect of Speedfast and three other related entities in the Grafikom group of companies. The materials filed in support of the receivership application' indicated Speedfast and the other respondents would be unable to pay their payrolls due on November 11, 2008. The Receiver's invoice suggests that the Receiver reviewed these materials, in draft, on November 8 or 9, 2008.

[14] The Order authorized the Receiver to operate Speedfast's business and incur obligations in the ordinary course of business. While the Order terminated the employment of all of Speedfast's employees, it also permitted the Receiver to engage persons to assist it. It further provided that all persons having agreements for the supply of goods or services with Speedfast, including without limitation payroll services, were restrained from terminating the supply of such services *as may be required by the receiver* [emphasis added], provided that the normal charges for all such services are paid by the Receiver.

[15] Pursuant to the Order, any expenditure or liability properly incurred by the Receiver forms a first charge on Speedfast's property, in priority to any other security interests or liens in favour of any person (the "Receiver's Charge").

[16] The Receiver took possession of Speedfast's Edmonton premises pursuant to the Order at about noon EST (10:00 a.m. (Alberta time)) on November 10, 2008. Speedfast had cancelled all shifts of hourly workers on November 7, 2008, in light of the intention of BMO to appoint a receiver and as a result only approximately ten salaried employees, including Mr. Healey, were present at the Edmonton premises. The Receiver advised the general manager, Mr. Barber, that the Order had been made and that the services of all employees

were terminated as a result of the receivership. At Mr. Barber's request, Mr. Barber communicated this information to the Speedfast employees who were present on an individual basis. The Receiver also communicated this information directly to the former employees on November 10, 2008.

[17] The Receiver learned that Mr. Healey was the individual at Speedfast who dealt with the Speedfast payroll between approximately noon and 1:00 p.m. EST (10:00 a.m. and 11:00 a.m. MT). It met with Mr. Healey at about 1:00 p.m. EST (11:00 a.m. MT) on November 10, 2008 and advised him of the receivership and that his employment was terminated as a result. Mr. Healey advised the Receiver that he was in the process of compiling the payroll information relating to the last payroll period ending November 9, 2008 for the hourly employees and November 14, 2008 for the salaried employees (the "Payroll Period"). The Receiver requested that Mr. Healey complete compilation of such information as it would be required for administration of the WEPP as well as for preparation of T4's and records of employment. Mr. Healey was advised that he would be paid by the Receiver as an independent consultant for this task on an hourly basis. The Receiver specifically advised Mr. Healey that payroll arrears for all of Speedfast's former employees were not being paid.

[18] Mr. Healey completed the requested initial calculation of wage and vacation pay arrears owing by Speedfast on November 10, 2008.

[19] At 2:07 p.m. EST (7 minutes past noon MT) Andrea Coros, who was based in Toronto and was the Company's senior payroll manager, sent an e-mail to Mr. Healey and to the respondents' other payroll administrators advising them that she "called ADP and advised that we are in receivership. ADP now requires more information before allowing the payrolls to go through and I will be working with them to provide that." The Receiver had retained Ms. Coros on a temporary basis to assist in coordinating the updating of payroll-related information.

[20] At 3:23 p.m. EST Ms. Coros left a voicemail message for Anna Sira, a client service representative at ADP, to call her.

[21] That afternoon, Mr. Healey accessed ADP's payroll application and submitted the Speedfast payroll to ADP for processing. Mr. Healey's electronic direction was received by ADP on November 10, 2008 at 3:48 p.m. EST.

[22] At 4:09 p.m. EST Ms. Sira returned Ms. Coros' call. ADP's case log summarizing the November 10 call as follows:

> Followed up with client on pending cases, client called back to advise that all of our company codes TOBU [the code for Speedfast], 7APA, COWO, COW1, 9AOY and 8 BPU are under receivership, they **may or may not be running payroll for the upcoming dates. Asked client to call me and let me know as majority of these company codes have run dates**

this week. Client will call back and provide information for the receivership as well. [emphasis added]

[23] ADP did not receive a follow-up call from Ms. Coros (or anyone else) asking ADP to stop running the payroll for Speedfast, or confirming that the Speedfast payroll was to be run.

[24] ADP understood that the Speedfast payroll was to proceed in the normal course, in accordance with Mr. Healey's electronic direction. Accordingly, on November 10, 2008 it directed its bank to debit from Speedfast's account at BMO (the "Pull") sufficient funds to cover Speedfast's payroll and at the same time directed ADP's bank to debit sufficient funds from ADP's account (the "Push") to pay the net wage obligations of Speedfast to its employees.

[25] As November 11, 2008 was a Bank Holiday, the Pull and Push occurred on November 12, 2008, the next business day.

[26] Ms. Daniel of ADP tried to reach Ms. Coros on the morning of November 12, 2009 to inquire with respect to the other respondents, which had failed to direct ADP to run their payrolls. Calls of this nature are made as a regular occurrence where a payroll is scheduled and a client has failed to direct ADP to run its payroll. Ms. Daniel finally reached Ms. Coros at approximately 2:00 p.m. At that time, Ms. Coros advised her that the respondents were in receivership and that their scheduled payrolls would not be running.

[27] By 2:00 p.m. it was too late for ADP to countermand the Push. The deadline was noon that day.

[28] Speedfast's employees were paid by ADP for the Payroll Period. The Payroll Period included the four-day period subsequent to the date of the Order.

[29] ADP spoke to the Receiver at approximately 4:00 p.m. on November 12, 2008 and the Receiver learned that ADP had processed the payroll. The Receiver indicated that it would not fund the payroll.

[30] The Receiver was not provided with and did not review contract documents governing the agreement between Speedfast and ADP before November 12, 2008. The Receiver's experience with ADP and other payroll service providers is that clients are contractually required to make funds available to the service provider in amounts that are sufficient to satisfy all of the client's payroll obligations by a set date and/or time that is prior to the client's scheduled pay date. It is further its experience that those funds are normally made available by the client to the service provider by direct debit from the client's bank account. Direct debit funds are not certified or guaranteed.

[31] On November 13, 2008, ADP advised the Receiver that it would be "changing the method of funding for all future payrolls" and that "funding of payrolls must be provided by wire transfer to ADP two days prior to any payroll being processed". This method is consistent with the Receiver's experience with ADP and other payroll service providers on other mandates.

[32] ADP did not fund the payrolls of the other respondents in the Grafikom Group which were the subject of the Order. The Receiver arranged to pay the priority claims of those employees up to $2,000 under the BIA. Had ADP not paid the Speedfast employees, the Receiver would have paid them as well, to the extent required by the WEPP.

[33] The Receiver retained Mr. Healey as a consultant again on December 2, 2008 for a few hours to confirm earlier calculations and to quantify accrued vacation pay owing to the employees.

[34] Mr. Healey submitted an invoice as an independent consultant for the services he was retained to provide on November 10 and December 2, 2008 and was paid for such services.

Issue 1: Is the Receiver liable to fund the payroll?

The Parties' Positions

[35] BMO argues that the Order terminated all of the employees, the Receiver did not in fact operate the business of Speedfast, Mr. Healey was an independent contractor of the Receiver and ADP has not established that Mr. Healey was operating under the direction of the Receiver in making the direction to ADP.

[36] BMO points to *671122 Ontario Ltd. v. Sagaz Industries Canada Inc.*, [2001] 2 S.C.R. 983, as clearly establishing that, subject to limited exceptions, the actions of an independent contractor do not give rise to vicarious liability of the party who retained the independent consultant. It submits, by analogy[2], that a Court-appointed receiver, and by extension the receivership estate, should not be held accountable for the actions of an independent consultant retained by the receiver where the consultant's actions were: (i) done without the receiver's knowledge, direction or authority; (ii) outside the terms of the independent contractor's retainer; and (iii) contrary to the receiver's advice to the independent consultant.

[37] ADP argues that the Receiver had control over the business and premises of Speedfast and it is bound by Mr. Healey's act in causing ADP to initiate the process of running the payroll. It submits, relying on *Bennett on Receiverships*, 2d ed., (Toronto: Carswell, 1999), at p. 376 and *Gresmak v. Yellowhead Town &Country Inn* (1989), 77 C.B.R. (N.S.) 245 (B.C. Co. Ct.), that while a court-appointed receiver is entitled to terminate the employment of the employees of the debtor, if it chooses to carry on the business of the debtor, and uses the employees of the debtor, then those employees become the receiver's employees.

[38] ADP argues Mr. Healey became an employee, and not an independent consultant, of the Receiver, and as such the Receiver is responsible for his conduct. ADP submits that a consideration of the factors in *Sagaz* for determining whether or not someone is an employee or an independent consultant indicates that Mr. Healey was an employee of the Receiver.

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[2] As noted in *Sagaz*, at para. 2, "Vicarious liability describes the event when the law holds one person responsible for the misconduct of another because of their relationship." It has not been alleged that Mr. Healey committed a tort. Misconduct on the part of Mr. Healey has not been established. This case is not about vicarious liability; hence, the analogy.

ADP submits that the references in the Receiver's accounts to "key employee retention agreements" and "paying employees retained by the Receiver" are also evidence that Mr. Healey was an employee. ADP submits that the fact that the Receiver paid the tax liabilities to Canada Revenue Agency ("CRA") resulting from the payroll payments triggered by Mr. Healey is evidence that the Receiver had ratified the agreement.

Analysis

[39] The Receiver's First Report indicates that while, at the date of the Order, all operations had ceased, the Receiver recommenced operations on a limited basis. By way of example, it negotiated the continuation of services with certain suppliers and completed certain work-in-progress.

[40] In *Re Pope & Talbot Ltd.* (2009), 50 C.B.R. (5th) 99 (B.C. S.C.), Brenner C.J.S.C. recently considered whether a court-appointed receiver was required to pay contractual standby charges. The receivership order in that case contained the same language as in the Order: suppliers were required to continue their contractual obligations to supply services "as may be required by the receiver". Framed in the alternative, the issue in this case is whether the Receiver required ADP to pay the payroll.

[41] Brenner C.J.S.C. noted, referring to *Re New Skeena Forest Products Inc.*, 251 D.L.R. (4th) 328 (B.C.C.A.), that it is well settled law that, in the absence of an affirmation, express or implied, a court-appointed receiver is not bound by existing contracts made by the debtor.[3]

[42] In *Re Pope*, the receivership order did not authorize the receiver to operate the business of the debtor. The contract at issue was for the supply of natural gas, and, as the mills were not being operated, no natural gas was supplied. The supplier sent invoices for the standby charges payable under the contract and the receiver did not reply. Brenner C.J.S.C. noted that typically, after a receiver is appointed, it assesses the contracts under which goods or services are supplied and decides which ones it wishes to continue. That decision, he commented, is usually prompted by a post-appointment delivery of goods or services. He held that, in the case before him, because no services were being provided, the receiver's silence did not amount to implied affirmation of the contract. He concluded that where no actual services were being supplied, the receiver is not under an obligation to affirm or disclaim the contract until required to do so.

[43] The parties indicated that they were unable to find any cases considering the principles of agency law in a receivership context for my assistance, and they did not argue general principles of agency law. In any event, I note that Mr. Healey had been designated as ADP's primary payroll contact by Speedfast, not by the Receiver.

[44] This case is very different from *Re Pope*. Here, the specific issue before me is whether the electronic direction of Mr. Healey, (i) done without the receiver's knowledge, direction or authority; (ii) outside the terms of the Mr. Healey's retainer; and (iii) contrary to

[3] This principle has been applied in *Royal Bank of Canada v. Penex Metropolis Ltd.*, [2009] O.J. No. 3645 (S.C.J.) at para. 23

the Receiver's advice to Mr. Healey that payroll arrears were not being paid, *on the very day the Receiver was appointed*, amounts to an affirmation of the agreement between Speedfast and ADP. In my view, it does not. This is particularly so, given Ms. Coros' communications with ADP.

[45] I come to this conclusion whether or not Mr. Healey might be found to have been an employee, and not an independent contractor, of the Receiver on the only two days - November 10, 2008 and December 2, 2008 - when he was retained to perform specific tasks at an hourly rate. (That being said, the very short-term and specific nature of Mr. Healey's hourly retainer persuades me that he was an independent contractor. While counsel for ADP correctly notes that the Supreme Court in *Sagaz* did not specifically point to the duration of the arrangement as a factor to be considered in determining whether a person is an employee or an independent contractor, the Supreme Court did note, at para. 47, that the factors it cited as relevant in determining whether or not a person was performing services as a person in business on his own account (and was therefore an independent contractor) were non-exhaustive, and there was no set formula as to their application. The references to "employees" ADP relies on in the Receiver's accounts are not persuasive: in context, they do not specifically or impliedly relate to Mr. Healey, and the Receiver's report specifically indicates that Mr. Healey was an independent contractor. The principle in *Bennett on Receiverships* and *Gresmak v. Yellowhead Town & Country Inn* that ADP relies on can, I believe, be displaced where, as here, the receiver and the former employee of the debtor specifically agreed to an hourly consulting arrangement consistent with an independent contractor relationship.)

[46] Payment of liabilities to CRA arising from the payroll triggered by Mr. Healey did not in my view constitute ratification of the agreement between ADP and Speedfast.

[47] Concerns regarding a receiver's liability in operating receiverships that have arisen out of jurisprudence have impacted on insolvency proceedings. Some receivers are reluctant to undertake them. This presumably has resulted in increased costs. It has also resulted in parties straining to obtain court approval of transactions in the course of insolvencies outside of receiverships. A decision imposing liability on a receiver on the facts of this case would in my view have a chilling impact on receivership proceedings.

Issue 2: The rule in Ex Parte James

[48] Under s. 81.4 of the BIA, which came into force on July 7, 2008, claims for wages rank as priority secured claims against current assets of the employer in the possession or control of the receiver to extent of $2,000. Pursuant to s. 81.4(5), when the Receiver took possession of Speedfast's current assets, it became liable for those claims, to the extent of the amount realized on the current assets. Sections 81.4(1), (3), (4) and (5) are set out in Schedule 1 to these Reasons.

[49] As noted above, it is not disputed that if ADP had not paid Speedfast's employees, the Receiver would have been required to do so out of Speedfast's current assets, as it did with respect to the employees of the other respondents in the Grafikom group, to the extent of $2,000 per employee, pursuant to s. 81.4 of the BIA. It is also not disputed that the

Receiver did not expect or intend ADP to pay the payroll, and in fact intended to make the payments under the BIA. The amounts available for distribution to BMO, as Speedfast's first secured creditor, would have been reduced accordingly.

[50] ADP argues that it is not fair for the Receiver to permit BMO to profit in this manner, and that, relying on the principle in *Ex Parte James, Re Condon* (1874), L.R. 9 Ch. App., as extended and applied by subsequent decisions, referred to below, the court should require the Receiver, an officer of the court, to do the high-minded thing and pay ADP's invoice even if it is not legally required to do so. ADP argues that the fact that the "windfall" has arisen as a result of someone ADP argues is an employee of the Receiver weighs in favour of the application of the rule in *Ex Parte James*.

[51] BMO argues that the principle in *Ex Parte James* is not applicable in this case because ADP is not an innocent or aggrieved party and there is no unusual hardship for the court to alleviate, as the funding of the payroll by ADP was due to ADP's: (a) acceptance of commercial risk by funding payroll without verification that Speedfast was in funds; and (b) failure to rescind the Push following Ms. Coros' call on November 10, 2008.

[52] Counsel for ADP refers me to the early cases establishing the rule in *Ex Parte James*, and several cases in which it has been applied to afford relief, in support of its argument that the rule should be applied in this case.

[53] In *Ex Parte James*, money was voluntarily paid to a trustee in bankruptcy by an execution creditor under mistake of law. While, at law, money paid under mistake of law could not be recovered, the court held that a trustee of bankruptcy, as an officer of the court, ought to set an example. It ordered the trustee in bankruptcy to pay the money to the person really entitled to it.

[54] In *Ex Parte Simmonds* (1885), 16 Q.B.D. 308 at 312, the court, in ordering the repayment of money paid to a trustee in bankruptcy under mistake of law, explained the rationale for the rule in *Ex Parte James*: "although the Court will not prevent a litigant party from acting in this way, it will not act so itself, and it will not allow its own officer to act so."

[55] A subsequent decision, *Re Tyler, Ex p. Official Receiver*, [1907] 1 K.B. 865 held that the rule in *Ex Parte James* was a rule of general application, and not restricted to money paid under mistake of law. The court described the rule as a "prerogative of mercy reposing in the court to alleviate cases of unusual hardship in which a regard to the strict legal or equitable rights only would work a manifest injustice....". There, the bankrupt had assigned an insurance policy on his own life as security. The wife of the bankrupt paid one premium on the bankrupt's life insurance policy before the commencement of the bankruptcy, and continued to pay the premiums on the insurance policy during the life of the bankrupt. The court, applying the principle in *Ex Parte James*, ordered the trustee to repay the premiums paid by the wife.

[56] In *Re Thellusson*, [1919] 2 K.B. 735 at 746 (C.A.), a receiving order was made against a debtor without his knowledge. The next day, before becoming aware of the receiving order, the debtor borrowed money. The creditor was similarly unaware of the

receiving order. Applying the rule in *Ex Parte James*, the court ordered the trustee in bankruptcy to repay the creditor the money loaned to the bankrupt debtor.

[57] In *Re MacDonald*, [1972] 1 O.R. 363 (H.C.J.), the bankrupt died owing $1.00 under his conditional discharge order. Approximately seven months before his death, he had sent two cheques sufficient to pay the amounts due to the trustee. One of the cheques was dated, and was cashed by the trustee. The second cheque, for the sum of $1.00, was undated and sent under cover of a letter from the bankrupt indicating that it could be applied, "at any other time". The bankrupt did this because of concerns about having a final notice of discharge published. Houlden J. concluded that it was an appropriate case to apply the rule in *Ex Parte James* and exercise the "prerogative of mercy". He ordered the trustee in bankruptcy to pay the life insurance proceeds to the bankrupt's executor.

[58] In *Re Springer and Higgins Co. Ltd.* (1979), 24 O.R. (2d) 411(Div. Ct.) the rule in *Ex Parte James* was applied to a liquidator appointed under the *Business Corporations Act*, R.S.O. 1970, c. 53. There, a liquidator agreed, with the consent of the company's four shareholders, to pay a commission on the sale of land owned by the company. One of the shareholders subsequently objected to the payment, on the basis that the commission was not permitted by applicable legislation. While the payment was indeed not permitted by applicable legislation, the court ordered the liquidator to do "the high minded thing" and pay it.

[59] Counsel for BMO refers me to the discussion of the rule in *Ex Parte James* in L.W. Houlden, G.B. Morawetz & J.P. Sarra, *The 2009 Annotated Bankruptcy and Insolvency Act* (Toronto: Thomson Carswell, 2008) ("Houlden & Morawetz"). At para. F31, Houlden & Morawetz indicates, citing a number of cases, some of which I refer to below, that three conditions must be met for the rule to apply in a bankruptcy context: (1) the bankrupt estate must be enriched or could be enriched at the expense of the person making the claim; (2) in most cases, the claimant must not be in a position to file a proof of claim in the bankruptcy; and (3) to allow the trustee to retain the enrichment would be unfair and unjust. Houlden & Morawetz also indicates that when the rule does apply, it applies only to the extent necessary to nullify the enrichment of the bankrupt estate and does not necessarily restore the claimant to the *status quo* ante.

[60] The above principles were summarized by Walton J. in *Re Clark (A Bankrupt); Ex p. Trustee v. Texaco Ltd.*, [1975] 1 W.L.R. 559 at pp. 563-564, which was cited with approval by the Court of Appeal in *Re Appleby Estates Ltd.*, [1984] O.J. No. 3337.

[61] With respect to the second condition, Walton J. commented, in *Re Clark*, "The rule is not to be used merely to confer a preference on an otherwise unsecured creditor, but to provide relief for a person who would otherwise be without any." In *Re Gozzett*, [1936] 1 All E.R. 79, 80 Sol. Jo. 146 (C.A.) the court declined to apply the rule in *Ex Parte James* because the parties seeking relief, "were simply unsecured creditors and their position was due to their failure to take the precautions of securing any sort of charge on the property." *Park City Products Ltd.* (2001), 27 C.B.R. (4th) 314 (Man. Q.B.); affirmed (2002), 33 C.B.R. (4th) 79 (Man. Q.B.) indicates that the logic for not applying the rule in *Ex Parte James* if the applicant is in a position to file a proof of claim is that the application of the rule would

conflict with the mandatory *pari passu* division of the bankrupt estate among the creditors as required by the BIA.[4]

[62] BMO also referred me to three cases, which I will refer to as the "payroll cases" - one from each of Ontario, British Columbia and Quebec - where the courts have refused to grant recovery to payroll service providers against corporate directors where the payroll service provider directly funded payroll to its client employees under the terms of a contract and was unable to recover the amount of the payroll from the employers' bank account. In these cases, which predate the enactment of s. 81.4 of the BIA, the claims were made against corporate directors, and not against a receiver or other officer of the court. Moreover, in these cases the action triggering the payment of payroll was taken before a receiver or trustee in bankruptcy was appointed.

[63] In *Canadian-Automatic Data Processing Services Ltd. v. CEEI Safety & Security Inc.* (2004), 2004 Carswell Ont. 4993 (C.A.) ("*CEEI Safety*") the employer breached its agreement with the payroll service provider by having insufficient funds in its account to cover the payroll. The payroll service provider sued a director of the employer, claiming unjust enrichment, and, in the alternative, that it was subrogated to the employees' rights against the directors under s. 131 of the Ontario *Business Corporations Act*, R.S.O. 1990, c. B.16 (the "OBCA").

[64] The Court of Appeal held that the payroll service provider's claim for unjust enrichment failed because the director did not receive a benefit. A director's liability to pay the employees' wages under the OBCA arises only when the corporation defaults on its primary contractual wage obligation to pay it employees' wages. In paying the employees, the payroll service provider was fulfilling the obligation of the corporate employer, and not an obligation of its director. As the employees were paid, they had no claim against the director and the director had no statutory obligation. The director therefore was not directly enriched when the payroll supplier discharged; the corporate employer was. The secondary collateral benefit the director received, incidental to that of the corporate employer, was incapable of supporting a claim for unjust enrichment.

[65] As to the subrogation claim, as factually ADP did not pay a debt owing by the director to ADP's employees, it could not be subrogated to the corporate employer or the employees as neither had a claim against the payroll supplier. The Court of Appeal also commented that recovery against the director should be denied on public policy grounds as it would extend protection intended for employees, who are uniquely vulnerable, to a creditor who could have, and failed to, avail itself of alternative commercial mechanisms that would have afforded it greater protection. (It could, the court noted, have required the employer to pay by prefunded certified cheque or wire transfer.)

[66] In *Canadian-Automatic Data Processing Services Ltd. v. Syntecor Ltd.* (2004), 2004 Carswell BC 1710 (C.A.) ("*Syntecor*") the payroll supplier also unsuccessfully advanced a claim of unjust enrichment against a director, although in this case the claims were made after the employer had filed an assignment in bankruptcy, and the obligation of the director

[4] This case is referred to in the loose leaf version of Houlden & Morawetz.

relied upon by the payroll supplier was the British Columbia *Employment Standards Act*. The British Columbia Court of Appeal concluded, as the Ontario Court of Appeal subsequently did in *CEEI Safety*, that a benefit had not been conferred on the director, and that even if one had, there was juristic reason to deny the payroll supplier's claim. The claim was a novel one and not within the reasonable expectation of the payroll supplier or the director it sued. Moreover, public policy grounds (those adopted in *CEEI Safety* and referred to above) provided a strong reason to deny the payroll supplier's claim. It noted, "ADP's loss was a foreseeable commercial risk, recognized in the contract."

[67] In *Ceridian Canada Ltd. v. Labreque* (2008), 2008 Carswell Que. 10388 (S.C.) ("*Ceridian*"), the payroll supplier processed the payroll at 12:00 a.m. on the same day that the corporate supplier filed an assignment in bankruptcy. The payroll supplier's claims of unjust enrichment and subrogation under the *Canada Business Corporations Act*, R.S., 1985, c. C-44 against the directors failed for essentially the same reasons as articulated in *CEEI Safety*. Claims advanced by the payroll supplier on a number of other bases similarly failed. The court expressed the view that the payroll supplier suffered its loss as a result of its own negligence and its failure to use the provisions of its standard form payroll service agreement to its own benefit.

[68] Neither party has provided a case to me where the rule in *Ex Parte James* was applied to a court-appointed receiver. It is clear, however, that a court appointed receiver is an officer of the court. The rule, therefore, can apply.

[69] In this case, the Receiver was clearly enriched at the expense of ADP. At the time of its appointment, the Receiver knew the payroll had not been paid, intended that it not be paid and intended to instead pay the employees' priority claims under the BIA. Upon its appointment the Receiver obtained, and therefore had at the time that ADP made the payment, possession of Speedfast's current assets and was directly and primarily liable for the employees' claims under s. 181.4 of the BIA. But for ADP's payment, the Receiver would have been required to pay those priority claims. The Receiver's position is different from that of the directors against whom payroll suppliers' claims of unjust enrichment failed in the payroll cases.

[70] While the Receiver was enriched at the expense of ADP when ADP paid the payroll, ADP is in a position to file a claim as an unsecured creditor. Moreover, in my view, it would not be unfair and unjust to permit the Receiver to retain the enrichment, which will ultimately flow to a secured creditor. As highlighted in the payroll cases, because ADP chose not to take security for its payroll advances, or to ensure that it was in funds from Speedfast before it issued the payroll, its loss was a foreseeable commercial risk. Having regard to the payroll cases, ADP was very clearly aware of the risk of continuing to structure its affairs in the manner it did. While ADP acted in good faith on the direction of the person from whom Speedfast had told it to accept directions, having regard to its commercial risk one would expect that upon hearing that Speedfast was in receivership it would have immediately contacted the Receiver to ensure that the payroll was funded. The Receiver's website was operational by November 10, 2008. The failure to take precautions and obtain security was recognized in *Re Gozzett* as a reason for declining to apply the rule in *Ex Parte James*. The logic in *Re Clark* and *Re Gozzett* is even more compelling in the era of the *Personal Property*

Security Act, R.S.O. 1990, c. P.10. It seems to me that, in the interests of commercial certainty, the court should be reluctant to apply the principle in *Ex Parte James* when to do so would effectively alter the priorities between unsecured and secured creditors.

[71] In the result, I conclude that the rule in *Ex Parte James* should not be applied in this case.

[72] Given that the payroll direction to ADP was (i) done without the Receiver's knowledge, direction or authority; (ii) outside the terms of the Mr. Healey's retainer; and (iii) contrary to the Receiver's advice to Mr. Healey that payroll arrears were not being paid, my conclusion would have been the same, even if I had concluded that Mr. Healey was an employee of the Receiver at the time he triggered the payroll.

Costs

[73] If the parties are unable to agree on costs, BMO shall provide brief written submissions to me within 14 days, and ADP shall provide brief written submissions within 10 days thereafter. There shall be no reply submissions without leave.

Hoy J.

Released: October 14, 2009

SCHEDULE 1

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

Security for unpaid wages, etc. — receivership

81.4 (1) The claim of a clerk, servant, travelling salesperson, labourer or worker who is owed wages, salaries, commissions or compensation by a person who is subject to a receivership for services rendered during the six months before the first day on which there was a receiver in relation to the person is secured, as of that day, to the extent of $2,000 — less any amount paid for those services by a receiver or trustee — by security on the person's current assets that are in the possession or under the control of the receiver.

. . .

Security for disbursements

(3) The claim of a travelling salesperson who is owed money by a person who is subject to a receivership for disbursements properly incurred in and about the person's business during the six months before the first day on which there was a receiver in relation to the person is secured, as of that day, to the extent of $1,000 — less any amount paid for those disbursements by a receiver or trustee — by security on the person's current assets that are in the possession or under the control of the receiver.

Rank of security

(4) A security under this section ranks above every other claim, right, charge or security against the person's current assets — regardless of when that other claim, right, charge or security arose — except rights under sections 81.1 and 81.2.

Liability of receiver

(5) If the receiver takes possession or in any way disposes of current assets covered by the security, the receiver is liable for the claim of the clerk, servant, travelling salesperson, labourer or worker to the extent of the amount realized on the disposition of the current assets and is subrogated in and to all rights of the clerk, servant, travelling salesperson, labourer or worker in respect of the amounts paid to that person

COURT FILE NO.: 08-CL-7840
DATE: 20091014

IN THE MATTER OF an Application under section 47(1) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, as amended

AND IN THE MATTER OF Section 101 of the *Courts of Justice Act*, R.S.O. 1990, c.43, as amended

ONTARIO

SUPERIOR COURT OF JUSTICE

B E T W E E N:

THE BANK OF MONTREAL, as agent for BANK OF MONTREAL, THE BANK OF NOVA SCOTIA and ALBERTA TREASURY BRANCHES

- and -

GRAFIKOM LIMITED PARTNERSHIP, GRAFIKOM GENERAL PARTNER INC., GRAFIKOM SPEEDFAST LIMITED and GRAFIKOM GRENVILLE LIMITED

REASONS FOR DECISION

Hoy J.

Released: October 14, 2009